

February 2010

RECOVERY ACT

IRS Quickly Implemented Tax Provisions, but Reporting and Enforcement Improvements Are Needed



GAO

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Highlights of [GAO-10-349](#), a report to congressional addressees

Why GAO Did This Study

The American Recovery and Reinvestment Act of 2009 (Recovery Act), was enacted to bolster the struggling U.S. economy at an estimated cost of \$787 billion, of which more than a third was in the form of tax relief to the public.

This report (1) describes the status of the Internal Revenue Service’s (IRS) implementation of Recovery Act tax provisions; (2) examines whether IRS captured or planned to capture data on the use of the provisions; (3) assesses IRS’s efforts to determine potential abuse of the provisions; and (4) discusses possible lessons learned for future tax administration. GAO analyzed IRS’s implementation and data-collection plans for each provision; reviewed IRS and Department of the Treasury (Treasury) risk-management documents; interviewed federal and industry officials; and focused on five provisions implemented in 2009: Build America Bonds (BAB), Consolidated Omnibus Budget Reconciliation Act (COBRA), First-Time Homebuyer Credit (FTHBC), Making Work Pay Credit, and Net Operating Loss carrybacks.

What GAO Recommends

GAO suggests that the Congress consider (1) authorizing IRS to publish more BAB information and (2) granting IRS broader authority to correct errors during tax-return processing. GAO also recommends IRS obtain more information on BABs, enhance compliance with the COBRA provision, and prepare a report on Recovery Act lessons learned.

View [GAO-10-349](#) or [key components](#). For more information, contact Michael Brostek at (202) 512-9110 or brostekm@gao.gov.

RECOVERY ACT

IRS Quickly Implemented Tax Provisions, but Reporting and Enforcement Improvements Are Needed

What GAO Found

IRS Quickly Addressed the Act’s Significant Implementation Challenges

The Recovery Act posed significant implementation challenges for IRS because it had more than 50 provisions, many of which were immediately or retroactively available and had to be implemented during the tax filing season—IRS’s busiest time. Some provisions affected the 2009 filing season (2008 tax year), while others mainly will affect the 2010 and 2011 filing seasons. IRS responded quickly to its challenges. For instance, within about 6 months of the Recovery Act’s enactment, IRS had issued guidance or instructions for more than 80 percent of the provisions.

Categorization	Number of provisions	Value of provisions (dollars in billions)
Individual credits	12	\$247
Bond incentives	14	27
Consolidated Omnibus Budget Reconciliation Act	1	25
Energy incentives	14	20
Business incentives	11	6
Health coverage improvement	1	0 ^a
Withholding on government contractors	1	0 ^a
Total	54	\$325^b

Source: GAO analysis of IRS and Joint Committee on Taxation data.

^aThe actual value is nonzero but is rounded down to zero.

^bThis dollar total differs from the \$288 billion used by the administration and posted on recovery.gov; it includes COBRA premium subsidies and economic recovery payments, because IRS is involved in administering them.

However, responding quickly entailed tradeoffs, such as not making some computer changes to collect data, and subsequent improvements were required. For example, because of the compressed time to implement the 2009 FTHBC, IRS did not make computer changes to collect data, including the home purchase date. Without such information, IRS was unable to easily distinguish 2008 and 2009 FTHBCs. Distinguishing between the two credits is critical because they involve different requirements, including whether and how the credit is to be repaid. IRS plans to verify the date of purchase on past claims and make any necessary adjustments when it begins enforcing 2008 FTHBC repayment provisions. IRS also plans to make the computer changes needed to collect all significant data, including the home purchase date, from a revised form for 2009 claims.

IRS’s Data-Collection Efforts Have Limitations

IRS went beyond its typical data-collection efforts and plans to collect some data to track many Recovery Act provisions. Specifically, IRS currently has detailed data-collection plans for 17 or about 31 percent of the provisions

and 63 percent of the total estimated cost of the tax provisions. Initial collections did not fully or accurately capture the use of some provisions. In addition, very little of the data that IRS has collected on the tax provisions has been released publicly.

As one example of limited data, neither IRS nor any other federal agency is collecting for publication the sort of information on BABs that the Congress required for the act's spending projects. BAB projects can be very similar to those funded by Recovery Act spending projects, but the same transparency and accountability do not apply. If IRS were to collect such information, then it would need the Congress to grant it the authority to publish the information. State and local governments may issue an unlimited number of BABs through December 31, 2010, and all BAB proceeds must be used for qualified capital expenditures. As of January 1, 2010, state and local governments reported 443 BABs, which raised about \$32.4 billion. One hundred and thirty-one BABs were issued for education, which were more issuances than for any other specified type of BAB.

As another example, COBRA data will understate the number of individuals receiving health insurance. For instance, if COBRA premium assistance was paid for a former employee, his or her spouse, and one child, an employer would count that as one person provided assistance. According to IRS officials, the relevant form did not include dependents due to a short implementation time frame, space constraints on the form, and a desire not to overburden employers with additional reporting requirements.

Provisions' Economic Stimulus Effect Cannot Be Precisely Isolated

Similar to what GAO has found about the act's spending projects, the tax provisions' economic stimulus effect cannot be precisely isolated. Economists use evidence from macroeconomic forecasting models and models that extrapolate from historical data to assess stimulus effects. These approaches, however, are imprecise because historical experience may not apply well given the magnitude of the Recovery Act. The effect of some provisions on specific aspects of the economy may be described in general terms. For example, the Council of Economic Advisers noted that in addition to other policy actions affecting residential real estate, the FTHBC may have moderated construction-industry job losses.

IRS Took Steps to Mitigate Abuse of Provisions, but Some Compliance Challenges Arose and Others Remain

As a result of IRS's FTHBC preresult compliance reviews, as of February 1, 2010, IRS had frozen about 140,000 refunds pending civil or criminal examination, and, as of December 2, 2009, had identified 175 criminal

schemes and had 123 criminal investigations open. Although IRS addressed some challenges with the FTHBC in these ways, it still needs to finalize a way to identify individuals who fail to report home sales and might be required to repay part of the credit because their homes ceased to be their principal places of residence within 3 years of purchase. A form already exists that could be used for this purpose—Form 1099-S, "Proceeds from Real Estate Transactions," but it is not clear IRS could use the form for this purpose under current legislative authority. As GAO's review ended, IRS identified third-party data that it expected to use and then evaluate the results.

Similarly, IRS had not finalized actions to ensure that employers stop claiming the credit for COBRA premium subsidies when former employees are no longer eligible. A cost-effective option to help IRS with unresolved compliance issues exists—expanding a planned project to determine if employers are claiming the subsidies for longer than allowed. If they are, IRS could send all employers letters reminding them of their obligations and urging them to correct any errors they have made.

Documenting IRS's Recovery Act Lessons Learned and Expanding Its Authority, with Appropriate Controls, Could Improve Future Tax Administration

Issues IRS encountered in its Recovery Act experience could provide useful guidance for the future. Officials intend to do a lessons-learned study after the 2010 filing season but have yet to develop plans for doing so.

In addition, IRS and taxpayers would have benefited if IRS had more statutory "math error authority" (MEA) to correct errors during tax-return processing when the Recovery Act was first implemented, rather than only after problems were identified. Authorizing such authority on a broader basis rather than case-by-case, with appropriate controls, could have several benefits to IRS and taxpayers; for example, it is an automated and low-cost means to protect revenue and avoid audits that are costly to IRS and burdensome to taxpayers.

Agency Comments

The Commissioner of Internal Revenue agreed fully with two recommendations and agreed with the benefit of the third. He noted that the benefit of more BAB information would have to be balanced with the burden on BAB issuers but said IRS stood ready to implement the recommendation if the Congress authorized publication of the data. GAO believes this burden could be tempered by having a minimum reporting threshold or delaying the onset of requirements, as was done when similar reporting for charitable organizations was instituted. He also said that in those cases in which more MEA could be effectively deployed, IRS would welcome it.

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Abbreviations

AEITC	Advance Earned Income Tax Credit
AGI	adjusted gross income
AMT	alternative minimum tax
BAB	Build America Bond
CBO	Congressional Budget Office
CEA	Council of Economic Advisers
COBRA	Consolidated Omnibus Budget Reconciliation Act
FMS	Financial Management Service
FTHBC	First-Time Homebuyer Credit
GDP	gross domestic product
HCTC	Health Coverage Tax Credit
IRA	individual retirement account
IRS	Internal Revenue Service
JCT	Joint Committee on Taxation
MAGI	modified adjusted gross income
MEA	math error authority
MWPC	Making Work Pay Credit
NOL	Net Operating Loss
PBGC	Pension Benefit Guaranty Corporation
SB/SE	Small Business/Self-Employed
TAA	Trade Adjustment Assistance
TIGTA	Treasury Inspector General for Tax Administration
Treasury	Department of the Treasury
WOTC	Work Opportunity Tax Credit

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United States Government Accountability Office
Washington, DC 20548

February 10, 2010

Congressional Addressees

The American Recovery and Reinvestment Act of 2009 (Recovery Act) is an estimated \$787 billion initiative intended to address the most serious economic crisis since the Great Depression.¹ Although the Recovery Act primarily consists of new funding for programs and other investments designed to stimulate the economy, more than a third of the act consists of tax relief to the American public. The Recovery Act calls for unprecedented levels of transparency and accountability in how Recovery Act dollars are being spent, but information on the tax provisions is generally not included in mandatory Recovery Act reporting. We raised the issue of providing similar oversight of the tax provisions in previous testimony.² GAO reports and testimonies on the Recovery Act are available at www.gao.gov/recovery.

As part of an effort to provide the Congress and others with relevant oversight information on the tax provisions in the Recovery Act, we performed this review under the Comptroller General's authority to conduct evaluations. Our objectives were to (1) describe the status of the Internal Revenue Service's (IRS) implementation of Recovery Act tax provisions; (2) analyze IRS's plans to collect data on the provisions, examine whether and how IRS captured data on the use of selected provisions, and discuss the provisions' overall effect; (3) assess IRS's efforts to determine potential abuse of the provisions and IRS's steps for minimizing it; and (4) discuss possible lessons learned for future tax administration. To meet our objectives, we obtained and analyzed IRS's implementation and data-collection plans for each provision; reviewed IRS, Department of the Treasury (Treasury), and Treasury Inspector General for Tax Administration (TIGTA) planning, implementation, risk management, and other documents; and interviewed federal officials and industry representatives.

We reviewed IRS's plans and actions for 54 provisions that it had a role in administering. Of these, we focused our analysis on five provisions—Build

¹Pub. L. No. 111-5, 123 Stat. 115 (Feb. 17, 2009).

²GAO, *American Recovery and Reinvestment Act: GAO's Role in Helping to Ensure Accountability and Transparency*, [GAO-09-453T](#) (Washington, D.C.: Mar. 5, 2009).

America Bonds (BAB), Consolidated Omnibus Budget Reconciliation Act (COBRA) premium subsidies, the First-Time Homebuyer Credit (FTHBC), the Making Work Pay Credit (MWPC), and net operating loss (NOL) carrybacks. We selected these provisions because they were all being implemented in 2009; included some that were among the largest in terms of estimated revenue loss; most were refundable, meaning that taxpayers may receive a tax refund even if they do not have any tax liability; and covered most of IRS's categories of Recovery Act provisions.³ We also reviewed a sixth provision—the Health Coverage Tax Credit (HCTC)—but limited our work to data-collection issues because we are doing a separate review of the HCTC, which is due in March 2010 as mandated by the Recovery Act. See the Background section or appendix I for a description of the provisions we reviewed. See appendix II for a full description of our scope and methodology.

We conducted this performance audit from June 2009 through February 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives and found the IRS data we used reliable for the purposes of this report.

Background

IRS received approximately \$197 million to implement 54 Recovery Act provisions.⁴ The Joint Committee on Taxation (JCT) estimated that these 54 provisions would cost about \$325 billion between fiscal year 2009 and fiscal year 2019. (App. III shows the estimated cost of each provision.) JCT's estimate can be reconciled with the Congressional Budget Office's (CBO) estimate of \$212 billion in reduced revenue and the administration's \$288 billion in tax relief shown on its Recovery Act Web site, recovery.gov.⁵ JCT's estimate includes the effect on the budget of provisions of the act administered through the tax code, but CBO's \$212

³See fig. 1 for a categorization of the tax provisions that IRS had a role in administering.

⁴As of January 29, 2010, IRS had obligated about \$121 million of the \$197 million for Recovery Act administrative expenses, with the majority of the money thus far used for HCTC.

⁵Recovery.gov is the official government Web site to help taxpayers track how Recovery Act money is being spent.

billion estimate, which is based on JCT's estimate, includes only the effect on revenue collections. The primary difference is that CBO's estimate does not include some provisions that result in additional federal outlays rather than only reduced tax collections. This occurs under several provisions when taxpayers can receive a refund even if they do not have any tax liability. On recovery.gov, the administration includes both categories to arrive at its estimate of \$288 billion in tax relief. The JCT estimate of \$325 billion also includes the cost of COBRA and economic recovery payments provisions that IRS administers.

IRS had a role in administering 54 Recovery Act provisions. However, IRS is not responsible for implementing all provisions included in the tax section of the Recovery Act, such as grants in lieu of credits and the New Markets Tax Credit. Grants were authorized because the effectiveness of particular credits was thought to be undermined by economic conditions; the grant provisions are administered elsewhere in Treasury. In a recent report, TIGTA's count of Recovery Act provisions also differed from ours; for example, it included the New Markets Tax Credit, which is being administered by Treasury's Community Development Financial Institutions Fund.⁶

To facilitate management of the provisions, as shown in figure 1, IRS grouped the provisions into six categories, with individual credits as the largest category by far in terms of dollars. A seventh category, withholding on government contractors, appears in the figure because it is being administered by IRS; however, IRS did not consider it to be a category because the Recovery Act only delayed the effective date for the withholding.

⁶TIGTA, *Recovery Act: Evaluation of the Internal Revenue Service's Capability to Ensure Proper Use of Recovery Act Funds* (Washington, D.C., Nov. 27, 2009).

Figure 1: Categorization of the Tax Provisions That IRS Had a Role in Administering, with Number and Dollar Value of Provisions

IRS categorization	Number of provisions	Value of provisions (dollars in billions)
Individual credits	12	\$247
Bond incentives	14	27
Consolidated Omnibus Budget Reconciliation Act	1	25
Energy incentives	14	20
Business incentives	11	6
Health coverage improvement	1	0 ^a
Withholding on government contractors	1	0 ^a
	Total=54	Total=\$325^b

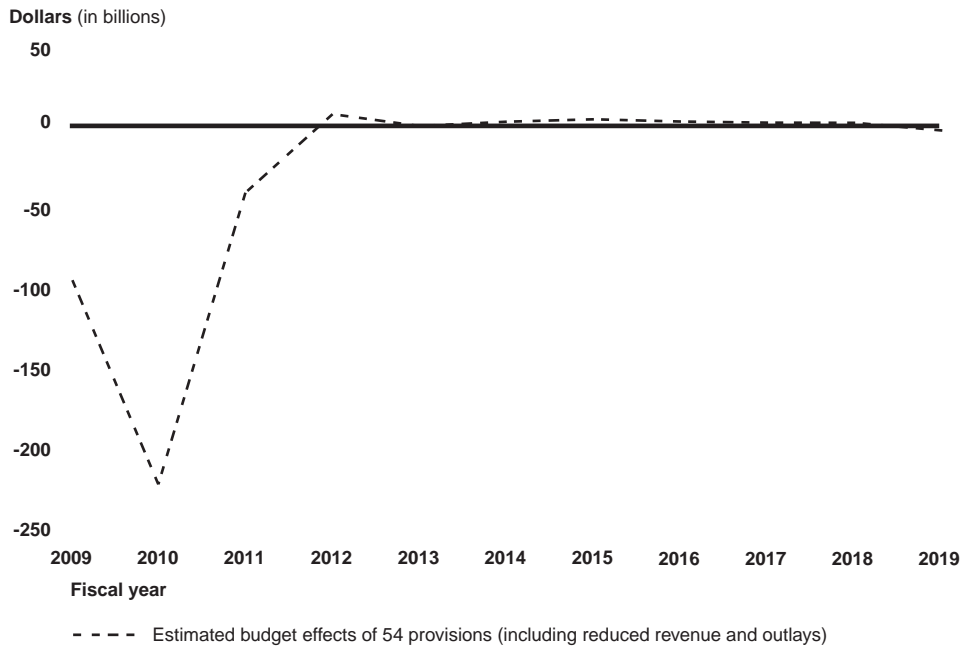
Source: GAO analysis of IRS and Joint Committee on Taxation data.

^aThe actual value is nonzero but is rounded down to zero.

^bThis dollar total differs from the total \$326 billion reported by JCT because it excludes seven provisions that IRS is not responsible for administering. These seven provisions are two grants-in-lieu-of-credits provisions, coordination of low-income housing credit and low-income housing grants, the New Markets Tax Credit, the public debt limit, a prohibition on the collection of certain payments, and executive compensation oversight.

The bulk of the stimulus to be provided by the tax provisions is expected to be in fiscal year 2010, as shown in figure 2.

Figure 2: Total JCT-Estimated Budget Effects of the 54 Recovery Act Provisions That IRS Has a Role in Administering, from Fiscal Year 2009 through 2019



Source: JCT.

As previously mentioned, we focused our work on five provisions and performed limited work on a sixth. A brief description of each provision follows. (See app. I for a more thorough description of these provisions, including provision requirements.)

- **Build America Bonds (BAB):** BABs are taxable government bonds that can be issued with federal subsidies for a portion of the borrowing costs delivered either through nonrefundable tax credits provided to holders of the bonds (tax credit BAB) or as refundable tax credits paid to state and local governmental issuers of the bonds (direct payment BAB). Direct payment BABs are a new type of bond that provides state and local government issuers with a direct subsidy payment equal to 35 percent of the bond interest they pay. Tax credit BABs provide investors with a nonrefundable tax credit of 35 percent of the net bond interest payments (excluding the credit), which represents a federal subsidy to the state or local governmental issuer equal to approximately 25 percent of the total return to the investor. State and local governments may issue an unlimited number of BABs through December 31, 2010, and all BAB proceeds must be used for capital expenditures.

-
- Consolidated Omnibus Budget Reconciliation Act (COBRA): Recently extended, the COBRA provision originally provided a 65 percent health insurance subsidy for up to 9 months for individuals who lost health insurance coverage due to involuntary termination between September 1, 2008, and December 31, 2009.⁷ Former employers, or in some cases multiemployer health plans or insurers, pay 65 percent of insurance premium costs and are reimbursed through a tax credit against their payroll tax liability or through a tax refund if the credit exceeds their payroll tax liability.
 - First-Time Homebuyer Credit (FTHBC): The Recovery Act expanded the FTHBC, which was initially established under the Housing and Economic Recovery Act of 2008,⁸ to provide taxpayers a refundable tax credit of up to \$8,000 for the purchase of a home.⁹ Taxpayers are generally not required to repay the credit unless the home ceases to be the taxpayer's principal residence within 3 years of purchase.¹⁰ Several of the issues with the FTHBC that are discussed in this report include differences between the 2008 and 2009 credits. The 2008 credit differs from the 2009 credit in that it provided taxpayers up to \$7,500, which has to be repaid in \$500 increments over the course of a 15-year period. We testified on the use of

⁷The Department of Defense Appropriations Act, 2010, Pub. L. No. 111-118, 123 Stat. 3409 (Dec. 19, 2009), extended COBRA premium assistance to include individuals involuntarily terminated through February 28, 2010. The maximum duration of assistance was also increased from 9 to 15 months.

⁸Pub. L. No. 110-289, 122 Stat. 2654 (July 30, 2008). The 2008 FTHBC operated similarly to an interest-free loan, which taxpayers must pay back over time. The credit originally applied to purchases made between April 9, 2008, and June 30, 2009. The Recovery Act amended the FTHBC to make it a true refundable credit (taxpayers do not repay the credit) and extended the tax credit to purchases made between January 1, 2009, and November 30, 2009.

⁹The Worker, Homeownership, and Business Assistance Act of 2009, Pub. L. No. 111-92, 123 Stat. 2984 (Nov. 6, 2009), extended the FTHBC to home purchases made through April 30, 2010, as well as those that are under a binding contract on that date if the contract provides for closing the sale on or before June 30, 2010. The act also authorized a credit of up to \$6,500 for individuals who owned and used the same residence as their principal residence for any 5 consecutive years during the 8-year period ending when they bought another property to use as their principal residence. The amendments and extensions by this act were generally outside the scope of our work.

¹⁰A principal residence is the main home a taxpayer lives in most of the time. It can be a house, houseboat, housetrailer, cooperative apartment, condominium, or other type of residence. Among other circumstances, a home ceases to be a principal residence when a taxpayer sells it.

the FTHBC and implementation and compliance challenges in October 2009.¹¹

- **Making Work Pay Credit (MWPC):** The MWPC is a refundable tax credit that provides up to \$400 and \$800, respectively, to working individuals and married couples who file joint returns. Taxpayers may receive the credit throughout the year in the form of lower amounts of tax withheld from their paychecks. Taxpayers who do not have taxes withheld throughout the year will not benefit from the credit until they claim it on their annual tax return.
- **Net Operating Loss (NOL) Carryback:** The NOL carryback provision allows eligible small businesses—those that had a 3-year gross receipts average of no more than \$15 million—to apply for a refund for taxes paid in up to 5 previous years if the business experienced a loss in 2008.¹²
- **Health Coverage Tax Credit (HCTC):** The HCTC can be claimed (1) by workers who have lost manufacturing or service jobs due to international trade or have lost public agency jobs and are eligible for a form of Trade Adjustment Assistance or (2) by those who are receiving payments from the Pension Benefit Guaranty Corporation. Among other things, the Recovery Act increased the health insurance premium subsidy rate from 65 percent to 80 percent of the premiums for an eligible taxpayer’s qualified health insurance plan.

IRS Moved Quickly to Address the Recovery Act’s Significant Implementation Challenges

While IRS has implemented major pieces of legislation in the past, the Recovery Act posed significant implementation challenges because it was a large piece of legislation and many provisions were immediately or retroactively effective and had to be implemented during the tax filing season—IRS’s busiest time of year. IRS officials moved quickly to implement the Recovery Act, aided by their efforts to organize internally and consult externally with lawmakers and industry groups before the act’s passage. IRS put its highest priority on implementing 14 of the 54 IRS provisions in 2009 because they required immediate action.¹³ Some of

¹¹GAO, *First-Time Homebuyer Tax Credit: Taxpayers’ Use of the Credit and Implementation and Compliance Challenges*, [GAO-10-166T](#) (Washington, D.C.: Oct. 22, 2009).

¹²The Worker, Homeownership, and Business Assistance Act of 2009 revised the NOL carryback provision by extending the NOLs qualifying for the 5-year carryback period to those occurring in 2009 and expanding the provision to include all businesses, except for those that received funds under the Troubled Asset Relief Program.

¹³The 14 provisions IRS implemented in 2009 were the MWPC, economic recovery payments to recipients of Social Security and other benefits, a special credit for government retirees, temporary increases in the Earned Income Tax Credit, the FTHBC, NOL carrybacks, COBRA, the HCTC, and six bond provisions, including BABs.

these provisions, such as the FTHBC and NOL carrybacks, were retroactive and could be claimed on a 2008 tax return. IRS started taking action on many of the remaining 40 provisions in 2009 as well. Some provisions affected the 2009 filing season (for tax year 2008), while others mainly will affect the 2010 and 2011 filing seasons.

To implement the provisions, IRS quickly issued forms and guidance, communicated with taxpayers and tax return preparers, and made computer programming or processing changes. For example, within days of the act's passage, IRS issued revised withholding tables for the MWPC and produced new or updated tax forms and instructions for it and COBRA. As shown in table 1, as of January 12, 2010, IRS either completed or initiated steps to issue new forms and instructions and revise many others for 48 of the 54 provisions, or 89 percent of the total. When we first checked on progress, as of August 20, 2009, or about 6 months after the Recovery Act's enactment, the percentage was also greater than 80 percent. In addition, as of January 12, 2010, IRS communicated with taxpayers and tax return preparers through a variety of avenues, such as news releases, postings on irs.gov, podcasts, and You Tube videos for 47 of the 54, or about 87 percent of the provisions. IRS also made computer programming changes to enable processing for paper and electronically filed returns for 39, or about 72 percent of the provisions. IRS did not plan to engage in guidance and instruction for 6 provisions or education and outreach activities for 7 provisions, or make processing and programming changes for 15 provisions because, according to IRS officials, some did not require activities to inform the public or ready IRS systems. We agree with this decision because, as we saw, some of the tax provisions without implementation activities were extensions or expansions of previously existing tax provisions, modified previously existing tax rules, or gave additional guidance. For example, one provision amended the Work Opportunity Tax Credit (WOTC) to create two new categories of targeted groups, and as a result, IRS updated the instructions to the related tax form to be filed with IRS but did not isolate amounts related to these categories on the form itself or make any substantive processing and programming changes.

Table 1: Implementation Status of IRS's 54 Provisions as of January 12, 2010

Provision category	Number of provisions	Number of provisions with guidance or instruction	Number of provisions with education or outreach	Number of provisions with processing or programming changes
Individual credits	12	12	11	12
Business incentives	11	10	9	6
Energy incentives	14	14	14	12
COBRA provision	1	1	1	1
Bond incentives	14	10	10	7
Health coverage improvement	1	1	1	1
Withholding on government contractors	1	0	1	0
Total	54	48	47	39

Source: GAO analysis of IRS data.

Responding Quickly Entailed Tradeoffs, and Subsequent Improvements Were Made

IRS management had to make tradeoffs, often balancing other factors, such as not making some computer changes to collect data, against the need to quickly process claims and get tax information and assistance out to the public, in order to implement the Recovery Act. For provisions we reviewed in detail, IRS's initial actions were at times later substantively adjusted.

As a first example of a tradeoff, because IRS needed to quickly issue a new set of withholding tables so taxpayers could immediately benefit from the MWPC through reduced federal tax withholding, Treasury decided not to fully account for the effect of the MWPC on taxpayers whose incomes were in the MWPC phaseout range.¹⁴ As a result, taxpayers with incomes in the phaseout range did not receive a precisely calculated tax reduction. In November 2009, IRS issued new withholding tables for 2010 that included two new brackets to better recognize the effect of the MWPC on taxpayers in the phaseout range.

The withholding changes for the MWPC may also have unfavorable consequences for some other taxpayers. For instance, TIGTA recently reported that over 15 million taxpayers, such as those receiving pensions and joint filers with two or more jobs between them, may be negatively

¹⁴The MWPC is reduced for single filers with modified adjusted gross incomes in excess of \$75,000 and joint filers with incomes in excess of \$150,000.

affected by the MWPC.¹⁵ These taxpayers may owe taxes or receive a lesser or no refund because not enough taxes were withheld from their paychecks to satisfy their eventual tax obligation or maintain previous withholding levels. IRS and Treasury have taken steps to deal with potential underwithholding for these taxpayers. IRS has conducted outreach to encourage taxpayers to look more closely at their tax withholding and plans to do more outreach. IRS's Web site contains publications and other guidance, including a tax withholding calculator, instructing taxpayers how to adjust their withholding in light of the MWPC. To address potential underwithholding for pensioners, Treasury developed supplemental withholding tables that pension administrators can use in conjunction with the previously issued tables to offset the effect of the MWPC.

In addition, because of the MWPC, some taxpayers could be subject to tax penalties as a result of the credit.¹⁶ TIGTA estimated that over 1 million taxpayers could be assessed a tax penalty or have their tax penalty increased because of the MWPC. IRS has taken steps to address these concerns as well, as it will allow taxpayers to use Form 2210, "Underpayment of Estimated Tax by Individuals, Estates, and Trusts," to request that the penalties be waived. IRS has alerted taxpayers to this option and how to exercise it by adding information to the instructions for the Form 1040, "U.S. Individual Income Tax Return," and, according to TIGTA, also plans to add information to Publication 505, "Tax Withholding and Estimated Tax."

A second tradeoff involved the FTHBC. Because of the compressed time to implement the revised credit, IRS did not make computer changes to easily collect data, including the home purchase date, from the Form 5405, "First-Time Homebuyer Credit," the form used to claim the credit.¹⁷ This was

¹⁵TIGTA, *Recovery Act: Millions of Taxpayers May Be Negatively Affected by the Reduced Withholding Associated With the Making Work Pay Credit* (Washington, D.C., 2009). In a written response to TIGTA's report, IRS officials said this estimate was overstated, but they did not provide their own estimate.

¹⁶If taxpayers have significantly underpaid their taxes at the time they file their individual income tax returns, they may be assessed a tax penalty. Based on IRS rules for 2008, taxpayers would generally not be required to pay a penalty if the total tax shown on their return minus the amount they paid through withholding is less than \$1,000, or if they had no tax liability in the previous year.

¹⁷The 2009 FTHBC can be claimed on regularly filed or amended 2008 tax returns or on 2009 returns, which are filed in 2010.

problematic because without the home purchase date IRS was unable to easily distinguish 2008 and 2009 FTHBC claims, a problem we noted in our October 2009 testimony.¹⁸ Distinguishing between the two credits is critical because the acts establishing them contain different requirements, including whether and how the credit is to be repaid.¹⁹ In studying FTHBC claims, TIGTA found that, as of May 29, 2009, IRS had not properly categorized more than 43,000 returns, considering them as 2008 claims instead of 2009 claims.²⁰ According to TIGTA, if further action is not taken, some taxpayers who bought a home in 2009 could receive a letter from IRS incorrectly indicating that they must repay the credit. IRS plans to verify the date of purchase on past claims and make any necessary adjustments when it begins enforcing the 2008 FTHBC repayment provisions. IRS also plans to make the computer changes needed to collect all significant data for 2009 claims, including home purchase date, from a revised Form 5405.

As a third example of a tradeoff, because of the limited time to make necessary computer programming changes that would have enabled payments by direct deposit, IRS issued BAB direct payments by paper check instead of electronic payments. According to IRS officials, IRS's use of paper checks possibly increased the costs of issuing BAB direct payments at least nominally. For 2010, IRS plans to change Form 8038-CP, "Return for Credit Payments to Issuers of Qualified Bonds," to include bank routing numbers so that payments can be made electronically.

Also, because of the limited time, IRS used an existing tax-exempt government bond form, Form 8038-G, "Information Return for Tax-Exempt Government Obligations," for state and local governments to report 2009 BAB information. Governmental issuers were required to submit a copy of Form 8038-G, to identify the issue as a BAB and to record information on the issue price, weighted average maturity, yield percentage, and the use of bond proceeds. However, unlike what is required for other bond issues, BAB issuers were also required to attach a separate schedule to identify the type of bond issue. For 2010, IRS plans to use a new form specifically designed for BABs. The new form will collect

¹⁸ [GAO-10-166T](#).

¹⁹ Generally, taxpayers must pay back the 2008 FTHBC in \$500 increments over a 15-year period, whereas the 2009 credit does not need to be repaid unless the home ceases to be the taxpayer's principal residence within 3 years of the date it was purchased.

²⁰ In late March 2009, IRS had begun categorizing incoming tax returns as either 2008 or 2009 claims based on the home acquisition date reported on the Form 5405.

the same information that was collected in 2009, but issuers will be able to identify the type of BAB and provide information on the type of bond issue all on the form itself, requiring no attachment.

Another effect of the limited time available to implement BABs was that BAB work took priority over already-existing bond projects, delaying the other projects somewhat, according to Treasury and IRS officials.

As a final example, IRS also made tradeoffs when implementing NOL carrybacks.

- As soon as the Recovery Act was enacted, taxpayers began filing 3-, 4-, and 5-year NOL carryback claims, which allowed them to use 2008 small business losses to reduce taxable income from 3, 4, or 5 years before and get tax refunds quickly. Because taxpayers made claims before IRS issued its guidance on March 16, 2009, taxpayers made what IRS officials considered invalid or unclear elections on their NOL carryback claims.²¹ Despite the March 16th guidance, taxpayers continued to file unclear carryback claims because they appeared to have not followed the instructions in the guidance, which told taxpayers to attach a statement to their tax return indicating certain information. Officials processed the claims and decided to issue on May 11, 2009, a second piece of guidance superseding the March 16th one in order to make the process easier for taxpayers. The May 11th guidance reduced the burden on taxpayers by allowing them to file the appropriate NOL carryback form without having to attach an election statement. By reviewing the computations on the appropriate form, IRS was able to find the information it needed to process the claim.
- When processing takes more than 45 days, IRS has to pay interest on NOL refunds, just as it must for other refunds taking more than 45 days to process. In order to process the claims on time, IRS initially took one to two revenue agents at seven campus locations away from examination cases for 1 to 2 days per week to determine whether small businesses' 3-year average gross receipts were under a \$15 million ceiling, making them

²¹The invalid or unclear elections generally refer to taxpayers not attaching a statement to their return indicating certain information, such as electing to apply the NOL to the taxpayer's taxable year that begins in 2008. For these claims, IRS sent a letter to the taxpayers that said that IRS assumed they were making an NOL claim under section 1211 of the Recovery Act and if that was their intent, no further action was required. If that was not the taxpayers' intent, they had 60 days to file an amended return. This guidance was in place until May 18, 2009. IRS did not track the number of invalid or unclear elections or the number of taxpayers who filed amended returns.

eligible for the NOL carryback refunds. This lasted for about 2 months until IRS developed a Gross Receipts Average Calculator tool. This tool replaced the need for extensive revenue agent involvement by automatically calculating a taxpayer's average gross receipts.

IRS's Data-Collection Efforts Have Limitations, and the Tax Provisions' Economic Stimulus Effect Cannot Be Precisely Isolated

Collecting data on the tax provisions is important to (1) ensure Recovery Act funds are used efficiently, (2) ensure program compliance, and (3) determine program effectiveness. Without appropriate data, it may be either impossible or costly to determine the extent to which the tax benefits were used, when they were used, whether they were used effectively and as intended, and whether any lessons could be learned. In previous reports, we noted that IRS did not collect sufficient information to determine the use and effectiveness of certain tax provisions.²² In the report on Indian reservation depreciation, we noted that the lack of sufficient data impeded IRS's ability to ensure program compliance.²³

IRS Has Plans to Collect Some Data to Track Many Provisions

In the past, IRS officials said that IRS's role is to collect data only to the extent that the data help it to administer the tax code. However, for the Recovery Act, IRS went beyond its typical efforts in order to provide transparency over the use of the tax provisions and to collect more reportable data on the tax provisions. For example, IRS did not collect any additional data related to the 5-year NOL carryback for the Job Creation and Worker Assistance Act of 2002, but it is collecting carryback data for the Recovery Act's NOL provision.

Throughout the year after the Recovery Act was enacted, IRS developed plans for collecting data. For example, as shown in table 2, of the 54 provisions that IRS has a role in implementing, IRS had detailed data-collection plans for 17, or about 31 percent. These 17 provisions cover about \$207 billion, or 63 percent, of the \$325 billion total cost that JCT estimated for the 54 provisions. For about 33 percent of the 54 provisions, covering about \$96 billion, or 30 percent, of the total cost, IRS had

²²See, for example, GAO, *Tax Expenditures: Available Data Are Insufficient to Determine the Use and Impact of Indian Reservation Depreciation*, [GAO-08-731](#) (Washington, D.C.: June 26, 2008); *Empowerment Zone and Enterprise Community Program: Improvements Occurred in Communities, but the Effect of the Program is Unclear*, [GAO-06-727](#) (Washington, D.C.: Sept. 22, 2006); and *Tax Administration: Information Is Not Available to Determine Whether \$5 Billion in Liberty Zone Tax Benefits Will Be Realized*, [GAO-03-1102](#) (Washington, D.C.: Sept. 30, 2003).

²³[GAO-08-731](#).

identified preliminary data sources, but not what, if any, data it will compile and report.

Table 2: Results of IRS’s Recovery Act Data-Collection Planning Effort

Calculation category	Detailed plans ^a	Preliminary data sources identified ^b	No data available from tax forms ^c	No reporting planned ^d	Total
Number of provisions	17	18	9	10	54
Percent of number of provisions	31	33	17	19	100
JCT total estimated revenue loss (in billions)	207	96	5	18	325^e
Percent of JCT total estimated revenue loss	63	30	1	6	100

Source: GAO analysis of IRS data.

^aIRS started or plans to have its nonresearch units create weekly or monthly reports or estimates, or it has noted the specific data it plans to collect.

^bIRS has identified forms from which data could be collected by its research unit but has not identified the specific data it plans to compile and report.

^cIRS does not plan to modify tax forms to collect data.

^dIRS does not plan to collect data or report any information. According to IRS officials, this category includes nine provisions related to guidance or reflecting rule changes where there is nothing for them to report and one provision that Treasury’s Financial Management Service (FMS) took the lead in administering, although IRS had a minimal role.

^eNumbers do not add to \$325 billion due to rounding.

For the remaining 19 provisions covering about 7 percent of the total cost, IRS does not plan to compile or report any data. For 9 of these provisions, covering about \$5 billion, or 1 percent of total cost, IRS officials stated that no data are available on tax forms and IRS does not plan to modify tax forms to enable data collection. As an example, the WOTC is included in this group. The Recovery Act expands the credit by adding two categories of eligible individuals. IRS does not plan to modify the tax form to enable data collection on the newly eligible individuals as it currently does not collect data on any of the eligible individuals. For the final 10 provisions, covering about \$18 billion or 6 percent of total cost, IRS did not plan to collect data or report any information because, according to IRS officials, this category included 9 provisions relating to guidance or reflecting rule changes.²⁴ For the other provision, IRS had a minimal role, and Treasury’s

²⁴Although IRS does not plan to collect or report information on certain provisions, it may still engage in enforcement-related activities to ensure a credit is lawfully claimed.

Financial Management Service (FMS) took the lead in administering it.²⁵ We agree with IRS's decision not to report on these 10 provisions.

Very little of the data that IRS has collected on the tax provisions has been released publicly. On September 3, 2009, Treasury released preliminary data collected on its Recovery Act programs, including the use of BABs, economic recovery payments, and the FTHBC. Recovery.gov includes a chart on the estimated dollars distributed through the tax provisions, but this estimate is not based on actual provision use. Rather, it prorates estimates that were created by Treasury's Office of Tax Analysis before the act's implementation. Data collected for individual tax provisions that specify the number of provision users and dollar amount of claims made were not reported on recovery.gov, as of January 20, 2010.

Initial Data Collection Did Not Fully or Accurately Capture the Use of Some Recovery Act Provisions

During much of our review, IRS focused on collecting and internally reporting data on four provisions—BABs, COBRA, the FTHBC, and the HCTC. (See app. IV for information on the use of these provisions.) Some of the data IRS collected did not accurately capture taxpayers' use of Recovery Act provisions, as provision use was sometimes incompletely described or overstated.

BAB Data Do Not Show Specific Bond Use

IRS's reporting requirements for BABs are minimal in contrast to requirements for Recovery Act infrastructure and other direct spending projects, even though such projects may be similar. For example, funding for both Recovery Act spending projects and BABs may be used for highway, school, water, sewer, or utility improvements. Currently, IRS requires state and local governments to submit an information return at the time of bond issuance that describes the type of bond issue, issue price, weighted average maturity, yield percentage, and the use of bond proceeds. As shown in appendix IV, as of January 1, 2010, state and local governments reported 443 BAB issuances valued at about \$32.4 billion. One hundred and thirty-one BABs were issued for education, which was more issuances than for any other type, except the "other" category.

Spending projects undertaken under the Recovery Act by state and local governments are subject to additional reporting requirements. Section

²⁵FMS took the lead in administering the economic recovery payments for Social Security recipients. IRS's role related to economic recovery payments arose from the fact that the MWPC must be reduced by the amount of economic recovery payment received. IRS conducted outreach related to the provision.

1512 of the act requires nonfederal recipients of Recovery Act grants, contracts, and loans to provide information on each project or activity, including a description of the project and its purpose, an evaluation of its status toward completion, the amount of recovery funds spent, and the number of jobs created and retained.²⁶ The reporting required for spending projects is intended to increase accountability and transparency. In addition, federal agencies are required to submit reports that describe the amount of Recovery Act funds made available and paid out to the states through contracts, grants, and loans. Although IRS is not required to publicly report data on BAB use, doing so could increase accountability and transparency. As part of its bond outreach efforts, Treasury has asked governmental issuers to report how their government has used BABs. Treasury plans to compile this information for its internal use only. There are no efforts by other federal agencies to compile or publish BAB information. The limited data collected and publicly reported for BABs does not reflect the same emphasis as that for spending projects.

According to the Director of IRS's Tax-Exempt Bonds division, more detailed information reporting on BAB-financed projects, such as that required on the Schedule K of Form 990, "Supplemental Information on Tax-Exempt Bonds," may increase compliance over the life of bonds because government issuers would be reminded of bond requirements each year when filing the form and would be more likely to keep and maintain required documentation. Charitable organizations are required to submit Schedule K annually with their tax returns, although no similar yearly bond reporting requirement exists for governmental bond issuers. The rationale for the Schedule K was that significant noncompliance with recordkeeping requirements for charitable organization tax-exempt bonds existed, making it hard for IRS to determine if the bonds remained qualified for tax exemption throughout their life. Accordingly, Schedule K and its instructions ask for a description of the bond's purpose—constructing a hospital or acquiring office equipment are examples cited—and the year the project was substantially completed, just like the reporting requirements for Recovery Act spending projects.

IRS officials said that yearly BAB reporting similar to the Schedule K would help IRS know whether bonds remained qualified for their tax-

²⁶Section 1512 of Division A of the Recovery Act. Neither individuals nor recipients receiving funds through entitlement programs, such as Medicaid, or tax programs are required to report.

advantaged status. One hundred percent of BAB proceeds are to be used for qualified capital expenditures, and yearly reporting by governmental issuers would allow IRS to more easily identify issuers who have not adhered to this standard or maintained the required documentation to show how bond proceeds were used. It could also help lawmakers or others in determining the overall effectiveness of the newly created bonds. Any additional cost of reporting, such as those already borne for spending projects, could be tempered by having a minimum reporting threshold or delaying the onset of requirements, as was the case when reporting for charitable organizations was instituted. However, if IRS required more specific reporting for BABs, it could not publicly release it for individual issuers. Currently, unlike the case with the Schedule K, IRS is prohibited from disclosing BAB-related information collected by IRS. Legislation would be needed to allow the BAB information and any similar information related to governmental bonds to be disclosed.

According to Treasury officials, given the periodic direct payments that IRS must make for the first time to state and local governments for BABs, ongoing safeguards are needed to verify that payments are only made on outstanding bond issues that continue to meet BAB eligibility requirements. To this end, IRS and Treasury have a working group to examine different approaches for acquiring BAB information over the life of bonds to verify payments and determine how frequently additional bond information reporting by issuers should occur. The working group may suggest new bond reporting requirements, such as a new tax form, in late 2010. More detailed reporting on BABs to provide added transparency and accountability could help with this effort and be beneficial if it were compatible with other needs identified by the working group.

COBRA Data Will Not Include the Number of Dependents Benefiting from COBRA Assistance

As of December 18, 2009, IRS had not reported the number of former employees receiving COBRA premium assistance. When the data are ready, IRS information on COBRA premium assistance claims will understate the total number of individuals receiving health insurance. Employers are instructed to list the number of individuals provided COBRA premium assistance on Form 941 for 2009, "Employer's Quarterly Federal Tax Return." However, the number entered on the form is only the total number of former employees receiving COBRA coverage and does not include their dependents who may be covered under the same insurance plan. For example, if COBRA premium assistance was paid for an insurance plan that covered a former employee and his or her spouse and child, an employer would count that as one person provided COBRA premium assistance on Form 941, not three. Counting this way prevents a meaningful comparison with the JCT's estimate that 7 million workers and

Initial FTHBC Data Did Not Reflect the Credit's Full Dollar Value

dependents would use the COBRA subsidy. Moreover, the number does not provide stakeholders complete information on provision use. According to IRS officials, the form did not include dependents due to a short time frame for implementation, space constraints on the form, and a desire not to overburden employers with additional reporting requirements. As of December 26, 2009, as shown in appendix IV, IRS had received approximately 192,000 returns from employers claiming about \$803 million in COBRA credits.²⁷

Before September 30, 2009, IRS's 2009 FTHBC information was understated—it did not show the full dollar amount of the credits claimed. Initially, IRS only reported the difference between the maximum benefits of the 2008 and 2009 FTHBCs as the total benefit of the 2009 FTHBC. That is, the data only reflected an estimated increment above the 2008 FTHBC's maximum benefit of \$7,500 as the amount of credit claimed for the 2009 FTHBC, rather than up to the full amount of the credit, a maximum of \$8,000. In a September 3, 2009, report on the Recovery Act, Treasury also reported this estimated incremental amount. On September 4, 2009, we pointed out to IRS officials that the increment did not consider that taxpayers might have decided to buy a house because the \$8,000 maximum benefit offered with the 2009 FTHBC generally would not have to be paid back to the federal government—unlike the 2008 credit for which the \$7,500 would have to be repaid over 15 years. IRS revised its data and provided information reflecting the full amount of the credit claimed in a September 30, 2009, report. As shown in appendix IV, as of November 21, 2009, IRS data show that about 1.1 million filers claimed about \$7.3 billion of the 2008 credit, while about 630,000 filers claimed about \$4.7 billion of the 2009 FTHBC.²⁸

²⁷Although the Form 941 is filed quarterly, employers were not required to submit all COBRA subsidy claims for 2009 until the fourth quarter of 2009; therefore, there may be an increase in the total number of COBRA filers for the year.

²⁸These data should be interpreted as interim, as some concerns exist about their reliability. In September 2009, TIGTA reported that 43,967 returns were coded as a 2008 FTHBC even though the purchase had occurred in 2009. IRS plans to verify the date of purchase and make any needed adjustments when it begins enforcing the 2008 FTHBC payback provisions. We reported this information to the Congress at a hearing on October 22, 2009, [GAO-10-166T](#).

HCTC Data Overstate the
Number of New Enrollees
Attributable to the Recovery
Act

The roughly 12,000 new enrollees in the HCTC program that IRS has attributed to the Recovery Act is overstated, at least for the early period soon after the Recovery Act. (App. IV provides more detailed data.) The number is overstated because it included some taxpayers who were in the pipeline for enrollment before the President signed the Recovery Act on February 17, 2009. IRS officials chose April 1, 2009, as the first date for attributing HCTC participation to the act. They chose this date because, among other things, it was the date the health insurance premium subsidy rate rose from 65 percent to 80 percent, and presumably more people would be inclined to enroll given the higher subsidy. However, according to June 2008 IRS data, IRS would only mail HCTC program kits and registration forms to taxpayers after other agencies spent 1 to many months determining if a taxpayer was in fact eligible for the credit in the first place. Thus, to be enrolled in April 2009, many taxpayers would have to have started the HCTC process before the Recovery Act was signed. IRS officials acknowledged some of the enrollees counted as new could have been in the pipeline for enrollment on February 17. Officials also said their collection of data in general was not intended to see whether the Recovery Act actually motivated someone to change behavior, in this case to enroll in the HCTC program.

The Economic Stimulus
Effect of the Tax
Provisions Cannot Be
Precisely Isolated

The data IRS has collected about the tax provisions it is administering are not designed to isolate or differentiate the stimulus effect of these provisions from that of other Recovery Act provisions. To assess the effects of stimulus policies such as tax incentives, economists use evidence from macroeconomic forecasting models and models that extrapolate from historical data. The forecasting models are based largely on historical evidence, and the analyses estimate behavior based on how economic variables such as gross domestic product (GDP) have responded to stimulus policies in the past. Neither type of model uses current data to assess the effect of the stimulus. The models are used to estimate “multipliers,” which represent the cumulative effect of a particular incentive, such as a tax cut, on GDP over time. For example, a multiplier of 1.0 means a dollar of stimulus financed by borrowing results in an additional dollar of GDP. Generally, multipliers can provide insights into the potential effect on GDP of different types of public spending. Because of the limited historical experience with a fiscal stimulus of the magnitude of the Recovery Act, there is uncertainty about the extent to which multipliers based on historical evidence about the effect of previous

business cycles will accurately reflect the stimulus effect this time. However, economists use the models as a basis for constructing reasonable ranges of values for multipliers.²⁹ Drawing on analyses based on past experience with the results of government spending, CBO has estimated multipliers for Recovery Act provisions that include tax expenditures (see table 3).

Table 3: Estimated Multipliers for Selected Recovery Act Provisions

Category	Estimated policy multiplier	
	High	Low
Onetime payments to retirees	1.2	0.2
2-year tax cuts for lower- and middle-income people	1.7	0.5
1-year tax cuts for higher-income people	0.5	0.1
Extension of the FTHBC	1.0	0.2
Tax provisions for businesses primarily affecting cash flow	0.4	0.0

Source: CBO.

Although the economic effect of each of the Recovery Act tax provisions cannot be precisely estimated, the effect of some provisions on specific aspects of the economy may be described in general terms. For example, reports released by the Executive Office of the President's Council of Economic Advisers (CEA) in September 2009 and January 2010 noted the potential effect of the bonus depreciation, MWPC, and FTHBC provisions.³⁰ According to CEA's analysis, the bonus depreciation provision, which allows businesses to recover the costs of acquired property at a faster rate than they otherwise would, benefited businesses and may have led to a slower investment decline in the second quarter of 2009 than would have occurred in the absence of such provisions. Additionally CEA concluded that although the MWPC, along with other provisions of the Recovery Act and other economic recovery policies,

²⁹For more information on the imprecision of economic forecasting and macroeconomic models and multipliers that were created for the Recovery Act, see GAO, *Recovery Act: Recipient Reported Jobs Data Provide Some Insight into Use of Recovery Act Funding, but Data Quality and Reporting Issues Need Attention*, [GAO-10-223](#) (Washington, D.C.: Nov. 19, 2009).

³⁰Executive Office of the President's Council of Economic Advisers, *The Economic Impact of the American Recovery and Reinvestment Act of 2009: First Quarterly Report* (Washington, D.C., Sept. 10, 2009); Executive Office of the President's Council of Economic Advisers, *The Economic Impact of the American Recovery and Reinvestment Act of 2009: Second Quarterly Report* (Washington, D.C., Jan. 13, 2010).

helped stabilize consumption, a small drop in consumption in the second quarter could indicate that households were using the MWPC mainly to increase savings and pay off debt. In addition, their analysis suggests that, in addition to other policy actions affecting residential real estate, the Recovery Act's FTHBC may have moderated job losses in the construction industry.

IRS Took Steps to Mitigate Abuse of Provisions, but Some Compliance Challenges Arose and Others Remain

We have previously reported that evaluating risk is important because it allows an organization to identify potential problems before they occur so that mitigating activities can be planned and implemented over a project's life to minimize adverse effects on objectives and outcomes.³¹ Risk management includes executive oversight, preparing for risk management, identifying and analyzing risks, and mitigating risks. Organizations prepare for risk management by establishing a strategy for identifying, analyzing, and mitigating risks. Identifying and analyzing risks involves identifying risks from internal and external sources and evaluating each risk to determine its likelihood and consequences. Mitigating risks involves developing risk-mitigation plans that outline the techniques and methods that will be used to avoid, reduce, and control the probability of risk occurrence.

Consistent with these activities, IRS established an executive steering committee to oversee Recovery Act implementation. The committee, which was formed before the act's enactment, included the heads of all IRS operating divisions. It met regularly to discuss issues such as the resources needed to implement the tax provisions, changes to be made to forms and information systems, information to be posted on the Internet, and compliance challenges.

IRS also completed eight risk assessments—questionnaires that identified potential risks, their likelihood of occurrence, and their effect—that

³¹GAO, *Foreign Assistance: State Department Foreign Aid Information Systems Have Improved Change Management Practices but Do Not Follow Risk Management Best Practices*, [GAO-09-52R](#) (Washington, D.C.: Nov. 21, 2008); and GAO, *Information Security Risk Assessment: Practices of Leading Organizations*, [GAO/AIMD-00-33](#) (Washington, D.C.: Nov. 1, 1999).

covered 12 provisions immediately available to taxpayers.³² The risk assessments considered common risk areas such as the adequacy of internal control procedures, agency-specific risks such as the extent of management oversight over the risk-management process, and program-specific risks such as resource availability. The risk assessments resulted in 9 of the 12 provisions being considered as medium risk and 3 as low risk. IRS plans to reevaluate these assessments and complete assessments of the remaining Recovery Act tax provisions in 2010. Following Treasury policy, IRS completed mitigation plans for the 9 provisions it found to be at medium risk.

The mitigation plans outlined the actions that IRS planned to take to address identified risks, and IRS program officials were responsible for monitoring their implementation. In addition, Treasury began reviewing IRS risk-mitigation plans in July 2009 and told us in January 2010 it planned to begin reviewing risk assessments and mitigation plans for tax year 2010 provisions that month, taking into account GAO, TIGTA, and Treasury Office of Inspector General findings.

IRS Has Addressed Some Compliance Challenges with the FTHBC, and Alternatives Exist That May Alleviate a Remaining Challenge

Despite its efforts to assess and mitigate potential risks, IRS still encountered compliance challenges with the FTHBC; it addressed some of them. For example, IRS used prerefund filters to ensure that taxpayer income and the amount of credit claimed on a return do not exceed statutory limits. IRS also used an electronic fraud-detection system with filters to detect and prevent fraudulent refund schemes. However, IRS and TIGTA reviews of early FTHBC filings identified additional compliance issues, such as instances where taxpayers who had previously owned a home claimed the credit. Based on its review of early filings, IRS implemented additional computer filters to better determine taxpayer eligibility before refunds were issued. For example, IRS developed filters to check for indications of prior homeownership within the past 3 years. As a result of its prerefund checks, as of February 1, 2010, IRS had frozen

³²Some risk assessments covered more than one provision. The 12 provisions were the COBRA provision, the FTHBC, the HCTC, the NOL carryback provision, the MWPC, the Advance Earned Income Tax Credit, and six bond provisions, including BABs. IRS did not assess the risks for two other provisions immediately available to taxpayers—economic recovery payments to Social Security recipients, disabled veterans, and railroad retirement beneficiaries because Treasury’s Financial Management Service administered this provision, and a tax credit for certain government retirees, because the credit could not be claimed until 2009 returns were filed, starting in 2010. IRS planned to prepare a risk assessment for this credit in 2010.

about 140,000 refunds pending civil or criminal examination, and, as of December 2, 2009, had identified 175 criminal schemes and had 123 criminal investigations open.

IRS faces a challenge in knowing whether homebuyer credit recipients sell their homes. This is important for the 2009 credit because the Recovery Act requires that at least part of the credit up to \$8,000 may have to be repaid if a home is sold or otherwise ceases to be the taxpayer's principal residence within 3 years of purchase.³³ Repayment is also an issue for the 2008 FTHBC, as individuals who sell their homes or otherwise cease to use their home as their principal residence before fully repaying their credit up to \$7,500 have to accelerate their repayment. IRS modified Form 5405 for taxpayers to report the disposition of their home or a change in its use, but as of December 2009 it had not decided how it will identify individuals who fail to report.³⁴

An IRS form already exists that could help resolve this compliance issue, but whether IRS is authorized to use it for this purpose would have to be determined. Currently, IRS annually receives some Forms 1099-S, "Proceeds from Real Estate Transactions," from agents closing real estate transactions such as home sales.³⁵ The form provides information such as the seller's name and Social Security number and the sale price of the home and is to be used by IRS to determine if taxpayers have filed returns and reported all of their proceeds from real estate transactions. However, closing agents are generally exempt from reporting information on the sale of principal residences sold for \$250,000 or less if the agent receives written certification from the seller that certain assurances are true.³⁶ Moreover, it is not clear whether IRS has the authority to require Form 1099-S be filed by third parties currently exempted for purposes of

³³The Worker, Homeownership, and Business Assistance Act of 2009, Pub. L. No. 111-92, which extended the credit until April 30, 2010, also maintained the requirement that at least part of the credit may have to be repaid if the home is sold within 3 years of purchase.

³⁴Form 5405 is the form used to claim the FTHBC. The 2009 FTHBC can be claimed on regularly filed or amended tax returns for 2008 or 2009 returns.

³⁵Section 6045(e) of the Internal Revenue Code generally requires some real estate parties such as closing agents to file information returns with IRS on Form 1099-S.

³⁶26 U.S.C. § 6045(e)(5). To be exempted from the information-reporting requirements on the sale or exchange of a principal residence, the closing agent must obtain from the seller a written certification, signed by the seller under penalties of perjury, that certain assurances (such as the sale or exchange is of the entire residence for \$250,000 or less) are true. See Internal Revenue Procedure 2007-12.

recapture from FTHBC recipients. If Form 1099-S information reporting could be required for all home sales or for those taxpayers who do not certify that they had not claimed the FTHBC, IRS might be better able to identify the taxpayers who need to repay part or all of the credit. Because Form 1099-S contains the seller's Social Security number, IRS could match the identification numbers on the Forms 1099-S to those reported on returns claiming the FTHBC, isolating Form 1099-S filers who should have reported their home sale on the FTHBC form, but did not.

As we were completing our review, IRS officials identified an alternative way to analyze whether homebuyer credit recipients sell their homes and are, therefore, possibly subject to payback requirements. This alternative involves acquiring access to third-party data in the form of publicly available real estate information from local governments. This information could include individual properties' addresses, previous and recent sales prices, and sales dates. IRS could use these data in matches against Form 5405 or other IRS data to identify taxpayers who claimed the FTHBC and then sold their property without repaying any required part of the FTHBC benefit they received. IRS expects to purchase the use of these data, use them, and then evaluate how well they help IRS enforce the FTHBC provisions. The evaluation is not yet designed but should be able to cover issues like data reliability, comprehensiveness, and cost-effectiveness.

An Option Exists to Better Identify Unresolved COBRA Compliance Issues

The Recovery Act provides eligible taxpayers with COBRA premium assistance—a 65 percent reduction in health insurance premiums for individuals who were involuntarily terminated between September 1, 2008, and December 31, 2009.³⁷ An employer pays 65 percent of its former employees' insurance premium costs and is reimbursed in the form of a payroll tax credit.³⁸ This tax provision is only the second refundable tax credit administered by IRS's Small Business/Self-Employed (SB/SE)

³⁷The Department of Defense Appropriations Act, 2010 (Pub. L. No. 111-118) extends premium assistance to those involuntarily terminated through February 28, 2010.

³⁸In some instances, such as for state health plans that are subject to COBRA requirements, multiemployer group health plans or insurers may provide the COBRA subsidy and file for a COBRA credit.

division.³⁹ Unlike the other credit, SB/SE's compliance strategy for COBRA focuses on the employer and the Form 941, not on individuals receiving assistance.

To identify fraudulent or erroneous COBRA claims made by employers, IRS instituted a number of prepayment checks, such as looking for irregularities in COBRA claims and in the dollar value of subsidies. As of September 22, 2009, the prepayment checks had stopped about 1,500, or 2 percent, of COBRA claims for further review.

Other compliance challenges have not been resolved. For example, IRS does not know who receives the COBRA subsidies, which limits its ability to determine if a taxpayer is qualified to receive a subsidy and to ensure that employers do not receive the credit for ineligible individuals. In an effort to reduce employer burden, IRS did not require employers to submit lists of all people receiving COBRA. As a result, it was only aware of the number of individuals an employer reported on Form 941 and the total amount of the subsidy claimed. Employers are required by IRS to keep records of the COBRA assistance, including the names and Social Security numbers of covered employees, but IRS would see this information only during any examinations.

Another challenge facing IRS is verifying that those taxpayers who are required to repay part of the COBRA subsidy they receive do so. Those individuals and married couples filing joint tax returns with modified adjusted incomes above \$125,000 and \$250,000, respectively, are required to report on their tax returns that they received COBRA assistance. This requirement is in place because the COBRA subsidy phases out for those taxpayers with higher incomes, and those above the phaseout range are ineligible. IRS plans to conduct a review of filed returns to identify high-income taxpayers who did not report the subsidy as an addition to tax. However, rather than rely solely on audits to determine if these taxpayers

³⁹The Advance Earned Income Tax Credit (AEITC) was the first tax credit to be administered by SB/SE. The AEITC allows individuals to receive a portion of the Earned Income Tax Credit in their paychecks, instead of receiving all of it when filing their year-end tax return. Employers report the amount paid on the Form 941, "Employer's Quarterly Federal Tax Return," and on the employee's Form W-2, "Wage and Tax Statement." In 2007, we found that there was low use and high noncompliance associated with the AEITC. For more information, see GAO, *Advance Earned Income Tax Credit: Low Use and Small Dollars Paid Impede IRS's Efforts to Reduce High Noncompliance*, [GAO-07-1110](#) (Washington, D.C.: Aug. 10, 2007). Based on our report, in 2009 the President recommended in his fiscal year 2010 budget request that the AEITC program be terminated.

are subject to additional tax, IRS has taken some steps to obtain this information. For example, IRS worked with tax-preparation software companies to ensure that pointed questions are asked during tax return preparation to determine if individuals received COBRA during the year. IRS also has plans to use a compliance initiative project to test whether taxpayers did not report the subsidy as an addition to tax and decide if further action is needed.⁴⁰

Individuals are allowed to receive a COBRA subsidy for up to 9 months after their involuntary termination, but, since IRS does not know from the Form 941 who is receiving COBRA subsidies, it also does not have the information to know when an individual's eligibility period ends.⁴¹ Claims beyond 9 months may not be widespread because some studies have shown that, even with the subsidy, COBRA is generally more expensive to employees than employer-sponsored plans.⁴² Thus, in most circumstances, individuals have an incentive to terminate their COBRA coverage when other options exist. However, employers may have an incentive to continue claiming the credit even when former employees are no longer eligible. A past report of ours noted that businesses facing economic hardship may take advantage of the tax system by diverting payroll taxes for their own uses.⁴³ Employer audits are one of the ways IRS learns if an employer claimed the credit for employees for longer than 9 months. IRS will not be able to audit all employers. To address this concern, IRS has conducted outreach with the employer and payroll communities emphasizing the time limit and planned to continue doing so in the coming months. Yet, other than relying on costly audits, IRS had not finalized actions that it could take to ensure employers stop claiming the credit

⁴⁰Compliance initiative projects are activities to identify potential areas of noncompliance within a group of taxpayers so that the noncompliance can be corrected.

⁴¹Under the Recovery Act, individual eligibility periods end 9 months after the employee is involuntarily terminated and subsequently elects COBRA continuation coverage or when the employee becomes eligible for another group health insurance plan, such as Medicare or a plan offered through a spouse's employer. The Department of Defense Appropriations Act, 2010 (Pub. L. No. 111-118) extended coverage for up to 15 months.

⁴²See Congressional Research Service, *Health Insurance Premium Assistance for the Unemployed: The American Recovery and Reinvestment Act of 2009*, R40420 (Washington, D.C., Mar. 6, 2009) and The Kaiser Commission on Medicaid and the Uninsured, *The COBRA Subsidy and Health Insurance for the Unemployed* (Washington, D.C., Mar. 2009).

⁴³GAO, *Tax Compliance: Businesses Owe Billions in Federal Payroll Taxes*, [GAO-08-617](#) (Washington, D.C.: July 25, 2008).

when their former employees are no longer eligible, thus safeguarding against invalid COBRA claims that increase costs to the federal government.

A cost-effective option to help IRS with the unresolved compliance issues exists. IRS could expand its planned compliance initiative project to test whether employers are claiming COBRA subsidies for employees for longer than 9 months, or 15 months when considering the recent extension. IRS can use existing information to determine if significant noncompliance with the 15-month provision is apparent. If significant indications of noncompliance are found, IRS could issue “soft notices” to employers to remind them of COBRA eligibility requirements and the consequences of noncompliance.⁴⁴ IRS officials responded favorably to these ideas and said they would consider adopting them.

Documenting IRS’s Recovery Act Lessons Learned and Expanding Its Authority, with Appropriate Controls, Could Improve Future Tax Administration

IRS plans to do a “lessons learned” review of its Recovery Act experiences and implementation, most likely after the 2010 filing season, but it had not yet developed detailed plans during our review. This study would be consistent with a recommendation we have previously made. In an August 2002 report on the advance tax refund program, which the Congress designed to stimulate the economy, we noted that analysis is a key part of understanding performance and identifying improvement options.⁴⁵ We therefore recommended that IRS convene a study group to assess its performance with respect to the advance tax refund and related rate-reduction credit. We also said that to ensure that managers faced with similar challenges in the future have the benefit of this assessment, the results should be thoroughly documented. IRS implemented this recommendation and later said that the resulting internal report was a cornerstone in improving administration of the advance child tax credit.

⁴⁴IRS tests have shown that the agency has successfully reduced subsequent noncompliance in situations that involve relatively small amounts of money by sending letters referred to as “soft notices” that ask taxpayers to voluntarily fix their misreporting by filing an amended return or not repeating the action in the next year.

⁴⁵GAO, *Tax Administration: Advance Tax Refund Program Was a Major Accomplishment, but Not Problem Free*, [GAO-02-827](#) (Washington, D.C.: Aug. 2, 2002).

IRS Could Benefit from Broader Math Error Authority

IRS would have benefited from having math error authority (MEA) to enforce at least one Recovery Act provision from the outset rather than only after problems were identified. The Internal Revenue Code provides IRS with MEA to assess additional tax or correct other tax return errors in limited circumstances when an adjustment is the result of mathematical or clerical errors on the return.⁴⁶ Over the years, the Congress has granted IRS MEA for specified purposes.⁴⁷ For example, when a taxpayer makes an entry on a tax return for a deduction or credit in an amount that exceeds the statutory limit for that deduction or credit, IRS uses its MEA to correct the error during tax return processing. MEA is an automated and low-cost means to protect federal revenue and avoid the need for costly audits. This is due, in part, to the fact that IRS does not have to follow its standard deficiency procedures when using MEA—it must only notify the taxpayer that the assessment has been made and provide an explanation of the error.

As described earlier, IRS had problems enforcing some of the eligibility requirements of the FTHBC. After learning about the compliance problems with the FTHBC, the Congress expanded IRS's MEA in the Worker, Homeownership, and Business Assistance Act of 2009.⁴⁸ It followed our suggestion that, to reduce IRS's reliance on costly and burdensome audits of the credit, the Congress should consider providing IRS with additional MEA.⁴⁹ Specifically, we suggested that the Congress consider giving IRS MEA to use tax return information to automatically verify taxpayers' compliance with the 2008 FTHBC payback provision and to ensure that taxpayers do not improperly claim the credit in multiple years. In addition to following these suggestions, based on noncompliance identified by TIGTA, the Congress granted IRS MEA to assess additional tax without the notice of deficiency otherwise required if a taxpayer did not meet the credit's age requirement or did not submit the settlement statement used in the home purchase.

⁴⁶26 U.S.C. § 6213(b).

⁴⁷Section 6213(g)(2) of the Internal Revenue Code lists the circumstances in which MEA may be used.

⁴⁸Pub. L. No. 111-92, 123 Stat. 2984 (Nov. 6, 2009).

⁴⁹GAO, *Tax Administration: Opportunities Exist for IRS to Enhance Taxpayer Service and Enforcement for the 2010 Filing Season*, [GAO-09-1026](#) (Washington, D.C.: Sept. 23, 2009).

The Congress has been incrementally adding MEA authorizations for almost a century. The first basic exemption to the deficiency procedures for mathematical errors can be found in the Internal Revenue law in 1926. In 1976, the Congress expanded the authority beyond mathematical errors to clerical errors and gave taxpayers the right to ask that IRS reverse the math error assessment and follow IRS's normal deficiency procedures. In the 1990s, the Congress extended MEA multiple times to help IRS determine eligibility for certain tax exemptions and credits. As a recent example of where MEA could also be useful, in 2008 we suggested that the Congress provide IRS with the authority to automatically correct returns for individual retirement account (IRA) contributions that violated certain dollar or age limits.⁵⁰ In 2004, IRS had found IRA contribution overclaims by taxpayers under age 50 resulting in \$23.2 million in underreported taxes but did not have the MEA to use age-based data to check for age-based eligibility. Also, on September 30, 2009, after finding more than \$600 million of inappropriately claimed Hope Credits for higher education, TIGTA recommended that the Congress give IRS MEA to disallow claims for the Hope Credit for more years than allowed by law.⁵¹ In a November 2009 report, TIGTA listed four examples of other reports it had issued in fiscal years 2008 and 2009 with issues related to MEA, three recommending that specific MEA be obtained or studied.⁵²

Authorizing the use of MEA on a broader basis rather than case-by-case, with appropriate controls, could have several benefits to IRS and taxpayers. It could

- enable IRS to correct all or nearly all returns with types of noncompliance for which IRS identifies with virtual certainty the noncompliance and the needed correction, not just those it can address through other enforcement means;
- be low cost and less intrusive and burdensome to taxpayers than audits;

⁵⁰GAO, *Tax Administration: IRS's 2008 Filing Season Generally Successful Despite Challenges, although IRS Could Expand Enforcement during Returns Processing*, [GAO-09-146](#) (Washington, D.C.: Dec. 12, 2008).

⁵¹TIGTA, *Improvements Are Needed in the Administration of Education Credits and Reporting Requirements for Educational Institutions* (Washington, D.C., Sept. 30, 2009).

⁵²TIGTA, *Recovery Act: Evaluation of the Internal Revenue Service's Capability to Ensure Proper Use of Recovery Act Funds* (Washington, D.C., Nov. 27, 2009).

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- ensure that taxpayers who are noncompliant on a particular issue are more often treated alike, that is, that a greater portion of them are brought into compliance, not just those that IRS could otherwise address;
 - enhance equity between compliant and noncompliant taxpayers because a greater portion of the noncompliant ones would be brought into compliance;
 - provide a taxpayer service as it would generally allow noncompliant taxpayers to receive their refunds faster than if IRS had to address the error through some other compliance mechanism, have their returns corrected without penalty and before interest is accrued, and avoid time-consuming interaction with IRS under its other programs for resolving noncompliance;
 - help ensure taxpayers receive the tax benefits for which they are eligible by identifying taxpayers underclaiming a tax benefit;
 - free up IRS resources to pursue other forms of noncompliance; and
 - allow IRS to quickly address provisions arising from new and quickly moving initiatives like the Recovery Act without waiting for new MEA to go through the legislative process.

Broader authority to use MEA could take several forms; for instance, it could be granted for (1) new legislation that had to be implemented in short time periods, (2) newly created or revised refundable credits, or (3) wherever IRS could check for obvious noncompliance in both new legislation and already enacted laws. Refundable credits, which entail cash payments to taxpayers irrespective of the amount of their tax liabilities, are growing in popularity and automatic authority could enable IRS to monitor low-dollar amounts on individual returns that would be too labor-intensive and costly to audit.

Although broader MEA could benefit IRS and taxpayers, controls may be needed to ensure broader authority is properly used. While stating that IRS generally uses its authority properly, the IRS National Taxpayer Advocate's 2006 annual report warned of IRS's implementation of MEA impairing taxpayer rights.⁵³ The Taxpayer Advocate pointed out that in considering the 1976 legislation mentioned above, the Congress was concerned that IRS might use its authority in ways that would undermine taxpayer rights. Consequently, the Congress incorporated certain taxpayer safeguards into the legislation, such as requiring IRS to explain to the taxpayer the errors it asserted. Still, the Taxpayer Advocate was

⁵³IRS, *National Taxpayer Advocate 2006 Annual Report to Congress* (Washington, D.C., Dec. 31, 2006).

concerned that taxpayers, especially low-income taxpayers, might not proactively ask, within 60 days after being assessed tax by IRS, to have their assessment reversed by IRS, and thus might be unable to challenge an IRS notice through normal deficiency procedures or in the Tax Court. She was also concerned that MEA notices to taxpayers did not contain the type of information the Congress envisioned that clearly explained to taxpayers the nature of the error that IRS addressed through MEA.

The Taxpayer Advocate's 2002 annual report recommended that the Congress specifically limit the scope of the assessment authority for mathematical or clerical errors and provide standards by which to judge any proposed expansion of this authority.⁵⁴ The Taxpayer Advocate said that MEA should be limited to situations where there are inconsistent items and the inconsistency is determined from the face of the return; where required items, such as schedules, were omitted from the tax return; and where items on the return are numerical or quantitative.

With these or other standards in mind, the Congress could extend broader MEA to IRS but could specify criteria governing when IRS could use the authority and require other controls as well. For example, the Congress could require IRS to submit a report on a proposed new use of MEA. The report could include how such use would meet the standards or criteria outlined by the Congress. The report could also describe IRS's or the Taxpayer Advocate's assessment of any potential effect on taxpayer rights. Or, the Congress could require a more informal procedure whereby IRS simply notifies a committee, such as JCT, of its proposed use and subsequently submits a report after such use is underway. In any case, the Congress could provide IRS broader authority to use MEA than is currently authorized, but still provide appropriate safeguards by outlining criteria and guidelines and requiring IRS to report in order to alleviate concerns of improper use of MEA.

Conclusions

A year since the passage of the Recovery Act, IRS's quick implementation has allowed billions of dollars to be available to bolster the struggling U.S. economy. In the face of significant challenges posed by the Recovery Act, IRS traded off the requirements for quick implementation against the needs to collect proper data and enforce compliance with tax laws. As IRS

⁵⁴IRS, *National Taxpayer Advocate FY 2002 Annual Report to Congress* (Washington, D.C., Dec. 31, 2002).

gained experience with Recovery Act implementation, it at times substantively adjusted its approach for specific provisions. Following through on its stated intention to capture the lessons it learned from the overall experience would help IRS the next time it is charged with similar tasks. Similarly, the data-collection and enforcement framework IRS has created allows room to enhance the data it collects for BABs and to strengthen the foundation for enforcing COBRA and FTHBC provisions. In terms of the FTHBC, we are making no recommendations concerning the payback feature because late in our review IRS identified a potentially promising alternative that it expected to pursue to enforce it. This alternative will bear watching, and we look forward to IRS assessing how well it will work. Finally, receiving broader MEA, with appropriate safeguards, from the Congress would give IRS the flexibility to respond quickly as new uses emerge in the future.

Matters for Congressional Consideration

The Congress should consider the following:

- Granting IRS the authority to publicly release information on Build America Bonds (BAB), such as project purpose, beginning and ending dates, and costs; this approach would be broadly consistent with the Recovery Act reporting and transparency provisions for direct spending programs.
- Broadening IRS's ability to use math error authority (MEA), with appropriate safeguards against misuse of that authority.

Recommendations for Executive Action

We recommend the Commissioner of Internal Revenue take three actions:

- Require governmental issuers to submit additional information on Build America Bond (BAB)-financed projects, including information on project purpose, beginning and ending dates, and costs. This reporting could be similar to the bond reporting required for charitable organizations on the Schedule K of Form 990, "Supplemental Information on Tax-Exempt Bonds." Should the Congress grant the authority, IRS should publish the information in a report available to the public.
- Direct officials to conduct a compliance initiative project to determine if individuals are receiving COBRA or employers are claiming individual COBRA subsidies for longer than 15 months. IRS can use existing information to determine if significant noncompliance with the 15-month provision is apparent. If significant noncompliance is found, IRS should issue soft notices to all employers to remind them of COBRA eligibility requirements and urge them to correct errors that may have been made.

-
- Prepare a report detailing the lessons learned from its Recovery Act experiences and implementation and publish the results of its review, in line with the Recovery Act's emphasis on transparency.

Agency Comments and Our Evaluation

We received written comments on a draft of this report from the Commissioner of Internal Revenue on February 4, 2010 (for the full text of the comments, see app. V). He agreed with the benefit of one of our recommendations and agreed fully with the other two. In agreeing that IRS compliance efforts would benefit from requiring more information from issuers of Build America Bonds, he noted that the benefit would have to be balanced against the burden imposed on state and municipal governments issuing the bonds. As we said in our report, any additional cost of reporting could be tempered by having a minimum reporting threshold or delaying the onset of requirements, as was done when similar reporting for charitable organizations was instituted. The Commissioner recognized, as we had, that IRS would need statutory authority before it could make the information public. He said that if granted that authority, IRS stood ready to implement the recommendation. In agreeing with our other recommendations, the Commissioner said that IRS (1) has plans in place to do a compliance project to test the 15-month COBRA rule, and (2) will review and publish a report on lessons learned from IRS's management and implementation of the Recovery Act.

The Commissioner added that in those cases in which additional math error authority could be effectively deployed, IRS would welcome it. He said IRS looked forward to discussing the issue in more detail as the Congress considers any new tax legislation.

We also received technical comments on a draft of this report from Treasury's Acting Tax Legislative Counsel and made changes where appropriate.

We plan to send copies of this report to the Secretary of the Treasury, the Commissioner of Internal Revenue, and other interested parties. The report will also be available at no charge on GAO's Web site at www.gao.gov.

For further information regarding this report, please contact me at (202) 512-9110 or at brostekm@gao.gov. Contacts for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Individuals making key contributions to this report may be found in appendix VI.

A handwritten signature in black ink that reads "Michael Brostek". The signature is written in a cursive style with a large initial "M".

Michael Brostek
Director, Tax Issues
Strategic Issues Team

List of Addressees

The Honorable Nancy Pelosi
Speaker of the House of Representatives

The Honorable Robert C. Byrd
President Pro Tempore of the Senate

The Honorable Harry Reid
Majority Leader
United States Senate

The Honorable Mitch McConnell
Republican Leader
United States Senate

The Honorable Steny Hoyer
Majority Leader
House of Representatives

The Honorable John Boehner
Minority Leader
House of Representatives

The Honorable Daniel K. Inouye
Chairman
The Honorable Thad Cochran
Vice Chairman
Committee on Appropriations
United States Senate

The Honorable Dave Obey
Chairman
The Honorable Jerry Lewis
Ranking Member
Committee on Appropriations
House of Representatives

The Honorable Joseph I. Lieberman
Chairman
The Honorable Susan M. Collins
Ranking Member
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable Edolphus Towns
Chairman
The Honorable Darrell E. Issa
Ranking Member
Committee on Oversight and Government Reform
House of Representatives

The Honorable Max Baucus
Chairman
The Honorable Charles E. Grassley
Ranking Member
Committee on Finance
United States Senate

The Honorable Charles Rangel
Chairman
The Honorable Dave Camp
Ranking Member
Committee on Ways and Means
House of Representatives

Appendix I: Background and Requirements of Selected Provisions

The sections below provide background and describe requirements of the five provisions we selected to review in detail, as well as the Health Coverage Tax Credit (HCTC). Appendix II details our objectives, scope, and methodology, including why we selected each provision.

Build America Bonds (BAB)

BABs are taxable government bonds, with federal subsidies for a portion of the borrowing costs, that state and local governments may issue through December 31, 2010.¹ BAB subsidies can be either nonrefundable tax credits provided to holders of the bonds (tax credit BABs) or refundable tax credits paid to state and local governmental issuers of the bonds (direct payment BABs). Direct payment bonds are a new type of bond that provides state and local government issuers with a direct subsidy payment equal to 35 percent of the bond interest they pay. Because of this feature, state and local governments are able to offer the bonds to investors at a higher interest rate than they can with tax-exempt bonds. Direct payment BABs may appeal to a broader market than traditional tax-exempt bonds because a wider range of investors, such as pension funds that pay no taxes and therefore have less incentive to invest in tax-exempt bonds, are able to take advantage of them and receive a return comparable to taxable debt instruments. Tax credit BABs provide investors with a nonrefundable tax credit of 35 percent of the net bond interest payments (excluding the credit), which represents a federal subsidy to the state or local governmental issuer equal to approximately 25 percent of the total return to the investor. This subsidy is expected to make investors indifferent between the tax credit bond and a taxed bond that is otherwise similar. As a result, each dollar of federal revenue foregone for both direct payment and tax credit BABs benefits state and local governments. One hundred percent of the proceeds from BABs must be used for capital expenditures. There is no volume limitation on the amount of eligible BABs that can be issued during this period.

¹Section 1531 of Title I of Division B of the American Recovery and Reinvestment Act of 2009 (Recovery Act).

Consolidated Omnibus
Budget Reconciliation Act
(COBRA) Premium
Subsidies

COBRA was established in 1985 and provides access to health insurance for individuals who lost their employer-sponsored coverage. Before the American Recovery and Reinvestment Act of 2009 (Recovery Act),² individuals paid up to 102 percent of the total COBRA premium cost—the full cost plus a two percent administration fee—to retain their health coverage. The act provided up to 9 months of premium assistance at a lower rate to individuals who were involuntarily terminated from their jobs. The Department of Defense Appropriations Act, 2010 (Pub. L. No. 111–118) extended the duration of premium assistance from 9 months to 15 months. Individuals pay no more than 35 percent of premium costs and their former employers pay the remaining 65 percent. Employers are reimbursed for their COBRA subsidies through a tax credit against their payroll tax liability or through a tax refund if the credit exceeds their payroll tax liability. Employers file Form 941, “Employer’s Quarterly Federal Tax Return,” for a COBRA credit. In some instances, such as for state health plans that are subject to COBRA requirements, multiemployer group health plans or insurers, instead of the former employer, may provide the COBRA subsidy and file for a COBRA credit.

To be eligible for COBRA premium assistance, individuals must (1) be involuntarily terminated between September 1, 2008, and December 31, 2009 (recently extended to February 28, 2010), (2) not be eligible for another group health plan, such as Medicare or a group plan offered through a spouse’s employer, and (3) have a modified adjusted income below \$145,000, or \$290,000 if married and filing a joint tax return.

The First-Time Homebuyer
Credit (FTHBC)

The FTHBC initially was established by the Housing and Economic Recovery Act of 2008 as a tax credit equal to 10 percent of the purchase price of the principal residence, up to \$7,500, which took the form of an interest-free loan that must be paid back in \$500 increments over 15 years.³

The Recovery Act increased the maximum credit for the 2009 FTHBC to \$8,000, with no payback required unless the home ceases to be the taxpayer’s principal residence within 3 years.⁴ This \$8,000 credit is a

²Title III of Division B of the Recovery Act.

³Pub. L. No. 110-289, 122 Stat. 2654 (July 30, 2008). The 2008 FTHBC applied to purchases made between April 9, 2008, and June 30, 2009.

⁴Section 1006 of Title I of Division B of the Recovery Act.

refundable tax credit, meaning that it is paid out even if there is no tax liability. The 2009 FTHBC was enacted into law on February 17, 2009, but eligibility was made retroactive to be applied to homes purchased between January 1, 2009, and November 30, 2009.

The Worker, Homeownership, and Business Assistance Act of 2009 extended the FTHBC to home purchases made through April 30, 2010, as well as those that are under a binding contract on that date if the contract provides for closing the sale on or before June 30, 2010.⁵ The act also authorized a credit of up to \$6,500 for individuals who owned and used the same residence as their principal residence for any 5 consecutive years during the 8-year period ending when they bought another property to use as their principal residence.

The 2008 and 2009 FTHBC, as well as the 2010 credit, have complex requirements. Regarding the amount of the credit, taxpayers buying their first home can claim the smaller of

- \$7,500 for the 2008 credit and \$8,000 for the 2009 and 2010 credits, or
- 10 percent of the purchase price of the home.

Virtually all eligibility requirements for the 2008 and 2009 FTHBC are identical, as noted in table 4. However, there are differences—the primary one being the purchase date. The 2010 FTHBC contains several new requirements.

Table 4: Eligibility Requirements for the FTHBC

Eligibility requirements	2008 FTHBC	2009 FTHBC	2010 FTHBC
Date of purchase must be between April 9, 2008, and June 30, 2009	x		
Date of purchase must be between January 1, 2009, and November 30, 2009		x	
Date of purchase must be between December 1, 2009, and April 30, 2010, or it may occur after April 30, 2010 if the seller enters into a binding contract by April 30, 2010, that provides for closing on the sale before July 1, 2010. These dates are extended by a year for those who have served on qualified official extended duty outside the United States for at least 90 days between January 1, 2009, and April 30, 2010			x
Home must be principal residence ^a	x	x	x
Taxpayer must have no prior homeownership within the past 3 years	x	x	

⁵Pub. L. No. 111-92, 123 Stat. 2984 (Nov. 6, 2009). This act was generally outside the scope of our work.

Appendix I: Background and Requirements of Selected Provisions

Eligibility requirements	2008 FTHBC	2009 FTHBC	2010 FTHBC
Taxpayers must have owned and used the same residence as their principal residence for any 5 consecutive years during the 8-year period ending when they bought another property to use as their principal residence to be eligible for a reduced credit of \$6,500.			x
Home cannot be a gift or inheritance	x	x	x
Home cannot be acquired from a relative	x	x	x
Home must be located in the United States	x	x	x
Single filers:			
Modified adjusted gross income (MAGI) must be less than \$95,000. ^b			
Between \$75,000 and \$95,000 the credit phases out.	x	x	
Married filing jointly filers:			
MAGI must be less than \$170,000.			
Between \$150,000 and \$170,000 the credit phases out.	x	x	
Single filers:			
MAGI must be less than \$145,000.			
Between \$125,000 and \$145,000 the credit phases out.			x
Married filing jointly filers:			
MAGI must be less than \$245,000.			
Between \$225,000 and \$245,000 the credit phases out.			x
Taxpayer cannot be a nonresident alien	x	x	x
Taxpayer must not have been allowed to claim the District of Columbia homebuyer credit for the current or any prior tax year	x		
Home financing cannot come from tax-exempt mortgage revenue bonds	x		
Taxpayer must be at least 18 years old unless married			x
Taxpayer cannot be eligible to be claimed as a dependent on someone else's tax return			x
Taxpayer must attach a copy of the settlement statement to the tax return			x
Home price cannot exceed \$800,000			x

Source: GAO analysis of FTHBC information.

Notes: The "x" indicates if the related eligibility requirement applies to FTHBC for homes purchased in 2008, 2009, or 2010.

^aA principal residence is the main home a taxpayer lives in most of the time. It can be a house, houseboat, house trailer, cooperative apartment, condominium, or other type of residence.

^bMAGI is modified adjusted gross income (AGI), as figured on an income tax return, plus various amounts excluded from the income tax return, such as some types of foreign income that would have to be added to AGI to yield MAGI.

The Making Work Pay Credit (MWPC)

The MWPC provides up to \$400 for working individuals and \$800 for working married couples.⁶ Taxpayers may receive the credit throughout

⁶Section 1001 of Title I of Division B of the Recovery Act.

the year in the form of lower amounts of tax withheld from their paychecks. The MWPC is completely phased out for single taxpayers and for married taxpayers filing jointly with modified adjusted gross incomes (MAGI) in excess of \$95,000 and \$190,000, respectively. Taxpayers must have a Social Security number in order to claim the credit, and nonresident aliens and dependents cannot claim it.

If a taxpayer received a \$250 economic recovery payment or a \$250 government retiree credit, the MWPC is reduced by that amount. Under the Recovery Act, individuals receiving Social Security and certain other benefits were to receive a onetime payment of \$250, as were certain government retirees.

Net Operating Loss (NOL) Carrybacks

The NOL carryback provision is available to eligible small businesses—those that had a 3-year gross receipts average of no more than \$15 million—if their costs and deductions exceeded their income in 2008.⁷ It allowed these businesses to apply for a tax refund for taxes paid in up to 5 previous years. The refund is the difference between previous taxes paid and the taxes that would have been paid if the amount of the 2008 loss were deducted from past profits. The Recovery Act increased the small-business gross-receipts limit from \$5 million to \$15 million and extended the NOL carryback period for 2008 NOLs from 2 years to up to 5 years.

Health Coverage Tax Credit (HCTC)

The HCTC helps workers pay for health insurance by subsidizing part of their health insurance premium when they are between the ages of 55 and 64 and are receiving payments from the Pension Benefit Guaranty Corporation (PBGC) or they are eligible for Trade Adjustment Assistance (TAA) benefits because they lost their jobs due to international trade. Other eligibility requirements for individuals include that they not be entitled to benefits from a government health insurance program and that they be enrolled in a qualified health plan. IRS administers the HCTC program but relies on the Department of Labor and PBGC to identify that

⁷Section 1211 of Title I of Division B of the Recovery Act. The Worker, Homeownership, and Business Assistance Act of 2009, mentioned earlier, revised the NOL carryback provision by extending the NOLs qualifying for the 5-year carryback period to those occurring in 2009 and expanding the provision to include all taxpayers, except for those that received funds under the Troubled Asset Relief Program. Refunds issued for the 5th year are limited to 50 percent of a taxpayer's taxable income for that year, with an exception for 2008 small-business losses. This revision was generally outside the scope of our work.

workers are potentially eligible for the credit. The HCTC can be claimed on a yearly basis on an individual's tax return or taxpayers can choose to have advance payments sent to their health plans on a monthly basis as health insurance premiums are due.

The Recovery Act made several changes to the HCTC, effective until December 31, 2010, including the following.⁸ First, it increased the health insurance premium subsidy rate from 65 percent of premiums to 80 percent. Second, it allowed taxpayers to be reimbursed for payments they made to their health plans when they were eligible for, but not yet enrolled in, the HCTC program. Third, it allowed family members of HCTC recipients to continue to receive coverage for up to 2 years if the qualified taxpayer becomes eligible for Medicare, the taxpayer and the spouse divorce, or the taxpayer dies. Fourth, it added a new qualified health insurance plan—one funded by a voluntary employees' beneficiary association. Other changes that do not expire but will need to be reauthorized in 2010 include broadening eligibility for the TAA program to include service sector and public agency workers and requiring the Department of the Treasury to conduct a biennial survey of HCTC-eligible individuals.

⁸The Trade Adjustment Assistance Health Coverage Improvement Act, sections 1899A-1899L of Title I of Division B of the Recovery Act. IRS is responsible for administering sections 1899A-1899J.

Appendix II: Objectives, Scope, and Methodology

Our objectives were to (1) describe the status of the Internal Revenue Service's (IRS) implementation of American Recovery and Reinvestment Act of 2009 (Recovery Act) tax provisions; (2) analyze IRS plans to collect data on the provisions, examine whether and how IRS captured data on the use of selected provisions, and discuss the provisions' overall effect; (3) assess IRS's efforts to determine potential abuse of the provisions and IRS's steps for minimizing it; and (4) discuss possible lessons learned for future tax administration.

To address the first objective, we identified from IRS documents implementation steps taken and planned for each of the 54 Recovery Act provisions that IRS had a role in administering. We focused on education and outreach, guidance and instruction, and processing and programming activities because they were part of a framework that IRS used to implement Recovery Act tax provisions.

To further address this objective as well as others, we selected five Recovery Act tax provisions to review in detail—Build America Bonds (BAB), Consolidated Omnibus Budget Reconciliation Act (COBRA) premium subsidies, the First-Time Homebuyer Credit (FTHBC), the Making Work Pay Credit (MWPC), and net operating loss (NOL) carrybacks. We also reviewed the Health Coverage Tax Credit (HCTC), but our analysis of the HCTC was limited to data-collection issues because we are doing a separate review of the HCTC, which is due in March 2010, as mandated by the Recovery Act.

We chose the five provisions to review in detail using the following four criteria:

- Year of implementation. By choosing provisions being implemented in 2009, we could study how IRS's forms, guidance, systems, and processes were used to implement change relatively quickly. In addition, more reliable data would be available than for provisions that could not be claimed until the future.
- Estimated revenue loss. We chose estimated revenue loss as another criterion to make sure we included provisions estimated to have a large effect on revenue. We were interested in whether a provision's estimated revenue loss was among the largest of the 54 provisions. The six provisions we selected had total estimated revenue losses of about \$153 billion over the period from fiscal year 2009 through fiscal year 2011, almost half the estimated losses for all 54 provisions.
- Refundable components. We chose refundability as a third criterion because IRS has frequently noted that refundable tax provisions are more

susceptible to abuse than other tax provisions. Further, when IRS actually refunds money to taxpayers, recouping it can be difficult if the monies were paid erroneously.

- Coverage. As shown earlier in table 1, IRS grouped Recovery Act provisions into the following categories: individual tax credits, tax incentives for business, renewable energy, various bond incentives, health coverage improvement, and COBRA. We chose coverage as a fourth criterion in order to ensure that we considered at least one provision from most of the IRS categories. We did not select provisions from the Renewable Energy group because none of them was being implemented in 2009. We selected the BAB and NOL carryback provisions in spite of their relatively small dollar estimates to achieve wider coverage of IRS categories.

Table 5 summarizes how the five provisions we selected for further study addressed these criteria and also shows how the HCTC relates to the criteria.

Table 5: Characteristics of the Five Provisions GAO Selected for Analysis Plus the HCTC

	Criterion 1	Criterion 2	Criterion 3	Criterion 4	
Provision	Was the provision being implemented in 2009?	Was the provision's estimated revenue cost for fiscal years 2009 through 2019 among the 10 largest of the 54 provisions?	What was the estimated revenue cost for that period? (dollars in millions)	Did the provision have a refundable feature?	In what IRS category was the provision?
BAB	Yes	No	\$4,348	Yes	Various bond incentives
COBRA	Yes	Yes	24,677	Yes	COBRA provision
FTHBC	Yes	Yes	6,638	Yes	Individual credits
MWPC	Yes	Yes	116,199	Yes	Individual credits
NOL carryback	Yes	No	947	No	Business incentives
HCTC	Yes	No	457	Yes	Health coverage improvement

Source: GAO analysis of IRS and Joint Committee on Taxation information.

For the second objective, dealing with IRS's collection of data on the Recovery Act provisions, we analyzed IRS planning documents for collecting data for the 54 provisions. For the 5 selected provisions and the HCTC, we analyzed whether IRS would be able to identify provision users

and the extent of use. To see how these data could relate to estimating IRS's Recovery Act provisions' effect on the overall economy, we consulted with GAO economics experts, including the Chief Economist's office, and studied Council of Economic Advisers (CEA) and Congressional Budget Office (CBO) reports.

To meet the third objective, relating to the potential abuse of provisions, we determined what risk assessments and risk-mitigation plans IRS had done or planned for the future and discussed them with IRS and Department of the Treasury officials. We also assessed IRS's risk-management efforts against GAO and other published criteria on mitigating abusive noncompliance. For the five selected provisions, we examined the potential for abuse by reviewing IRS documentation and risk assessments and interviewing Treasury Inspector General for Tax Administration (TIGTA) and IRS officials.

We used the results of our work and TIGTA's to answer our fourth objective—discussing possible lessons learned for future tax administration. We interviewed responsible IRS officials to obtain their views on these observations.

We found the IRS data we used reliable for the purposes of this report. We determined this after interviewing IRS and, where appropriate, TIGTA officials, and reviewing various TIGTA reports.

We conducted this performance audit from June 2009 through February 2010 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix III: The 54 Recovery Act Tax Provisions That IRS Has a Role in Administering

Table 6 details information about the 54 American Recovery and Reinvestment Act of 2009 (Recovery Act) provisions that the Internal Revenue Service (IRS) has a role in administering.

Table 6: Information about the 54 Recovery Act Provisions That IRS Has a Role in Administering

Provision number	Short provision name	Original expiration date ^a	Refundable ^b	IRS category	Total Joint Committee on Taxation (JCT) estimated revenue cost from fiscal year 2009 through fiscal year 2019 (dollars in millions)
1001	Making Work Pay Credit	2010	X	Individual credits	\$116,199
1002	Increase in Earned Income Tax Credit	2010	X	Individual credits	4,663
1003	Increase in Child Tax Credit	2010	X	Individual credits	14,830
1004	American Opportunity Tax Credit	2010	X	Individual credits	13,907
1005	Computer equipment allowed as education expense	2010		Individual credits	6
1006	First-Time Home Buyer Credit	2009	X	Individual credits	6,638
1007	Suspension of tax on portion of unemployment compensation	2009		Individual credits	4,740
1008	Deduction for state sales tax on the purchase of new car	2009		Individual credits	1,684
1011	Increase alternative minimum tax (AMT) relief for nonrefundable credits	2009		Individual credits	69,759
1012	Extension of increased AMT exemption amount	2009		Individual credits	0
1101	Extend credit for renewable energy resources	2013		Energy incentives	13,143
1102	Election of investment credit in lieu of production tax credits	2013		Energy incentives	285
1103	Repeal of certain limitations on credit for renewable energy property	n.a.		Energy incentives	604
1104	Coordination with renewable energy grants	2010		Energy incentives	No revenue effect
1111	New clean renewable energy bonds	n.a.		Bond incentives	578
1112	Qualified energy conservation bonds	n.a.		Bond incentives	803
1121	Extension and modification of credit for nonbusiness energy property	2010		Energy incentives	2,034
1122	Modification of credit for residential energy-efficient property	n.a.		Energy incentives	268
1123	Increase in credit for alternative fuel vehicle refueling property	2010		Energy incentives	54

Appendix III: The 54 Recovery Act Tax Provisions That IRS Has a Role in Administering

Provision number	Short provision name	Original expiration date^a	Refundable^b	IRS category	Total Joint Committee on Taxation (JCT) estimated revenue cost from fiscal year 2009 through fiscal year 2019 (dollars in millions)
1131	Application of monitoring requirement for carbon dioxide	n.a.		Energy incentives	No revenue effect
1141	Credit for qualified plug-in electric-drive motor vehicles	n.a.		Energy incentives	2,002
1142	Credit for certain plug-in electric vehicles	2011		Energy incentives	0
1143	Conversion kits	2011		Energy incentives	No revenue effect
1144	Treatment of alternative motor vehicle credit as a personal credit allowed against AMT	n.a.		Energy incentives	No revenue effect
1151	Increased exclusion amount for commuter transit benefits and passes	2010		Energy incentives	192
1201	Special allowance for property acquired during 2009	2010		Business incentives	5,879
1202	Temporary increase in limitations on expensing of certain depreciable business assets	2009		Business incentives	41
1211	5-year carryback of 2008 net operating losses (NOL)	2008		Business incentives	947
1212	Decreased required estimated tax payments for small businesses in 2009	2009		Business incentives	0
1221	Modify the Work Opportunity Tax Credit	2010		Business incentives	231
1231	Allow deferral of income from cancellation of indebtedness	2010		Business incentives	1,622
1232	Modification of rules for original issue discount	n.a.		Business incentives	No revenue effect
1241	Increase exclusion for qualified small business stock	2010		Business incentives	829
1251	Reduction of recognition period for S corporation built-in gain	2010		Business incentives	415
1261	Clarify regulations related to limitations on built-in losses	2009		Business incentives	-6,977 ^c
1262	Treatment of change of ownership of automaker for NOLs	n.a.		Business incentives	3,163
1301	Industrial Development Bonds	2010		Bond incentives	203
1302	Energy Investment Credit	2011		Energy incentives	1,647
1401	Recovery Zone Bonds	2010	X	Bond incentives	5,371

Appendix III: The 54 Recovery Act Tax Provisions That IRS Has a Role in Administering

Provision number	Short provision name	Original expiration date^a	Refundable^b	IRS category	Total Joint Committee on Taxation (JCT) estimated revenue cost from fiscal year 2009 through fiscal year 2019 (dollars in millions)
1402	Tribal Economic Development Bonds	n.a.		Bond incentives	315
1501	De minimis safe harbor exemption	2010		Bond incentives	3,234
1502	Modification of small-issuer exception	2010		Bond incentives	No revenue effect
1503	Temporary modification of AMT limitation on tax-exempt bonds	2010		Bond incentives	555
1504	Modification to High Speed Intercity Rail Facility Bonds	n.a.		Bond incentives	288
1511	Delay in application of withholding tax on government contractors	2011		Withholding on government contractors	291
1521	Qualified school construction bonds	2010		Bond incentives	9,877
1522	Qualified zone academy bonds	2010		Bond incentives	1,045
1531	Build America Bonds	2010	X	Bond incentives	4,348
1541	Regulated investment companies allow to pass-thru tax credit bonds	n.a.		Bond incentives	0
1601	Application of certain labor standards for projects financed with certain bonds	n.a.		Bond incentives	No revenue effect
2201	Economic Recovery Payments	2009		Individual credits	14,225
2202	Economic Recovery Payments for government retirees	2009		Individual credits	218
3001	Consolidated Omnibus Budget Reconciliation Act (COBRA)	2009	X	COBRA	24,677
1899 A-J	Health Coverage Tax Credit	2010	X	Health coverage improvement	457
Total					\$325,290

Source: GAO analysis of IRS and JCT data.

^aThe expiration date is defined as the last year for which the benefit can be claimed or the qualifying purchase or event must occur. The notation n.a., not applicable, indicates that no expiration date exists. An example of a provision without an expiration date is bonds that have volume limits, but not date limits. Original expiration dates are cited, but some provisions have already been extended, such as the provision 1006, the First-Time Homebuyer Credit. This provision was also revised as part of the extension.

^bAn X denotes that the provision has a refundable feature.

^cThis provision generates revenue.

Appendix IV: IRS Data Collected on Four Tax Provisions in the Recovery Act

The Internal Revenue Service (IRS) collected and internally circulated data on the use of three of the five provisions we focused on in our review, plus the Health Coverage Tax Credit (HCTC). Treasury released limited data to the public, but data on the individual provisions' use was not posted on recovery.gov, the administration's official Web site for monitoring the American Recovery and Reinvestment Act of 2009 (Recovery Act). As shown in tables 7 through 10, respectively, and in figure 3, these provisions were (1) Build America Bonds (BAB), (2) Consolidated Omnibus Budget Reconciliation Act (COBRA) premium subsidies, (3) the First-Time Homebuyer Credit (FTHBC), and (4) the HCTC. IRS has plans to collect data on other provisions in the future, as noted in table 2. For example, IRS plans to report data on the Making Work Pay Credit (MWPC) in April 2010.¹

Table 7: Recent Selected IRS Data Collected on BABs

Data category	Amount
Number of information returns showing BAB issuances ^a	443
Dollar value of associated issuances ^b (in billions)	32.4
Number of returns requesting a BAB direct payment ^c	140
Number of returns requesting a BAB tax credit ^d	0

Source: IRS.

Note: Data on the number of information returns showing BAB issuances and the dollar value of associated issuances are as of January 1, 2010. Information on the number of returns requesting a BAB direct payment is as of November 14, 2009.

^aThe number of filings of Form 8038-G, "Information Return for Tax-Exempt Government Obligations," which notifies IRS of a BAB issue.

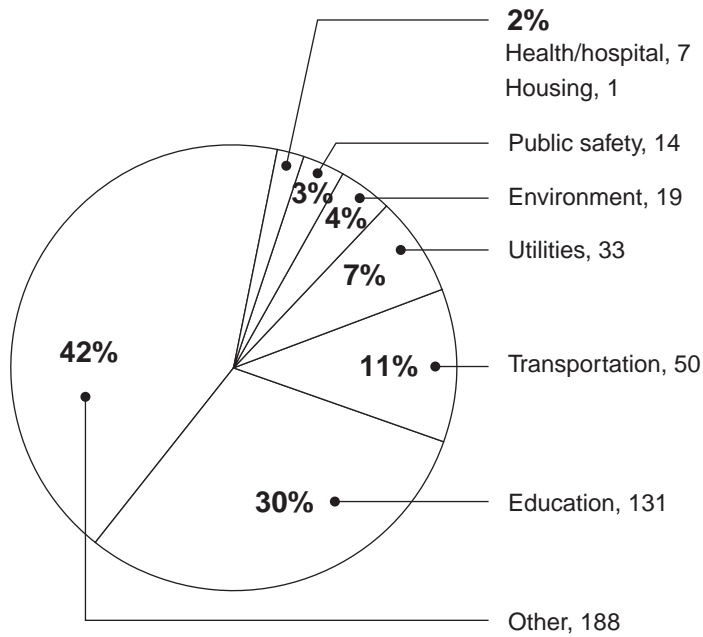
^bThe dollar value of all BABs issued and reported on Form 8038-G.

^cThe number of filings of Form 8038-CP, "Return for Credit Payments for Issuers of Qualified Bonds," which requests a BAB direct payment.

^dThe number of filings of Form 8912, "Credit to Holders of Tax Credit Bonds," which requests a BAB tax credit.

¹To accelerate the delivery of the credit, IRS issued new withholding tables that reduce federal tax withholding. However, IRS does not know how many employers used the new tables.

Figure 3: Number of BAB Issuances by Type of Issue as of January 1, 2010



Source: IRS.

Note: Percentages do not add to 100 percent due to rounding.

Table 8: Recent Selected IRS Data Collected on COBRA

Data category	Amount
Number of returns claiming a COBRA credit ^a	191,618
Number of employees receiving benefits ^b	Not yet available
Amount of credits claimed (dollars in millions) ^c	\$803
Amount of outlays made (dollars in millions) ^d	\$254

Source: IRS.

Notes: Information on the number of returns claiming a COBRA credit is as of December 26, 2009. Data on the amount of credits claimed and the amount of outlays made are as of November 14, 2009.

^aThe number of employer filings of Form 941 with claims for the COBRA subsidy.

^bThe number of employees for which COBRA premium assistance was provided.

^cThe dollar value of all COBRA subsidy claims.

^dThe dollar value of COBRA subsidy claims that resulted in a tax refund to employers.

Appendix IV: IRS Data Collected on Four Tax Provisions in the Recovery Act

Table 9: Selected IRS Data Collected on the FTHBC through November 21, 2009

Data category	2008	2009
Number of filers claiming the FTHBC	1,068,253	630,045
Amount of credits claimed (dollars in billions)	\$7.3	\$4.7

Source: IRS.

Note: While combined 2008 and 2009 data appear reliable, some concerns exist about the reliability of each year's data. In a group of 47,276 electronically filed returns that appeared not to have claimed the whole FTHBC, the Treasury Inspector General for Tax Administration (TIGTA) found that 93 percent, or 43,967, were not coded as a 2009 FTHBC even though the purchase had occurred in 2009. It is likely that the errors are a result of (1) taxpayers who purchased a house in 2009 prior to the passage of the Recovery Act and claimed the 2008 credit, when, in fact, they are eligible for the expanded benefits of the 2009 credit; and (2) IRS's not properly coding the purchase date as a 2009 FTHBC on some returns. IRS had plans to monitor instances where taxpayers claimed the 2008 instead of the 2009 credit. When those taxpayers did not file an amended return, IRS had plans to notify them of their eligibility for the expanded benefits of the 2009 credit. According to IRS officials, IRS planned to correct the other errors when it began enforcing the 2008 FTHBC payback provisions. At that time, IRS planned to verify the date of purchase and make any adjustments.

Table 10: Selected IRS Data Collected on the HCTC through November 2009

Data category	Amount
Number of new enrollees ^a	12,116
Payments to enrollees ^b (dollars in millions)	\$26.2

Source: IRS.

^aFor April 2009 through August 2009, the monthly number of new enrollees was roughly 1,000, ranging between 1,066 and 1,420. In September 2009, October 2009, and November 2009, the numbers rose to 1,930, 2,494, and 1,624 respectively.

^bThe payments include not only amounts for new enrollees but also incremental amounts for current participants because those already enrolled had the percentage of their health insurance costs covered by the HCTC increased from 65 percent to 80 percent.

Appendix V: Comments from the Internal Revenue Service



COMMISSIONER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

February 4, 2010

Mr. Michael Brostek
Director, Tax Issues
Strategic issues Team
U.S. Government Accountability Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Brostek:

I am writing in response to your report entitled *Recovery Act - IRS Quickly Implemented Tax Provisions, but Reporting and Enforcement Improvements are Needed*. I appreciate the GAO's valuable work and feedback on the IRS's implementation of the tax provisions of the American Recovery and Reinvestment Act of 2009. I appreciate that the report recognizes that the IRS moved quickly to implement the provisions of the Recovery Act, and delivered much needed support to families and businesses struggling in a challenging economy.

Providing the public with detailed information on how Recovery Act tax dollars were used is a top priority for the IRS. The Administration developed a comprehensive plan to report on the tax credits claimed and the accrual of other benefits provided in the tax provisions of the Recovery Act. I agree with your conclusion that increased information reporting for Build America Bonds would aid IRS compliance efforts. Should Congress choose to pass the legislation needed for us to act on this recommendation, we stand ready to implement.

At the same time that we were conducting outreach to maximize participation in Recovery Act programs, we designed and implemented a series of programs to minimize errors and fraud in claiming Recovery Act benefits. I agree with your assessment that opportunities exist to improve compliance efforts, and the IRS is committed to a focused, multi-year effort to adapt and enhance our compliance programs as these programs evolve. The GAO's continued input will be very helpful as we further refine our strategy.

Finally, as your report notes, increased "math error" authority often provides the IRS with an efficient means of improving compliance while carrying with it the responsibility

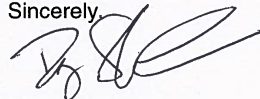
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to protect taxpayer rights. In those cases where this additional authority could be effectively deployed, the IRS would welcome it. As Congress considers any new tax legislation, we will look forward to discussing this issue in more detail.

A separate enclosure specifically addresses each of your recommendations.

If you have any questions, or if you would like to discuss this response in more detail, please contact Frederick W. Schindler, Recovery Act Accountable Official, at (202) 283-7650.

Sincerely,



Douglas H. Shulman

Enclosure

Enclosure

GAO Recommendations and IRS Responses to
GAO Draft Report Recovery Act: IRS Quickly Implemented Tax Provisions, but
Reporting and Enforcement Improvements Are Needed

Recommendation:

Require governmental issuers to submit additional information on Build America Bond (BAB) – financed projects, including information on project purpose, beginning and ending dates, and costs. This reporting could be similar to the bond reporting required for tax-exempt organizations on the Schedule K of Form 990, “Supplemental Information on Tax-Exempt Bonds”. Should Congress grant the authority, IRS should publish the information in a report available to the public.

Comment:

We agree that requiring additional information from issuers of Build America Bonds would aid the Service’s compliance efforts. That benefit, however, must be balanced against the burden that the reporting of this information would impose on State and municipal governments that issue Build America Bonds. Further, the Service would need specific statutory authority before it could make public Build America Bond return information.

Recommendation:

Direct officials to conduct a compliance initiative project to determine if individuals are receiving COBRA or employers are claiming individual COBRA subsidies for longer than 15 months. If significant noncompliance is found in the sample, IRS should issue soft notices to all employers to remind them of COBRA eligibility requirements and urge them to correct errors that may have been made.

Comment: We agree with the recommendation and have plans in place to conduct a compliance project to test the 15 month rule.

Recommendation:

Prepare a report detailing the lessons learned from its Recovery Act experiences and implementation and publish the results of its review, in line with the Recovery Act’s emphasis on transparency.

Comment:

We agree with this recommendation and will review the management and implementation of ARRA 2009, evaluating the work accomplished by all IRS divisions supporting the effort and capturing the lessons learned. This report will then be published, in line with the Recovery Act’s emphasis on transparency.

Appendix VI: GAO Contact and Staff Acknowledgments

GAO Contact

Michael Brostek, (202) 512-9110, brostekm@gao.gov

Staff Acknowledgments

In addition to the contact named above, Libby Mixon, Assistant Director; Amy R. Bowser; Gerardine Brennan; Sherwin D. Chapman; Andrea S. Clark; William J. Cordrey; Mary C. Coyle; John E. Dicken; Rachel E. Dunsmoor; Shirley A. Jones; Lawrence M. Korb; Susan E. Offutt; John G. Smale, Jr.; Steven J. Sebastian; and Anne O. Stevens made key contributions to this report.

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