

TAS Research and Related Studies

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Study of Subsequent Compliance of Taxpayers Who Received Educational Letters From the National Taxpayer Advocate

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EXECUTIVE SUMMARY

This study expands upon two studies, described in the National Taxpayer Advocate's 2016 and 2017 Annual Reports to Congress, of taxpayers who received educational letters from the National Taxpayer Advocate in January 2016 or January 2017.¹ The National Taxpayer Advocate sent the letters to taxpayers who appeared to have claimed the Earned Income Tax Credit (EITC) in error because they did not meet the relationship or residency requirements, or another taxpayer claimed EITC with respect to the same child. The letters explained the requirements for claiming EITC with respect to a qualifying child and advised which requirement the taxpayer did not appear to meet.

In 2017, a separate group of taxpayers who appeared to have claimed EITC without meeting the residency test received a letter that included an extra help phone number the taxpayer could call to speak with a Taxpayer Advocate Service (TAS) employee about his or her eligibility for EITC. This study considers the effect of the TAS letters on taxpayers' compliance in claiming EITC in the years following the year in which they received TAS's letter.

Among this year's study findings:

- Where the error consisted of not meeting the relationship test, the TAS letter enhanced compliance for all three years following the year the taxpayer received the letter; and
- Where the error consisted of not meeting the residency test, the TAS letter that included an extra help phone number enhanced compliance for both years following the year the taxpayer received the letter.²

INTRODUCTION

Internal Revenue Code (IRC) § 32 provides for the EITC, a refundable credit available to low-income workers and families. During 2019, 25 million eligible workers and families received about \$61 billion in EITC.³ The amount of EITC available is a function not only of a taxpayer's earned income but also the number of "qualifying children" in the household.⁴ A "qualifying child" is a person who, among other things, meets age requirements, bears a specified relationship to the taxpayer, and has the same principal residence as the taxpayer for more than half the year.⁵ Taxpayers usually receive EITC with respect to qualifying children, although taxpayers who did not have a qualifying child accounted for nearly 25 percent of all 2018 tax returns claiming EITC that the IRS processed in 2019.⁶

- 1 National Taxpayer Advocate 2016 Annual Report to Congress vol. 2, 32-52 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*); National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 15-39 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently in Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC*). The statistical information in this research study was not provided or reviewed by the Secretary under IRC § 6108(d). See IRC § 7803(c)(2)(B)(ii)(XII).
- 2 As discussed below, the TAS letter with the extra help phone number was sent for the first time as part of the 2017 study. Thus, we had data about the effect of this letter for only two years following the year in which it was sent. As discussed below, very few — 35 — taxpayers actually called the extra help phone number and spoke to a TAS employee.
- 3 IRS, EITC Fast Facts, <https://www.eitc.irs.gov/partner-toolkit/basic-marketing-communication-materials/eitc-fast-facts/eitc-fast-facts> (Nov. 18, 2019).
- 4 IRC § 32(c)(1) sets out the definition of "eligible individual" and IRC § 32(b) contains the calculation of the amount of allowable credit.
- 5 IRC §§ 32(c)(3); 152(c).
- 6 IRS, Compliance Data Warehouse (CDW), Individual Returns Transaction File (IRTF) as of 2019 cycle 26.

The IRS generally selects returns that claim EITC for audit using the Dependent Database (DDb) workload selection tool. The DDb combines data from IRS and third-party sources, compares returns against this data, and scores returns for the probability of noncompliance, using filters for characteristics that are strong indicators of noncompliance.⁷

Of the returns filed for tax year 2018 on which EITC was claimed, DDb identified over 6.5 million returns as potentially noncompliant, including over 1.4 million returns that broke a DDb rule because the child claimed for EITC purposes appeared to not meet the residency or relationship rules for claiming EITC, or more than one taxpayer claimed the same qualifying child.⁸ However, the IRS only has the resources to audit a fraction of these EITC claims that appear to be erroneous. EITC has an improper payment rate of about a quarter of the EITC dollars disbursed by the IRS.⁹

BACKGROUND

For the 2016 study, TAS identified a representative sample of taxpayers who were not audited but who, according to the DDb, erroneously claimed EITC on their tax year 2014 returns. The error consisted of claiming EITC with respect to a qualifying child when:

- The relationship test did not appear to have been met;
- The residency test did not appear to have been met; or
- Another taxpayer claimed EITC with respect to the same child (*i.e.*, there were duplicate claims).¹⁰

In January 2016, before tax year 2015 returns were due, the National Taxpayer Advocate sent taxpayers in the sample a letter that explained the requirements for claiming EITC and identified the error the taxpayers appeared to have made on their 2014 returns.

TAS then studied the extent to which taxpayers who received the TAS letter properly claimed EITC on their tax year 2015 returns, compared to two groups:

- A representative sample of unaudited taxpayers who also appeared to have claimed EITC in error on their 2014 returns for one of the same three reasons (the relationship or residency tests were not met, or there was a duplicate claim), but who were not sent a TAS letter (*i.e.*, the control group); and
- A representative sample of taxpayers who appeared to have claimed EITC in error on their 2014 returns for one of the same three reasons, and whose 2014 return was audited.¹¹

For the 2017 study, TAS identified a representative sample of taxpayers who were not audited but who, according to the DDb, erroneously claimed EITC on their tax year 2015 returns for one of the same

7 See Department of the Treasury, *Report to Congress on Strengthening Earned Income Tax Credit Compliance through Data Driven Analysis 14* (July 5, 2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/Report-EITC-Data-Driven-Compliance-2016.pdf>.

8 Data is from a Business Object interface with the DDb, showing returns claiming EITC scored by the DDb.

9 See, e.g., Department of Treasury, *Agency Financial Report (AFR) Fiscal Year (FY) 2018* at 194 (Nov. 2018), estimating an EITC improper payment rate of 25.06 percent.

10 National Taxpayer Advocate 2016 Annual Report to Congress vol. 2, at 32 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*).

11 Audited taxpayers were not sent TAS letters. Taxpayers whose TAS letters were returned as undeliverable, or were deceased, were excluded from the samples.

three reasons (failing to meet the relationship or residency tests, or the existence of a duplicate claim).¹² In January 2017, before tax year 2016 returns were due, the National Taxpayer Advocate sent these taxpayers educational letters that were similar to the previous year's letters. Part of the purpose of the study was to corroborate the findings of the prior year study, which primarily showed a statistically valid increase in compliance among the group of taxpayers who had received a TAS letter after apparently violating DDb *relationship* rules.

In addition, in January 2017, TAS sent a separate letter to a group of unaudited taxpayers who appeared to have erroneously claimed EITC on their 2015 returns because the *residency* test was not met.¹³ The letter to this group was the same as the letter sent to other taxpayers who claimed EITC without appearing to have met the residency test, except that this letter included a toll-free number taxpayers could call to speak to a TAS employee about their eligibility for EITC.

TAS then studied the extent to which taxpayers who received the TAS letter (including the letter with the extra help phone line sent to taxpayers who appeared not to meet the residency test) properly claimed EITC on their tax year 2016 returns, compared to two groups:

- A representative sample of unaudited taxpayers who also appeared to have claimed EITC on their 2016 returns in error for one of the same three reasons (the relationship or residency tests were not met, or there was a duplicate claim) but who were not sent a TAS letter (*i.e.*, the control group); and
- A representative sample of taxpayers who appeared to have claimed EITC in error on their 2015 returns for one of the same three reasons, and the 2015 returns had been audited.¹⁴

Among other things, the 2016 and 2017 studies showed that taxpayers' improved compliance behavior depended on the type of DDb rule that was broken. The TAS letter was particularly effective in averting erroneous EITC claims where the apparent error was that the relationship test had not been met. For example, both reports found that sending the TAS letter to all taxpayers whose returns appeared to be erroneous because the relationship test was not met would have averted about \$50 million of erroneous EITC claims.¹⁵

The 2017 study also showed that the TAS letter was effective in averting erroneous claims where the residency test appeared not to have been met, but only where the letter included the additional phone

12 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, at 15 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC*).

13 All of the TAS letters sent in 2017 also reminded taxpayers they could be eligible for EITC even if they did not have a qualifying child. The 2017 study found that some taxpayers who received the TAS letter claimed the childless-worker credit more frequently on their 2016 returns than they had on their 2015 returns. National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 32-33 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC*). For the 2019 study, we did not explore the extent to which recipients of a TAS letter claimed the childless-worker EITC in the following years.

14 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 15-39 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC*).

15 National Taxpayer Advocate 2016 Annual Report to Congress vol. 2, at 32 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Sent an Educational Letter From the National Taxpayer Advocate*), reporting that \$47 million of these erroneous claims could have been averted.

number. The 2017 study found that sending that letter to all taxpayers whose 2015 returns appeared to be erroneous because the residency test was not met would have averted more than \$44 million of erroneous EITC claims.¹⁶

In 2019, we studied the effect of the previous years' letters on the same taxpayers' compliance with respect to claiming EITC. Specifically, we studied whether the 2016 TAS letter continued to be effective by analyzing returns the recipients filed for the following three tax years — 2016, 2017, and 2018. We studied whether the 2017 TAS letters continued to be effective by analyzing the returns the recipients filed for the following two tax years — 2017 and 2018.

RESEARCH QUESTIONS

1. **Whether the tax returns filed by recipients of TAS letters were more compliant, in terms of claiming EITC in the following two or three years, compared to:**
 - a. **Tax returns filed by unaudited taxpayers who were not sent a TAS letter (i.e., taxpayers in the control group); and**
 - b. **Tax returns filed by taxpayers who were audited; and**
2. **Whether compliance in later years depended on whether the error the TAS letter identified was:**
 - a. **Not meeting the relationship test;**
 - b. **Not meeting the residency test; or**
 - c. **The existence of a duplicate claim.**

METHODOLOGY

As described above, TAS began testing the effect of issuing an educational letter to taxpayers whose returns broke only one of three DDb rules (i.e., the relationship or residency tests were not met, or there was a duplicate claim). Specifically, for both of the prior studies, TAS selected, for each type of rule break, a representative sample of approximately 2,400 taxpayers whose returns were unaudited but had broken the corresponding DDb rule for a total sample selection of about 7,200 returns. For the 2017 study, in addition to these sample groups, we selected a representative sample of approximately 1,200 taxpayers who appeared to not meet the residency test to whom we sent a letter that contained an additional help phone number, for a total sample selection of about 8,400 returns. Each of the three sample groups were mailed a letter, corresponding to the specific DDb rule break issue, which provided a plain summary of the EITC eligibility rule the taxpayer appeared to have not met.

A comparable control group of about twice the size of the sample groups was also selected for each of the three types of DDb rule breaks. Finally, three groups of audited taxpayers with corresponding

16 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, at 24 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC*), reporting that \$53 million of these erroneous claims could have been averted.

characteristics were also selected to compare to both the group receiving the TAS letters and the control group.¹⁷

TAS had hoped to continue testing these letters on a sample of taxpayers who violated DDb rules in tax year 2016; however, TAS was unable to send the letters prior to the beginning of the filing season for tax year 2017 returns. A 2018 government shutdown prevented TAS from sending similar letters the following year in 2019 in time for the filing season for tax year 2018 returns.

This study uses the same sample taxpayers from the two prior studies and explores the EITC compliance of these taxpayers in the subsequent tax years. We examined subsequent EITC compliance for each of the tax years due after the year in which TAS mailed the initial study letter.

We analyzed the data in terms of the number of tax years that elapsed from receipt of the TAS letter until the taxpayer filed a return. Where possible, for each type of rule break we combined the data about the three groups of taxpayers who were part of the first TAS study (in 2016) with data about the three groups of taxpayers who were part of the second TAS study (in 2017). For example:

- To analyze compliance one year after receipt of the TAS letters, we combined the data about tax year 2016 returns filed by taxpayers who were part of the first TAS study with data about tax year 2017 returns filed by taxpayers who were part of the second TAS study; and
- To analyze compliance two years after receipt of the TAS letters, we combined the data about tax year 2017 returns filed by taxpayers who were part of the first TAS study with data about tax year 2018 returns filed by taxpayers who were part of the second TAS study.¹⁸

This study reports on the percentage of taxpayers in the test, control, and audit groups who broke *any* DDb rule and who broke *the same* DDB rule for taxpayers in the residency and relationship groups. We separately discuss the subsequent compliance of taxpayers who broke a residency rule and received an educational letter with a telephone number to call for more assistance. We provide the percentages of taxpayers who filed returns with any DDb rule breaks as well as the percentages that filed returns with the same DDb rule break identified in the TAS letter.

Unless otherwise noted, all findings are statistically significant at the 95 percent confidence level.¹⁹ Because so few taxpayers continued to make duplicate claims in subsequent years, we do not provide detailed findings on the subsequent compliance of taxpayer with duplicate dependent DDb rule breaks.

17 For a detailed description of the methodology adopted in the earlier studies, see National Taxpayer Advocate 2016 Annual Report to Congress vol. 2, at 36 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*); National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, at 19 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC*).

18 The tax year 2018 returns we analyzed in this study were those filed by cycle 26 of 2019, which is approximately the end of June 2019.

19 We did not attempt to determine statistical significance for the data shown in Figures 4.1.2 and 4.1.4, pertaining to the reduction in noncompliance within each group over the three year period.

DATA COLLECTION

TAS Research reviewed IRS records to determine how many taxpayers who received a TAS letter filed a return for 2016, 2017, and 2018 and claimed EITC with respect to a child.

The prior TAS EITC educational letter studies only analyzed the taxpayers' level of compliance for the return that was due shortly after TAS mailed the educational letter. This study quantifies the EITC compliance of these same taxpayers for tax returns due in the years after TAS mailed the educational letter. For each return these taxpayers filed in the years after the taxpayer received the TAS educational letter, TAS researched:

- How many taxpayers appeared to have claimed EITC erroneously because the return broke a DDb rule including relationship or residency rules, or was a duplicate claim; and
- Of the returns that broke a DDb rule, how many appeared to break the same DDb rule as that identified in the TAS letter.

TAS Research collected the same information about taxpayers:

- Who broke the same DDb rules in the same year as those who received the TAS letter, but who were not sent a TAS letter and were not audited (*i.e.*, the control group); and
- Who broke the same DDb rules in the same years as those who received the TAS letter, and who were audited.

FINDINGS

1. In All Three Years Following the Year in Which a TAS Letter Advised That the EITC Claim Appeared Erroneous Because the Relationship Test Had Not Been Met, Taxpayers Who Received the Letters Filed Returns That Were More Compliant Than the Returns of Taxpayers in the Control Group

As discussed above, some taxpayers received a TAS letter advising them that they apparently erred in claiming EITC because the relationship test had not been met. Some taxpayers received the letter in 2016 and some in 2017. There were 2,202 taxpayers in this group in the 2016 study and 2,309 taxpayers in this group in the 2017 study. The combined results are presented below.

A. Returns Filed One Year After the TAS Letter Advised That the Apparent Error Consisted of Not Meeting the Relationship Test

Of the returns filed by taxpayers in the year after they received a TAS letter (*i.e.*, tax year 2016 returns for taxpayers who received the letter in 2016, and tax year 2017 returns for taxpayers who received the letter in 2017):

- i. 74.4 percent appeared to have claimed EITC in error. In contrast, 77.3 percent of returns filed by taxpayers in the control group, but only 71.3 percent of returns filed by audited taxpayers, appeared to claim EITC in error; and
- ii. 59.4 percent appeared to have claimed EITC in error because the relationship test had not been met (*i.e.*, the return contained the same error identified in the TAS letter). In contrast, 66.7 percent of returns filed by taxpayers in the control group, but only 46.6 percent of returns filed by taxpayers who had been audited, appeared to contain the same error.

Thus, taxpayers who received the TAS letter filed returns that were more compliant with respect to EITC for the following tax year, compared to control group taxpayers. However, returns filed by audited taxpayers were more compliant than returns filed by taxpayers in either of the other two groups.

B. Returns Filed Two Years After the TAS Letter Advised That the Apparent Error Consisted of Not Meeting the Relationship Test

Of the returns filed by taxpayers two years after they received a TAS letter (*i.e.*, tax year 2017 returns for taxpayers who received the letter in 2016, and tax year 2018 returns for taxpayers who received the letter in 2017):

- i. 69.7 percent appeared to have claimed EITC in error. In contrast, 72.7 percent of returns filed by taxpayers in the control group, but only 66.7 percent of returns filed by audited taxpayers, appeared to claim EITC in error; and
- ii. 52.2 percent appeared to have claimed EITC in error because the relationship test had not been met (*i.e.*, the return contained the same error identified in the TAS letter). In contrast, 58.5 percent of returns filed by taxpayers in the control group, but only 40.3 percent of returns filed by taxpayers who had been audited, appeared to contain the same error.

Thus, taxpayers who received the TAS letter filed returns that were more compliant with respect to EITC in the following two tax years, compared to control group taxpayers. However, returns filed by audited taxpayers continued to be more compliant than returns filed by taxpayers in either of the other two groups.

C. Returns Filed Three Years After the TAS Letter Advised That the Apparent Error Consisted of Not Meeting the Relationship Test

Of the returns filed by taxpayers three years after they received a TAS letter (*i.e.*, tax year 2018 returns for taxpayers who received the TAS letter in 2016):

- i. 66.6 percent appeared to have claimed EITC in error. In contrast, 70.3 percent of returns filed by taxpayers in the control group, but only 65.1 percent of returns filed by audited taxpayers, appeared to claim EITC in error;²⁰ and
- ii. 45.1 percent appeared to have claimed EITC in error because the relationship test had not been met (*i.e.*, the return contained the same error identified in the TAS letter). In contrast, 54.5 percent of returns filed by taxpayers in the control group, but only 37.1 percent of returns filed by taxpayers who had been audited, appeared to contain the same error.

Thus, taxpayers who received the TAS letter filed returns that were more compliant with respect to EITC in the following three tax years, compared to taxpayers in the control group. Moreover, by the third year, there was no statistically significant difference between the error rate in returns filed by taxpayers who received a TAS letter and returns filed by audited taxpayers. Audited taxpayers continued to be less likely to *repeat* their error, however, than taxpayers in either of the other two groups.

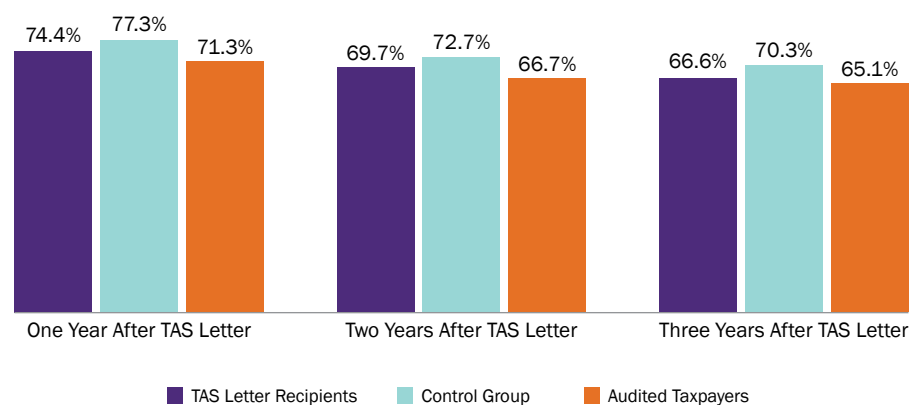
20 The difference between the error rate for taxpayers who received the TAS letter and taxpayers who were audited is not statistically significant.

We first illustrate how often taxpayers made *any* error in claiming EITC on subsequent returns (Figures 4.1.1 and 4.1.2), and then how often taxpayers *repeated their error* on subsequent returns (Figures 4.1.3 and 4.1.4).

Figure 4.1.1 summarizes the data about the frequency with which taxpayers appeared to continue to claim EITC in error.

FIGURE 4.1.1

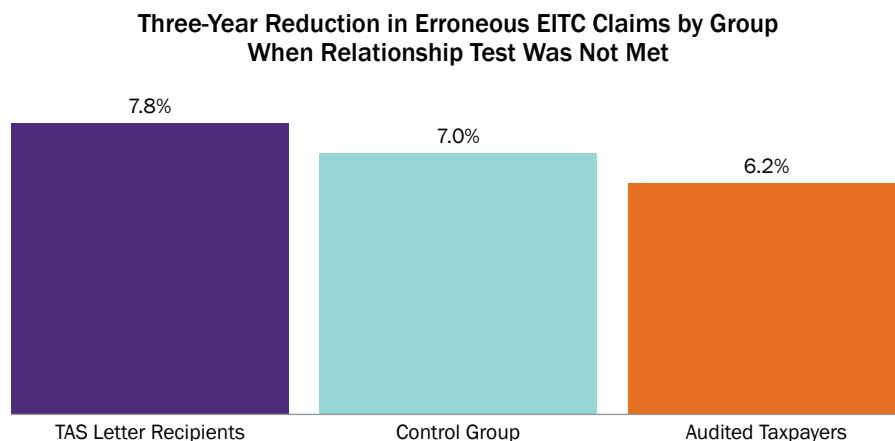
Frequency With Which Taxpayers in the Study Groups Erroneously Claimed EITC When the Relationship Test Was Apparently Not Met



As Figure 4.1.1 demonstrates, taxpayers in all three groups were less likely to make erroneous EITC claims over time. However, taxpayers who received the TAS letter showed more improvement in tax compliance over time than taxpayers in the other two groups. For example, one year after receiving the TAS letter, taxpayers erroneously claimed EITC 74.4 percent of the time, but this rate decreased to 66.6 percent by the third year after receiving the letter, a decline of 7.8 percentage points. In contrast, the rate at which control group taxpayers erroneously claimed EITC over the same three-year period declined by only seven percentage points (from 77.3 percent to 70.3 percent). The rate at which audited taxpayers erroneously claimed EITC over the same three-year period declined by only 6.2 percentage points (from 71.3 percent to 65.1 percent).

Figure 4.1.2 shows the increase in compliance (or decrease in noncompliance) of the three groups over three years.

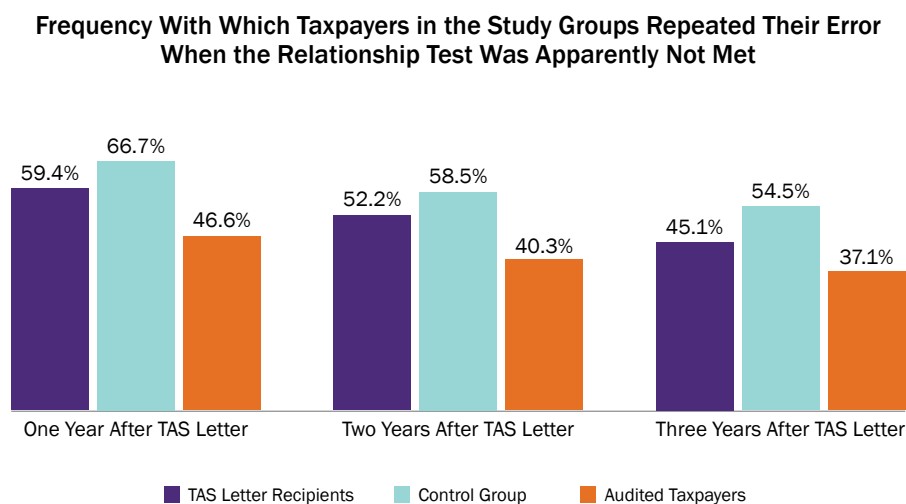
FIGURE 4.1.2



As discussed above, taxpayers who received the TAS letter were less likely to make the same error of claiming EITC when the relationship test did not appear to be met, compared to taxpayers in the control group. Audited taxpayers were less likely to repeat their error than taxpayers in the other two groups.

Figure 4.1.3 summarizes the frequency with which taxpayers appeared to repeat their error.

FIGURE 4.1.3



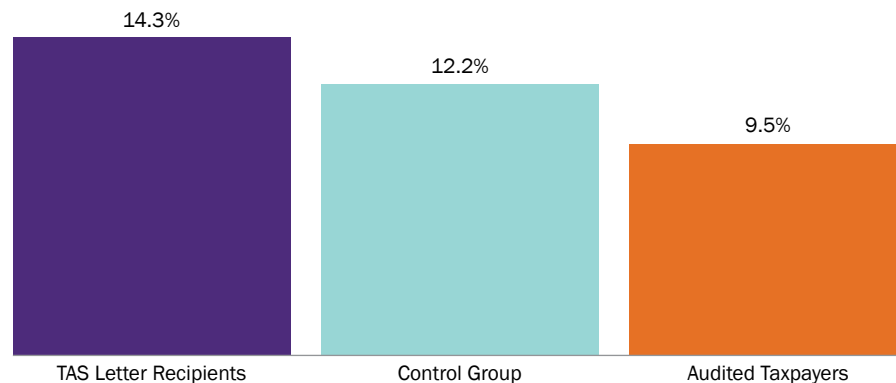
As Figure 4.1.3 demonstrates, taxpayers in all three groups were less likely to repeat their error each year. However, taxpayers who received the TAS letter again showed more improvement in tax compliance over time than taxpayers in the other two groups. For example, one year after receiving the TAS letter, taxpayers erroneously repeated their error 59.4 percent of the time, but this rate decreased to 45.1 percent by the third year after receiving the letter, a decline of 14.3 percentage points. In contrast, the

rate at which taxpayers in the control group repeated their error over the same three-year period declined by only 12.2 percentage points (from 66.7 percent to 54.5 percent). The rate at which audited taxpayers repeated their error over the same three-year period declined by only 9.5 percentage points (from 46.6 percent to 37.1 percent).

Figure 4.1.4 shows the increase in compliance (or decrease in noncompliance), in terms of repeating their error, of the three groups over three years.

FIGURE 4.1.4

Three-Year Reduction in Repeating the Error of Not Meeting the Relationship Test



2. In Both Years Following the Year in Which a TAS Letter Advised That the Residency Test Appeared Not to Have Been Met and Provided an Additional Help Line, Taxpayers Who Received the Letter Filed Returns That Were More Compliant Than the Returns of Taxpayers in Any Other Group

As discussed above, the first version of the TAS letter sent as part of the 2016 study to taxpayers who appeared to not meet the residency test did not include a telephone help line that taxpayers could call and speak to a TAS employee about their eligibility for EITC.²¹ In addition, a separate group of taxpayers, 967 in total, who appeared to have claimed EITC without meeting the residency test received a different letter that not only advised them of the error but also included an additional toll-free phone number they could call to speak with a TAS employee.²²

21 There were 2,173 taxpayers who received this letter as part of the 2016 study and 2,255 taxpayers who received this letter as part of the 2017 study.

22 As we reported in the 2017 study, the letters we sent to these taxpayers were returned as undeliverable more often than letters sent to taxpayers who appeared not to meet the residency test whose letter did not include an additional phone number. National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, at 22, note 19 (*Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC*). We analyzed the returns filed by taxpayers who received a letter with an extra help phone number and whose letters were undeliverable and found that including these taxpayers in the sample would not have changed the outcomes we report here (i.e., as discussed below, returns filed by taxpayers who received the TAS letter with the extra help phone number were more compliant than returns filed taxpayers in any of the other groups).

A. Returns Filed One Year After the TAS Letter Advised That the Apparent Error Consisted of Not Meeting the Residency Test and Included an Extra Help Phone Line

Of the returns filed by taxpayers one year after the TAS letter was received (*i.e.*, for tax year 2017):

- i. 73.4 percent appeared to have claimed EITC in error. In contrast, 81.5 percent of 2017 returns filed by taxpayers who had received a letter from TAS which did not contain the additional phone number; 81.1 percent of returns filed by taxpayers in the control group; and 81.6 percent of returns filed by taxpayers who were audited appeared to have claimed EITC in error;²³ and
- ii. 54.1 percent appeared to have claimed EITC in error because the residency test had not been met (*i.e.*, the return contained the same error identified in the TAS letter). In contrast, 67.7 percent of returns filed by taxpayers who received a letter from TAS without the additional phone number; 66.5 percent of returns filed by taxpayers in the control group; and 60.1 percent of returns filed by taxpayers who had been audited appeared to contain the same error.

Thus, the TAS letter with the extra help phone line was more effective in averting erroneous EITC claims than sending the TAS letter without the extra help phone line, not sending a letter at all, or even auditing the taxpayer. This finding is particularly interesting considering that very few taxpayers — 35 in total — actually called the extra help number and spoke to a TAS employee.

B. Returns Filed Two Years After the TAS Letter Advised That the Apparent Error Consisted of Not Meeting the Residency Test and Included an Extra Help Phone Line

Of the returns filed by taxpayers two years after the TAS letter was received (*i.e.*, for tax year 2018):

- i. 73.1 percent appeared to have claimed EITC in error. In contrast, 79.2 percent of returns filed by taxpayers who received a letter from TAS without the additional phone number; 77.8 percent of returns filed by taxpayers in the control group; and 77.7 percent of returns filed by taxpayers who were audited appeared to have claimed EITC in error; and
- ii. 49.3 percent appeared to have claimed EITC in error because the residency test had not been met (*i.e.*, the return contained the same error identified in the TAS letter). In contrast, 60.2 percent of returns filed by taxpayers who received a letter from TAS without the additional phone number; 61.9 percent of returns filed by taxpayers in the control group; and 53.6 percent of returns filed by taxpayers who had been audited appeared to contain the same error.

Thus, the TAS letter with the extra help phone line was still more effective in averting repeated errors in claiming EITC claims than sending the TAS letter without the extra help phone line, not sending a letter at all, or even auditing the taxpayer.

We first illustrate how often taxpayers made *any error* in claiming EITC on subsequent returns (Figure 4.1.5), and then illustrate how often taxpayers *repeated their error* on subsequent returns (Figure 4.1.6).

Figure 4.1.5 summarizes the frequency with which taxpayers appeared to continue to claim EITC in error when the residency test was apparently not met.

23 There was never any statistically significant difference in the subsequent compliance of returns filed by taxpayers who received a TAS letter advising that the residency test had not been met, but without providing an extra help phone number, and returns filed by taxpayers in the control group.

FIGURE 4.1.5

Frequency With Which Taxpayers in the Study Groups Erroneously Claimed EITC When the Residency Test Was Apparently Not Met



As Figure 4.1.5 demonstrates, taxpayers in all four groups were less likely to make erroneous EITC claims over time, but the returns of taxpayers who received the TAS letter *with the extra help line* were markedly more compliant than the returns of taxpayers in any of the other groups.

Figure 4.1.6 summarizes the differences in the frequency with which taxpayers repeated their error.

FIGURE 4.1.6

Frequency With Which Taxpayers in the Study Groups Repeated Their Error When the Residency Test Was Apparently Not Met



As Figure 4.1.6 demonstrates, taxpayers in all four groups were less likely to repeat their error over time, but the returns of taxpayers who received the TAS letter *with the extra help line* were much less likely to

repeat the error of claiming EITC when the residency test was not met than the returns of taxpayers in any of the other groups.

3. The TAS Letter Advising Taxpayers That a Duplicate Claim Had Been Made Did Not Affect Future Erroneous Claims

As discussed above, some taxpayers received a TAS letter advising them that they apparently erred in claiming EITC because another taxpayer had claimed EITC with respect to the same child.²⁴

The TAS letter did not appear to avert erroneous EITC claims with respect to returns these taxpayers filed in any of the three years after receiving the TAS letter, compared to taxpayers in the control group. Thus, we do not present those detailed findings. However, we note that the number of taxpayers who *repeated* this error dwindled over the years; by the second year after the TAS letter advised that there appeared to be duplicate claims, no more than five percent of taxpayers in any of the three groups repeated this error.

CONCLUSION

The data demonstrates that sending a tailored, educational letter to taxpayers who appear to have erroneously claimed EITC averts future erroneous EITC claims, and the effect extends beyond the year in which the taxpayer receives the letter. The letter is particularly effective where the apparent error consists of not meeting the relationship test. Audits are sometimes more effective in averting erroneous EITC claims where the error consists of not meeting the relationship or residency tests, compared to sending an educational letter. However, where the relationship test appears not to have been met, there is no statistically significant difference between the overall accuracy of the returns filed by taxpayers three years after receiving a TAS letter and returns filed by audited taxpayers. Where the apparent error is that the residency test was not met, an educational letter that includes a telephone help line that taxpayers can use to determine their eligibility for the credit averts noncompliance even more effectively than audits do. In any event, in view of the volume of returns that appear to erroneously claim EITC because the relationship or residency tests were not met, audits do not appear to be the most realistic option for addressing erroneous EITC claims.

RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS send tailored, educational letters, similar to the TAS letters, to EITC claimants the IRS does not have current plans to audit:

1. Where the claimant does not appear to meet the relationship requirement for claiming EITC, because such a letter appears to prevent taxpayers from erroneously claiming EITC for at least three years; and
2. Where the claimant does not appear to meet the residency requirement for claiming EITC, but only if the letter includes an additional help telephone number the taxpayer can call for assistance in determining for EITC, because such a letter appears to prevent taxpayers from erroneously claiming EITC for at least two years.

24 There were 2,189 taxpayers who received this letter as part of the 2016 study and 2,340 taxpayers who received this letter as part of the 2017 study.