
IRS Earned Income Tax Credit (EITC) Initiative

Final Report to Congress, October 2005

**Department of the Treasury
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Executive Summary

In June 2003, the Commissioner of Internal Revenue announced a five-point initiative to improve service, fairness, and compliance in the administration of the Earned Income Tax Credit (EITC). One of the goals set forth in this initiative was to reduce EITC overclaims without adversely affecting participation among eligible taxpayers. The Internal Revenue Service (IRS) has conducted three studies to address elements of the five-point initiative:

- An EITC Qualifying Child Residency Certification Study;
- An EITC Filing Status Study; and
- An EITC Automated Underreporter (AUR) Study.

This final report fulfills the congressional mandate (Public Law 108-199, Section 206) for a report on the Qualifying Child Study. In August 2004 and March 2005, the IRS issued its preliminary status reports on these programs to Congress. This report is an update of the March report, containing findings for each of the three EITC studies.

The studies described in this report address the three overclaim areas highlighted in the Commissioner's five-point plan. The objectives of these studies are to determine, for the test taxpayers, the effect of the initiatives being tested on EITC overclaims, participation among eligible taxpayers, and the associated burden, both on the taxpayer and on the IRS.

EITC Qualifying Child Residency Certification Study

The Qualifying Child Study examined the effects of a residency certification requirement on: (1) the amount of EITC claimed including the amount of erroneous claims; (2) the number of children claimed; (3) taxpayer participation in the EITC; (4) taxpayer burden; and (5) the amount of erroneous claims that were prevented from being paid to ineligible taxpayers. The primary focus of the evaluation was to determine how certification affected the taxpayers involved in the test, that is, those taxpayers who were asked to certify. The study design, however, enabled the results to be projected to the population of taxpayers from which the test sample was selected.

The EITC Qualifying Child Residency Certification Study included elements of an education/outreach program, a "soft-notice" program, and an examination program. It was designed to include:

- A random sample of 25,000 EITC claimants (the "test group") for whom IRS could not establish qualifying child residency eligibility through available data, and who, therefore, were required to go through the certification process for Tax Year (TY) 2003;
- A similarly sized control group of taxpayers with characteristics similar to the test group; and
- Extensive data collection, including information from a telephone/mail survey administered to a random sub-sample of taxpayers in both the test and control groups.

Mathematica Policy Research, Inc., a private consulting firm, along with the Government Accountability Office (GAO) and the Treasury Inspector General for Tax Administration (TIGTA), favorably reviewed the IRS study design.

In December 2003, the IRS mailed out documents to the 25,000 taxpayers in the test group who had claimed the EITC with qualifying children in the previous tax year (TY 2002). These documents included a letter describing the study, a certification form offering three options for certifying (letters, official records, or third party affidavits), the affidavits themselves, and IRS publications containing information on the EITC. The IRS has completed processing the information received from nearly all the taxpayers in the test group.

The certification process was designed to give taxpayers sufficient time to respond to IRS requests (for example, requests for additional information or notifications of decisions). In general, the IRS allows at least 30 days for a response from a taxpayer (90 days for the statutory *Notice of Deficiency*) before moving on to the next step in the process. Thus, the completion of the certification process could reasonably be expected to take several months for taxpayers who do not respond immediately to the IRS.

The results in this report are based on taxpayer return filings through the end of December 2004 and certification processing activities through late May 2005. By the end of December 2004, a total of 22,422 control group returns were filed, or about 90 percent of the control group. This compares with 21,784 test group returns that were filed, or 89 percent of the test group. About 19 percent of the test group filed returns but did not claim EITC. This is five percentage points higher than for the control group. Approximately three percent of the test group claimed the EITC without qualifying children. This is one percentage point higher than the control group percentage.¹

About 36 percent of the control group claimed EITC with one qualifying child and 38 percent claimed EITC with two qualifying children. Thus a total of about 74 percent of the control group claimed EITC with qualifying children. About two percent of the control group claimed EITC without qualifying children. The remaining return filers, about 14 percent of the control group did not claim EITC.

Compared with the control group, fewer test group returns claimed EITC with children. About 34 percent of the test group claimed EITC with one qualifying child and 33 percent claimed EITC with two qualifying children. The difference was statistically significant. Therefore, about 67 percent of the test group claimed EITC with qualifying children – or about seven percentage points lower than for the control group. Most of the difference between the two groups is attributable to a decline in claims of two or more children.

The study results suggest that the certification requirement reduced EITC claims. The total amount of EITC claimed by the test group was about \$36.9 million. This is about \$4.3 million, or approximately 10 percent, less than the \$41.2 million claimed by the control group. This 10 percent difference in EITC claimed suggests that a certification requirement does influence taxpayer behavior. This reduction in claims may be the result of increased voluntary compliance through better understanding of the residency requirement or deterrence of erroneous claims from ineligible claimants. However, it also may reflect a reduction in claims by eligible taxpayers who should have claimed the EITC but were deterred by the certification requirement. This would affect participation rates. Based in large part on the survey data, the IRS estimates

¹ This report presents the final results of the study. Some of these results differ from the preliminary results presented in earlier reports due to revisions in the data.

that deterred erroneous claims are between \$2.9 million and \$3.3 million while between \$1.1 and \$1.4 million of reduced claims are attributable to the unintended deterrence of eligible claimants.

The data also indicate that the certification process prevented the payment of erroneous claims for cases where a claim was made but the residency requirement was not met. As of May 2005 IRS had completed processing for all but 414 returns of the 16,480 taxpayers in the test group who filed for TY 2003 and claimed EITC with qualifying children. About \$10.9 million in EITC claims were denied in the certification process. The amount of control group claims that were not paid as a result of normal IRS enforcement programs was \$1.4 million.

Based on findings of a survey of taxpayers, certification appeared to increase both the average time and expense involved with preparing and filing the tax return and certification materials. The test group spent an average of 6.9 hours preparing their tax returns—about 2.6 hours more than the control group. For those who used paid preparers, the cost of that service was roughly the same for the test and control groups (about \$136 and \$132, respectively). Excluding the cost of paid preparers, out-of-pocket expenses were, on average, about \$36 for the test group, about \$8 more than the control group. About 18 percent of the test group reported taking time off from work to complete their tax return, compared to 9 percent of the control group.

While taxpayers involved in the certification process seemed fairly evenly split in their assessments about their difficulty or ease in understanding the new forms and in deciding which documents to use for certification, more found it very or somewhat easy either to obtain the documents they needed or to respond to IRS requests for additional information. Nearly two-thirds of those in the test group thought taxpayers should be required to prove EITC requirements before they receive the EITC—a slightly higher proportion than those in the control group.

The certification requirement in the Qualifying Child Study required proof of qualifying child residency in the form of records, a letter on official letterhead, or a Third Party Affidavit. The Study pioneered the use of affidavits to support the determination of the residency of the qualifying children in the EITC claim. The results show that affidavits had a higher acceptance rate than the other two types of documents and, in general, seemed to provide a reliable way to substantiate claims in this context. The higher acceptance rate likely is due in part to the fact that the affidavits were special forms with dedicated lines for all the required information.

EITC Filing Status Study

The EITC Filing Status Study, like the EITC Qualifying Child Residency Certification Study, included a randomly selected sample of EITC claimants that may have a high likelihood of filing returns with EITC overclaims. The EITC Filing Status Study sample consisted of 36,000 taxpayers who filed a TY 2002 return using the single or head of household filing status and had filed as married filing jointly or married filing separately in at least one of the previous three years. The EITC Filing Status Study investigated the impact of requiring these EITC taxpayers to document marital status.

Taxpayers selected for inclusion in the EITC Filing Status Study were not contacted prior to filing their TY 2003 return. However, if they claimed the EITC and filed as single or head of

household on their TY 2003 return, the IRS held the EITC portion of their refunds and asked them to provide additional information about marital status for TY 2003. IRS examiners used the information furnished by claimants as the sole basis for determining whether the filing status requirements were satisfied.

As of the end of December 2004, 26,550 returns meeting the criteria described above had been filed. IRS has completed processing for 26,445 returns, or 99 percent of those who were asked to document their marital statuses. A total of \$11.9 million in revenue was protected (that is, the EITC was not paid) on the completed cases, which is roughly 20 percent of the \$58.3 million in EITC claimed by taxpayers in the Filing Status Study.

Automated Underreporter (AUR) Study

The EITC Automated Underreporter (AUR) Study is an IRS initiative to focus compliance efforts on taxpayers who claim EITC but are either ineligible because their incomes are too high or eligible but overclaim the EITC because they misreport their incomes. Beginning in 2003, the IRS initiated the EITC AUR Study to identify, through document matching, EITC claimants with a high likelihood of income reporting errors. The study had two objectives:

- To observe the impact of applying EITC income criteria to AUR-selected cases in order to determine the overall impact on EITC claims; and
- To use the resulting EITC data to update the AUR case selection method so that it identifies EITC claimants with a higher likelihood of income reporting errors.

The IRS selected 300,000 taxpayers who claimed EITC and for whom there were indications of income misreporting for Tax Year 2002. Under prior AUR processing criteria that did not consider changes to the EITC claim as a selection factor, IRS would have selected approximately the same number of cases that contained EITC claims. In this study, the selection methodology focused on the expected change to the EITC claim. IRS did not hold refunds or EITC claims because the income mis-matches were identified well after the return was filed.

The IRS has completed working the 300,000 EITC returns selected for the AUR Study. As of the end of December 2004, all 300,000 EITC returns had been manually reviewed. For about 38,800 of these cases, the reviewer resolved the apparent income discrepancy and closed the case (these are called “screenout cases”). For the remaining 261,200 cases, notices were sent to taxpayers about the seemingly misreported income amounts. About 260,300 of these notice cases have been closed. Approximately 16 percent of the notices were closed without a change to the taxpayer’s account. Nearly 83 percent were closed with reductions in, or disallowances of, the EITC and/or increases in tax. About 1,400 cases were transferred to another operation for additional IRS processing.

A review of the AUR study data indicates that both the screen-out and the no change rates for the AUR EITC cases in this study were lower than the rates for other AUR cases. The data also show a reduction in, or disallowance of, EITC of approximately \$250 million and an increase in tax—net of offsetting withholding amounts—of approximately \$134 million. Based on the changes to the credit, the EITC-specific AUR approach for TY 2002 was an improvement over past practice.

The selection methodology for the TY 2002 study, however, focused on the expected change to EITC only and did not incorporate expected changes to tax, other credits, or prepayments. For TY 2003 and subsequent years, the focus has been broadened to incorporate these other items, and therefore, better characterizes the overall impact of the underreported income on revenue. Information from these subsequent studies will provide a better picture of the effect of the change in methodology on revenue in general, rather than on EITC only.

Summary

This final report fulfills the congressional mandate (Public Law 108-199, Section 206) for a report on the Qualifying Child Study. It provides an overview of the three EITC initiatives being tested—Qualifying Child Certification, Filing Status, and Automated Underreporter—and reports the final results of the three studies. The data indicate that these efforts have, in the aggregate, uncovered more than \$275 million of apparently erroneous claims and prevented the payment of these claims. The result also points up the need for further testing in the qualifying child and filing status areas. In particular, the IRS needs to conduct more testing of alternative scenarios of implementation models in order to determine how to best maximize the return on investment in these two areas, while reducing taxpayer error and minimizing taxpayer burden.

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IRS Earned Income Tax Credit (EITC) Initiative: Final Report to Congress, August 2005

I. Introduction

In June 2003, the Commissioner of Internal Revenue announced a five-point initiative to improve service, fairness, and compliance in the administration of the Earned Income Tax Credit (EITC). One of the goals set forth in this initiative was to improve compliance with the EITC without adversely affecting participation by eligible taxpayers. During tax year (TY) 2003 the Internal Revenue Service (IRS) conducted three tests to address the goals set forth in this initiative: the EITC Qualifying Child Residency Certification Study, the EITC Filing Status Study, and the EITC Automated Underreporter (AUR) Study.¹

This final report fulfills the congressional mandate (Public Law 108-199, Section 206) for a report on the Qualifying Child Study (see Appendix A for details). For completeness, this document includes most of the background information presented in earlier interim reports. In addition, it includes analyses of taxpayer survey data and third-party documentation verification data that were part of the Qualifying Child Study. The report presents the results of the three test studies and includes an assessment of the costs and benefits of these studies and lays out a framework for developing a return on investment estimate for a fully implemented certification requirement. It is important to note, however, that the IRS has reached no conclusion as to whether to impose such a requirement. While the test discussed in this report has provided valuable information, we believe additional testing is necessary.

II. The Earned Income Tax Credit (EITC)

The EITC, enacted in 1975, provides a refundable tax credit for low-income working families. Originally intended to ease the burden of Social Security taxes and provide an incentive to work, the credit has been modified several times during the years since its introduction. The credit now provides a substantial benefit to millions of American families. Eligibility for the EITC is based on three types of income: earned income, adjusted gross income and investment income. The amount of the credit depends on earned income and adjusted gross income, as well as the presence and number of qualifying children and filing status. The credit amount is equal to a specified percentage of the taxpayer's income, up to a ceiling that varies by filing status and the number of qualifying children. Taxpayers with investment income greater than a specified amount are not eligible for the EITC.

A qualifying child must meet residency, relationship, and age tests. In particular, the children must reside with the claimant for more than half of the tax year. Married taxpayers filing separately do not qualify for EITC.

¹ Throughout the remainder of the document, these studies will be referred to as the Qualifying Child Study, the Filing Status Study, and the AUR Study, respectively.

The EITC program has grown significantly since its inception in 1975. In its first year, 6.2 million taxpayers claimed \$1.25 billion in earned income tax credits, or about \$4.3 billion in 2003 dollars. At that time, the maximum credit was \$400, or approximately \$1,350 in 2003 dollars, and the income level at which the credit phased-out completely was \$8,000, or about \$27,350 in 2003 dollars.

Between 1975 and 2002, Congress significantly expanded the credit. Since 1991, the amount of the credit has varied with the number of qualifying children (up to two). Since 1994, a small credit has been available for taxpayers without any qualifying children. And, beginning in 2002, Congress provided a benefit to joint filers by extending the credit's phase-out range for married couples.

In TY 2003, about \$39 billion in credits were claimed; the maximum credit and income level at which the credit phased-out completely had grown to \$4,204 (for taxpayers with two or more children) and \$34,692 (for married filing jointly taxpayers with two or more children), respectively. In TY 2003, more than two-thirds of all EITC claimants relied on paid preparers, and about the same percentage filed electronically.

For TY 2003, the focus year for the Qualifying Child Study, taxpayers who were married filing jointly with two qualifying children were eligible for the maximum credit at income levels between \$10,510 and \$14,730. The phaseout began at \$13,730 for single and head of household taxpayers with two qualifying children. The credit completely phased out at \$34,692 for married taxpayers filing jointly and \$33,692 for single and head of household taxpayers. See **Table 1** for the EITC parameters applicable to TY 2003.

Table 1. EITC Parameters for Tax Year 2003 by Filing Status and Number of Qualifying Children

EITC Parameters	Filing Status					
	Single/Head of Household/ Qualifying Widow(er)			Married Filing Jointly		
	No Qualifying Children	One Qualifying Child	Two Qualifying Children	No Qualifying Children	One Qualifying Child	Two Qualifying Children
Credit percentage	7.65%	34.00%	40.00%	7.65%	34.00%	40.00%
Phaseout percentage	7.65%	15.98%	21.06%	7.65%	15.98%	21.06%
Maximum credit	\$382	\$2,547	\$4,204	\$382	\$2,547	\$4,204
Income at which begin maximum credit	\$4,990	\$7,490	\$10,510	\$4,990	\$7,490	\$10,510
Income at which begin phaseout	\$6,240	\$13,730	\$13,730	\$7,240	\$14,730	\$14,730
Income at which credit completely phased-out	\$11,230	\$29,666	\$33,692	\$12,230	\$30,666	\$34,692

III. EITC Compliance Estimates

IRS studies of EITC compliance have consistently shown relatively high overclaim rates for the EITC. The most recent IRS study of overall EITC compliance, the TY 1999 EITC Compliance Study, estimated that between \$8.5 billion and \$9.9 billion of the claims filed for TY 1999 should not have been paid. Though the IRS has implemented a number of legal and administrative changes since that study, IRS officials believe the error rate is still

substantial. The 1999 study estimates identified three major sources of errors.² These included qualifying child errors, filing status errors and income reporting errors.

Qualifying child errors account for the largest share of overclaims. To claim a qualifying child, a taxpayer must satisfy relationship, age, and residency tests. However, the results from the 1999 EITC compliance study indicated that the chief compliance issue associated with qualifying children involved the residency test.³ In fact, the study estimates showed that about 80 percent of the EITC overclaimed on returns with qualifying child errors was associated with returns for which the child (or children) did not meet the qualifying child residency requirement or did not meet the residency and relationship requirements.

IRS recently completed another compliance study that will provide slightly more current information about EITC compliance. Information from the National Research Program (NRP) study of TY 2001 individual income tax returns is now becoming available and is beginning to be analyzed by IRS researchers. Based on analysis of preliminary data, the EITC overclaim estimates developed from the NRP individual income tax reporting compliance study are not expected to be substantially different from those developed from the TY 1999 compliance study. Also, because the NRP individual income tax reporting compliance study covered TY 2001, the estimates will not reflect possible effects of several changes to the EITC that became effective for TY 2002.

IV. IRS Five-Point Initiative

In the summer of 2003, IRS Commissioner Mark W. Everson announced a five-point initiative to improve service, fairness, and compliance with EITC rules. This initiative was designed to:

- Reduce the backlog of pending EITC examinations to ensure that eligible taxpayers being examined receive their refunds timely;
- Minimize burden and enhance the quality of communications with taxpayers by improving the existing audit process;
- Encourage eligible taxpayers to claim EITC by increasing outreach efforts and making EITC requirements easier to understand;

² The 1999 study also identified another major source of error. This error involved taxpayers claiming EITC using a qualifying child who was also the qualifying child of someone else with a higher modified adjusted gross income. This EITC eligibility rule was known as the AGI-tiebreaker rule. However, the *Economic Growth and Tax Relief Reconciliation Act of 2001* (EGTRRA) simplified the tiebreaker rule by replacing, in most cases, an adjusted gross income comparison rule with a relationship-based hierarchy for determining the party eligible to claim the credit in situations where a child is the qualifying child of more than one person. The new rule only applies if a child is claimed (and may be claimed) by more than one person. This law change, first effective for TY 2002 returns, was expected to eliminate the tiebreaker rule as a significant source of EITC error. Consequently, efforts to reduce EITC overclaims were not focused on this source of error.

³ IRS research has shown that the major source of error associated with qualifying children involves the residency test rather than the age or relationship tests. Errors occur because taxpayers claim qualifying children who did not live with them for more than half of the year – an EITC requirement.

- Ensure fairness by refocusing compliance efforts on taxpayers who claimed the credit but were ineligible because their income was too high; and
- Pilot a certification program to substantiate qualifying child residency eligibility for claimants whose returns are associated with a high likelihood of error.

A solicitation for public comment on the proposed certification pilot program accompanied the announcement of the five-point initiative. IRS executives also met with various stakeholders to explain the proposed test and obtain comments and suggestions. In developing the final study design and procedures, IRS took into consideration the comments received through the meetings and public comment process. For example, IRS incorporated suggestions about the start date of the test, the design of the forms, outreach to taxpayers, and the number of taxpayers involved in the test. The IRS also agreed to test the concept rather than launch a pilot in preparation for full-scale implementation as originally planned.

The three studies described in this report address the last two points of the Commissioner's five-point plan. The objective of these studies was to determine the effect of these programs on EITC overclaims, participation among eligible taxpayers, and the associated burden, both on taxpayers and the IRS. As part of the analysis, the IRS evaluated the costs and benefits associated with each of the studies. These estimates enable the IRS to determine if certification and the two other processes studied could provide a cost-effective way to reduce erroneous EITC payments while maintaining historically high participation rates. The remainder of this report discusses each study.

V. EITC Qualifying Child Residency Certification Study

The Qualifying Child Study sought to determine the impact of a residency certification requirement on: (1) the amount of EITC claimed including the amount of erroneous claims; (2) on the number of children claimed; (3) on taxpayer participation in the EITC; (4) on taxpayer burden; (5) and on the amount of erroneous claims that were prevented from being paid to ineligible taxpayers. This study focused on the population of EITC claimants for whom IRS could not establish qualifying child residency through available data. The results from this study should not be assumed to apply to all EITC claimants with qualifying children.

The IRS also sought to test various components of the certification study. The results are intended to help the IRS evaluate whether to implement a certification requirement more broadly and to provide insight into how the requirement might be administered. The Qualifying Child Study was designed to include:

- A random sample of EITC claimants (the "test group") for whom IRS could not establish qualifying child residency eligibility through available data, and who, therefore, would be required to go through the certification process for TY 2003;
- A control group of similar size and taxpayer characteristics as the test group but who would not go through the certification process; and
- Extensive data collection, including a telephone/mail survey administered to a random subsample of taxpayers in both the test and control groups.

The IRS required study data that could be used to determine the impact of certification on taxpayer filing behavior and understand claimants' experience with the certification process and its effect on their filing choices. As part of the data collection activities, in April 2004, IRS awarded a contract to design and administer the survey to the Westat Corporation. Westat administered the survey between August 2004 and November 2004.

V.A EITC Qualifying Child Residency Certification Study Sample Development

In developing a sample for the Qualifying Child Study, the IRS took advantage of multiple data sets, including data from numerous internal and external databases that could be used to ascertain whether qualifying child residency requirements are met by EITC taxpayers. For the Qualifying Child Study, IRS selected a random sample of 25,000 taxpayers who claimed the EITC with at least one qualifying child in TY 2002 but for whom IRS could not establish, based on available data, that the residency requirements were met for one or more of those qualifying children.

The IRS employed a two-stage sample design for the study. The sample frame for the first stage of the design was the population of taxpayers who filed TY 2002 returns in the first five months of 2003 and claimed the EITC with at least one qualifying child. From this population of approximately 16 million taxpayers, IRS drew a 10 percent random sample. To these 1.6 million returns, IRS applied a computer algorithm that utilizes information from various data sources and identifies EITC claimants who filed a claim that was likely to have met the eligibility residency requirements for qualifying children.

The IRS computer algorithm utilized data from the following databases:

Federal Case Registry—A Department of Health and Human Services (HHS) database that identifies presumed custodial relationships based on child support cases;

KidLink—A Treasury database which uses Social Security Administration (SSA) data that identifies the relationship between birth parents and children born since 1998;

DM-1—A database of taxpayer identification numbers (either Social Security Numbers or Individual Taxpayer Identification Numbers) and their associated name histories; and

Numident—SSA data that provides birth certificate information, including parent names.

IRS created the sample frame for the second stage of the sample design by removing claimants identified by the algorithm as having filed claims that likely met the residency requirement from consideration for residency certification. In addition, claimants were

removed from consideration for residency certification to ensure that IRS did not contact a taxpayer twice about the same return (e.g., for regular audit processing).

The subset of claimants whose qualifying children could not be substantiated through the computer algorithm, therefore, make up the sample frame for the second stage of the design. Altogether, 73 percent of the EITC claimants in the 10 percent sample were excluded from the study based on IRS being confident that residency could be shown based on data available from the above sources, leaving a pool of approximately 400,000 claimants in the second stage sample frame.

A systematic sampling process was used to draw two separate random samples of 25,000 taxpayers. The first sample of 25,000 serves as the test sample, and the second sample serves as a control sample. IRS also selected two 1,000-taxpayer subsamples from the 25,000-taxpayer test sample. The first subsample was used to test a variant of the residency certification documentation (see Section V.B for a discussion of the certification forms and schedules). In response to concerns that the English-only documents might weaken participation among the Spanish-speaking population, IRS sent forms and schedules in both English and Spanish to the second subsample. The overall sample size was driven by a desire to evaluate the operational and administrative issues that certification involves for both IRS and the taxpayer.⁴

Mathematica Policy Research Inc., the U.S. Government Accountability Office (GAO), and the Treasury Inspector General for Tax Administration (TIGTA) favorably reviewed the Qualifying Child Study sample design.⁵ In its review, Mathematica strongly endorsed the major elements of the study design, in particular, the decision to focus the certification study on a subset of taxpayers with a high likelihood of EITC overclaims (see **Appendix B**). Mathematica also commended IRS for its use of an array of data sources. GAO reviewed the steps that IRS has taken to implement the certification study and concluded that IRS “has struck a reasonable balance between preventing unreasonable burden on [EITC] taxpayers and balancing the need to obtain information on whether certification can be a useful approach to improving [EITC] compliance.” The objective of the TIGTA review was to determine the usefulness of the study in enabling IRS to make decisions regarding the future of the EITC program. TIGTA concluded that the “statistical sampling method used to select the samples for the {study} appears adequate and should provide reliable information on which to base future decisions.”

⁴ The size of the test group, among other things, reflected IRS’ estimate of its capacity to process certification documents and collect data from the sample at the Kansas City Compliance Campus where the data collection for the study was based. One element of the study is to determine the resources required by IRS to handle the certification procedures.

⁵ In the fall of 2003, Mathematica Research Policy, Inc., and GAO finalized their reports, *A Review of the Earned Income Tax Credit Residency Certification Pilot Study* and *Qualifying Child Certification Test Appears Justified, But Evaluation Plan is Incomplete*, respectively. In May 2004, TIGTA finalized its report, *The Statistical Sampling Method Used in the Earned Income Tax Credit Proof of Concept Test Appears Valid*.

V.B EITC Qualifying Child Residency Certification Process

In December 2003, the IRS sent the following five documents to the 25,000 taxpayers in the test group:

- A letter (Notice 84-A) describing the new certification requirement;
- Form 8836, Qualifying Children Residency Statement, which offers three options for certification (to be completed by the taxpayer and returned to the IRS). The three options are letters, records and affidavits;
- A Third Party Affidavit (Schedule A or Schedule B) form to be filed with Form 8836, attesting to the validity of the taxpayer's child residency certification on Form 8836;
- Publication 3211M, Earned Income Tax Credit Questions and Answers; and
- Publication 4134, Free/Nominal Cost Assistance Available for Low Income Taxpayers.

The letters, forms, and publications were in English, like the tax packages that IRS mails to individual taxpayers each December (see **Appendix C** for copies of Notice 84-A, Form 8836, Form 8836-SP, and Schedules A and B in both English and Spanish). The letter, Form 8836, and affidavit contained a note in Spanish referring Spanish-speaking persons to a telephone customer service center from which they could request copies of these documents in Spanish. The Qualifying Child Study marks the first usage of affidavits for IRS tax administration purposes.

Form 8836 requires proof of qualifying child residency in the form of records, a letter on official letterhead, or a signed affidavit (Schedule A) from any of the following: attorney, child-care provider, clergy, community-based organization, court or placement agency official, employer, health-care provider, Indian tribe official, landlord or property manager, law enforcement officer, school official, or social service agency or other government official.

Taxpayers could submit any combination of documents described in Form 8836 or in the Third Party Affidavit. The residency requirement would be fulfilled if they showed, when taken in combination, that the taxpayer and child lived together for more than half of 2003. In order to be accepted by the IRS, all documents submitted to prove residency had to show the child's or taxpayer's name, the address, and the dates at the address. It was not necessary for the taxpayer's and child's names to be on the same piece of documentation.

Individual documents were reviewed by tax examiners for acceptability. For the IRS to accept an item, documents had to include the required information (name, address, dates of residence), statements or letters needed to be on official letterhead, Third Party Affidavits had to be filled out completely and signed, and all information had to be legible. The review by tax examiners did not include contacting the document provider to verify the authenticity of the document or personal knowledge of the residency of the taxpayer and child; rather the focus was on identifying acceptable documents on which to base the decision of whether the taxpayer met the EITC residency requirement.

A subsample of 1,000 taxpayers received an alternate Third Party Affidavit (Schedule B) that broadens the definition of those allowed to certify the taxpayer's residency. The alternate Third Party Affidavit defines those eligible to complete the form more generally as anyone (except a spouse, dependent, qualifying child, or a parent of the qualifying child) with personal knowledge or records showing that the taxpayer and qualifying child lived together during the tax year. Therefore, this included most relatives, friend, and neighbors. In testing this alternate affidavit, the IRS responded to concerns that taxpayers may have difficulty certifying using any of the other approved sources and may most easily prove that they meet the qualifying child residency requirement using this form of certification.

In response to concerns that the English-only documents might weaken participation among taxpayers with limited English proficiency, the IRS sent both English and Spanish letters and forms to the randomly selected second subsample of 1,000 taxpayers, as noted earlier. This subsample was selected at random because the IRS lacks the type of information necessary to identify those taxpayers who would most benefit from the Spanish documents: those with low English proficiency who can read Spanish and those who have better access to Spanish-literate than to English-literate assistants.

For each of these two subsamples, the IRS evaluation focuses on the impact of the alternative procedures on the proportion of taxpayers who return Form 8836. For the first subsample, the key item is the type of third party providing certification documents. A possible impact of the alternate affidavit, and one that concerns the IRS, is that taxpayers may shift away from preferred, official sources to more informal and potentially less reliable (or less verifiable) sources. As part of the study, the IRS explored the validity and reliability of third-party affidavits.

To accomplish this, the IRS selected a subsample of 10 percent of taxpayers who received Schedule A and then validated that the third parties listed as certifying residency on the certification forms did provide the requested information and were also in a position to substantiate that the child met residency requirements. This process was called mandatory validation. IRS also validated the records and letters submitted for child residency certification by taxpayers in this 10 percent subsample. Mandatory validation was also carried out for *all* of the taxpayers in the Schedule B subsample.

For the Qualifying Child Study, certification generally occurred at the time of filing. Taxpayers were instructed to submit their certification materials when they filed their tax returns.⁶ However, some 700 taxpayers disregarded the instructions to send documents with their returns and sent the materials in December. For these taxpayers, IRS attempted to review their submission and certify them prior to the filing season so as not to delay their EITC claims. This response indicates interest in pre-certification on the part of some taxpayers. The goal for processing all certification cases was to check the documentation as

⁶ Paper return filers were instructed to attach Form 8836 and supporting documentation (records, letters, and/or affidavits) to their return and send the return to Field Compliance Services, Kansas City Campus. Electronic filers were instructed to file their return as they normally would and then send Form 8836 and supporting documentation to Field Compliance Services, Kansas City Campus.

quickly as possible and therefore minimize, to the extent possible, delays in payment of the credit to eligible taxpayers.

The process was designed to give taxpayers sufficient time to respond to IRS requests (for example, requests for additional information or notifications of decisions.) The certification procedures included both an additional letter and extra time that are not part of standard IRS procedures for EITC-related examinations. IRS standard procedures allow taxpayers 30 days to respond to the report of proposed changes. This timeframe was extended to 45 days for certification. The IRS also sent a second letter and report of proposed changes—which is not part of standard procedures—to taxpayers who did not respond to the first letter. This additional letter could add up to 45 days to the process. These two procedural changes added an additional letter and up to 60 additional days to the process.

In cases where taxpayers did not substantiate the residency of a child claimed for EITC, the credit based on this child was disallowed through IRS deficiency procedures. A statutory Notice of Deficiency, issued if the taxpayer did not respond to either of the two prior letters of proposed changes, gives the taxpayer 90 days to respond to the proposed assessment. If the taxpayer does not respond within the 90-day timeframe, an assessment is made. The completion of the certification process took several months for taxpayers who did not respond immediately to the IRS.

As explained earlier, 25,000 taxpayers were selected as a control group for the study. The control group taxpayers were *not* subject to the additional certification requirement. Instead, they were subject only to standard IRS procedures and programs. These standard procedures involve return processing that incorporates math error checks for mathematical, clerical, and taxpayer identification number (TIN) errors, scoring and possible selection of returns for EITC-specific pre-refund and post-refund examinations, scoring and possible selection of returns for other examination programs, and matching of information documents to tax return line item data through the AUR program which identifies misreported income. Under these standard procedures, fewer control group returns were subject to examination than test group returns were subject to certification review. . This is because everyone in the test group who claimed EITC with children was subject to the certification review process. However, the scope of the audit was typically broader for the control group, generally including more than just one EITC-related issue. The scope of the certification review generally was limited to one issue—residency of the child.

Because the test groups taxpayers and control group taxpayers were randomly selected from the same population of taxpayers, the experiences of the control group are believed to be reflective of what would have been observed for the test group had they not been part of the certification test.

V.C EITC Qualifying Child Residency Certification Study, Overview

As explained above, the certification test involved notifying test taxpayers, about a month prior to the start of the tax filing season, of a new requirement to provide

documentation in support of the EITC qualifying child residency requirement as a condition for receiving EITC. The package mailed to taxpayers included information about the residency requirement. IRS tax examiners reviewed the documents a taxpayer submitted and determined whether the residency requirement was satisfied. When the IRS determined that the documentation originally submitted by taxpayers was incomplete or insufficient to establish that the residency requirement was satisfied, taxpayers were afforded repeated opportunities to provide additional documentation. Once residency was established the EITC was allowed.

By its design, the certification test requirement has elements of an educational/outreach program, a “soft-notice” program⁷, and an examination (audit) program. Within the context of the certification test, the objective of the first two elements are to increase voluntary compliance by increasing taxpayers’ awareness and understanding of the EITC qualifying child residency requirement. The content of the materials sent to the taxpayers as well as the actual requirement to certify residency was intended to educate taxpayers to make the correct decision about claiming EITC.

The examination element, which included holding taxpayers’ EITC claim until the documentation for qualifying child residency was reviewed and residency established has several effects. First, it provides a deterrence against erroneous claims because it increases the chances that an incorrect claim will be uncovered. Second, it provides a process whereby IRS can detect erroneous claims due to qualifying child residency errors. Thus, the certification requirement should provide a deterrence to taxpayers who would have intentionally made incorrect claims although they understood they did not meet the qualifying child residency requirement. The certification process also allows the IRS to identify erroneous EITC claims made by taxpayers either because their understanding of the qualifying child residency rules was not increased by the pre-filing mailing or they are intentionally making incorrect claims.

As described earlier, the certification test was designed to include a test group and a control group. The purpose of this design was to enable IRS to separate the effects of the certification requirement on taxpayer behavior from changes that normally occur from one year to the next due to other factors. Because the test and control groups are randomly selected from the same population, in the absence of any special treatment—such as certification—one would expect the behavior of both groups of taxpayers to be the same. In this certification test, the only difference between the test and control groups was the requirement to certify; consequently observed differences between the groups can be attributed to certification.

The IRS evaluated the certification program to determine if the certification process achieved its operational objectives and to assess the impact of the certification process on compliance and participation. Examples of the types of administrative data collected for the study include tax return information, certification process information including data on

⁷ A soft notice is a letter sent to taxpayers generally advising them of a possible issue/error with their return. It generally does not require a response from the taxpayer but encourages them to review what they are doing for mistakes and to avoid repeating them on future returns.

certification-related contacts and documentation, and information collected during mandatory validation.

In addition to the administrative data, a survey of taxpayers was conducted on behalf of the IRS by the Westat Corporation. Excerpts from the final report of the survey are attached in Appendix D. It covers the survey background, development, and implementation in detail, along with the results. The taxpayer survey results provide the IRS with insights about claimants' experiences with the certification process as well as the impact of certification on filing behavior and EITC participation. The IRS used the information self-reported in this survey to determine whether sampled taxpayers who did not claim EITC were eligible for the EITC. The primary use of these estimates was to determine the extent to which the certification requirement unintentionally deterred eligible taxpayers from claiming the credit. The survey data were also used to understand the burden that certification imposed in general and to probe the details of taxpayers' certification experience.⁸

The next section of this report, Section V.D, contains the results of the evaluation. Section V.D.1 presents information about TY 2003 EITC claims and certification outcomes. Section V.D.2 contains information on the characteristics of the study returns and the outcome of certification by these characteristics. The section includes a discussion about the interest for Spanish language forms and assistance and also a discussion of the mobility of the study population. Section V.D.3 looks at test group taxpayers responses to the certification requirement and the documentation submitted to prove residency. Section V.D.4 discusses the mandatory validation process and examines its affect on certification outcomes. Section V.D.5 presents information on the costs of certification for taxpayers and their opinions about the process. Section V.D.6 presents information on IRS costs and lays out a framework for developing a return-on-investment estimate for a fully implemented certification requirement. The effects of the study on participation are discussed in Section V.D.6.a.

V.D Qualifying Child Residency Certification Study, Study Groups

IRS collected and analyzed certification data (Forms 8836 and the Schedule A and B) from taxpayers included in the sample of Qualifying Child Study and other administrative information compiled for the study. The IRS also analyzed the data from the survey of EITC taxpayers conducted by Westat.

The results in this report are based on taxpayer return filings through the end of December 2004 and certification processing activities through late May 2005. The IRS uses a calendar year return processing cycle and typically uses a calendar year period for studies and analyses. This analysis follows that methodology. This report used a calendar year, in this case calendar year 2004, as the period for tracking the TY 2003 tax return filing and EITC claims of study taxpayers. Although most returns that are filed during a calendar year are filed by the April deadline, obtaining more complete and unbiased information and

⁸ While survey data may have limitations, this was believed to be the most effective way to gain information about taxpayer's experiences with the certification program.

conducting a more thorough analysis requires including returns that are filed later in the calendar year. This is especially important for an EITC-related study because some EITC claimants have no requirement to file a tax return other than to claim EITC and, therefore, have no requirement to file a return by April. The analysis covers certification-related activity through the end of May 2005. At the time of the analysis, there were still 414 cases in processing. The final results for these returns were estimated based on the current status they were in and are included in the overall results.

The analysis that follows compares the test and control group results—as well as comparing the results of various subsamples and subgroups—to determine whether there are statistically significant differences between the groups. All the statistical tests in this report were conducted using a 95 percent confidence level. This 95 percent confidence level will be implied in statements made later in the report such as “there is a significant difference” or the results are “not significantly different”.

Table 2 presents the disposition of the original study group for the Qualifying Child Study. IRS selected 25,000 taxpayers for inclusion in the study based on returns filed for TY 2002. The adjusted test group final sample of 24,563 includes 46 taxpayers who filed as married filing jointly in TY 2002 but did not file joint returns in TY 2003. IRS ended up excluding about 2 percent of the original sample after they had been selected because of a change in the taxpayers’ circumstances. These taxpayers resided in a disaster area, were in combat, or their returns were already under examination by IRS.

Table 2: EITC Qualifying Child Residency Certification Study: Number of Study Returns

	Test Groups				Control Group
	Schedule A-English	Schedule B	Schedule A-Spanish	Total	
Original Sample	23,000	1,000	1,000	25,000	25,000
Added -Married Filing Jointly Return Split	40	2	4	46	49
Adjusted Sample	23,040	1,002	1,004	25,046	25,049
Excluded*	432	23	28	483	0
Final Sample	22,608	979	976	24,563	25,049

*The majority (313) of these were excluded prior to the initial mailing. Most were excluded because the taxpayer’s address was in the California wildfire disaster area.

V.D.1 Qualifying Child Residency Certification Study, EITC Claims and Certification Outcomes

This section of the report presents information on the test and control groups’ tax return filing and EITC claim patterns for tax year 2003. It also presents the results of certification for the test groups and compares this to the control group. The control group was subject to standard IRS processes and activities, including selection for examination under existing examination programs that focus on EITC. In the absence of the certification test, the experiences of the test groups would have been expected to be the same as those observed in the control group.

Table 3 presents the status of returns in the study groups. As of the end of December 2004, a total of 22,422 control group returns were filed, or about 90 percent of the control group. This compares with 21,784 test group returns that have been filed, or 89 percent of the test group. About 19 percent or about 4,576 of the test group filed returns but did not claim EITC. This is five percentage points higher than the control group. Approximately three percent of the test group, or 728 returns, claimed the EITC without qualifying children. This is one percentage point higher than the control group percentage. All these differences are significant.

Table 3: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Filing Status for Test and Control Groups

	Test Groups				Control Group
	Schedule A-English	Schedule B	Schedule A-Spanish	Total	
I. Number of Returns					
Final Sample	22,608	979	976	24,563	25,049
Did Not File Tax Return for TY 2003	2,548	95	136	2,779	2,627
Filed Tax Return for TY 2003	20,060	884	840	21,784	22,422
Did Not Claim EITC	4,210	175	191	4,576	3,401
Claimed EITC	15,850	709	649	17,208	19,021
With Children	15,174	681	625	16,480	18,536
<i>Claimed one child</i>	7,694	354	318	8,366	8,930
<i>Claimed two children</i>	7,480	327	307	8,114	9,606
Without Children	676	28	24	728	485
II. Number of Returns as Percent of Final Sample					
Final Sample	100%	100%	100%	100%	100%
Did Not File Tax Return for TY 2003	11%	10%	14%	11%	10%
Filed Tax Return for TY 2003	89%	90%	86%	89%	90%
Did Not Claim EITC	19%	18%	20%	19%	14%
Claimed EITC	70%	72%	66%	70%	76%
With Children	67%	70%	64%	67%	74%
<i>Claimed one child</i>	34%	36%	33%	34%	36%
<i>Claimed two children</i>	33%	33%	31%	33%	38%
Without Children	3%	3%	2%	3%	2%

Note: Percentage detail may not add to total due to rounding.

About 36 percent of the control group claimed EITC with one qualifying child and 38 percent claimed EITC with two qualifying children. Thus a total of about 74 percent of the control group, or 18,536 returns, claimed EITC with qualifying children. About two percent of the control group, or 485 returns, claimed EITC without qualifying children. The remaining return filers, about 14 percent of the control group, or 3,401 returns, did not claim EITC.

Compared with the control group, statistically significantly fewer test group returns claimed EITC with children. About 34 percent of the test group claimed EITC with one qualifying child and 33 percent claimed EITC with two qualifying children. Therefore about 67 percent of the test group, or 16,480 returns, claimed EITC with qualifying children

– about seven percentage points lower than for the control group. Most of the difference between the two groups is attributable to a decline in claims of more than one child.

Taxpayers' responses to survey questions about the reasons that they did not claim EITC suggest that the certification requirement increased taxpayer's awareness and understanding of the qualifying child residency requirement. For taxpayers who reported they did not claim the EITC, 44 percent of those in the test group reported that child residency was a reason they did not claim EITC compared to 18 percent in the control group. (The survey results are discussed in greater detail in Sections V.D.5 and 6 later in the report.)

IRS reviewed administrative information from a data file containing all usages of taxpayer information numbers (TINS) for TY 2003 to learn the TY 2003 usage of all test and control group qualifying child TINS from TY 2002 sample.

In TY 2002, taxpayers in both the test and control group each claimed about 36,600 qualifying children (36,596 and 36,579 respectively). In TY 2003, the test group claimed about 54 percent of the same qualifying children, while the control group claimed 61 percent of the same qualifying children. However, 21 percent of the qualifying children from TY2002 in the test group were claimed by another taxpayer in TY 2003 compared to 18 percent of the control group children being claimed by someone else. Thus it appears that in some cases, certification could have caused a change in who claimed a child for EITC purposes, rather than the child not being claimed at all.⁹

For the subsamples, 11 percent of the Schedule A – English subsample did not file a return compared to 14 percent of the Schedule A – Spanish subsample. Likewise, 70 percent of the Schedule A – English subsample claimed EITC compared to 66 percent of the Schedule A – Spanish subsample. Both of these differences are statistically significant. Conversely, the differences between the Schedule A – English and Schedule B subsamples in the proportion who did not file (11 percent and 10 percent respectively) and the proportion who claimed EITC (70 percent and 72 percent respectively) are not statistically significant.

The data demonstrate that the certification requirement led to reduced EITC claims. As reported in **Table 4** the total amount of EITC claimed by the test group on their returns was about \$37.2 million. This is about \$4.2 million, or approximately 10 percent, less than the \$41.4 million claimed by the control group. However, some of this difference can be attributed to unclaimed EITC by eligible taxpayers who were deterred due to the certification process (see section V.D.6.a for more detailed discussion). The data also indicate that the certification process prevented the payment of erroneous claims for cases where a claim was made but the residency requirement was not met. About \$10.9 million in EITC claims were denied in the certification process. In comparison, for the control group,

⁹ The movement of qualifying children between different taxpayers is something that is not fully understood and IRS plans to study further.

which was subject to ordinary IRS examination processes, approximately \$1.4 million in EITC claims were denied.¹⁰

Table 4: EITC Qualifying Child Residency Certification Study: Amount Claimed and Adjustments (money amounts are in thousands of dollars)

	Test Groups				Control Group
	Schedule A-English	Schedule B	Schedule A-Spanish	Total	
Adjusted Sample Amount EITC Claimed per Taxpayer	\$34,172	\$1,556	\$1,427	\$37,155	\$41,424
Amount EITC Claimed Disallowed in Processing (math error)	\$218	\$12	\$8	\$238	\$232
Adjusted Amount	\$33,954	\$1,544	\$1,419	\$36,918	\$41,191
EITC Claimed on Excluded Cases	\$637	\$20	\$50	\$707	-
Final Sample Claims	\$33,317	\$1,524	\$1,369	\$36,210	\$41,191
Amount EITC Claimed Disallowed in Exam Process (adjustments)	\$9,915	\$566	\$406	\$10,887	\$1,357
Total EITC Claimed Allowed	\$23,402	\$958	\$963	\$25,323	\$39,834
Total EITC Allowed Including Excluded Returns	\$24,038	\$978	\$1,014	\$26,030	\$39,834

Note: Detail may not add to total due to rounding.

Table 5a presents the outcome of the certification process for the test group compared to the outcome for the control group. The control group was subject to normal IRS procedures, including examination under existing programs that focus on EITC. While the entire test group was subject to certification, exactly 500 taxpayers in the control group were selected for examination. All of these exams were for EITC-related issues.

Table 5a: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Outcome of Certification Process for Test Groups Compared to Examination Process for Control Group

	Test Groups			Control Group		
	Number of Returns	Number with Adjustments	Number without Adjustments	Number of Returns	Number with Adjustments	Number without Adjustments
I. Number of Returns						
Claimed EITC	17,208	5,584	11,624	19,021	437	18,584
With Children	16,480	5,580	10,900	18,536	437	18,099
<i>Claimed one child</i>	8,366	2,981	5,385	8,930	170	8,760
<i>Claimed two children</i>	8,114	2,599	5,515	9,606	267	9,339
Without Children	728	4	724	485	0	485
II. Percents	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent
Claimed EITC	100%	32%	68%	100%	2%	98%
With Children	96%	34%	66%	97%	2%	98%
<i>Claimed one child</i>	49%	36%	64%	47%	2%	98%
<i>Claimed two children</i>	47%	32%	68%	51%	3%	97%
Without Children	4%	1%	99%	3%	0%	100%

Note: Percentage detail may not add to total due to rounding.

¹⁰ It is possible that some of the claims that were denied in the certification process (for the test group) or the examination process (for the control group) were made by taxpayers who were actually eligible for the EITC but chose not to substantiate their claims. This taxpayer response also is believed to occur in other situations and, therefore, is not unique either to certification or to EITC.

In the test group, 34 percent of the claims with qualifying children had adjustments made to the amount of EITC claimed compared to 2 percent in the control group. While the number of claims with qualifying children in the test group was split fairly evenly between claiming one child versus two children (8,366 and 8,114 of the returns respectively), 36 percent of the claims for one child had adjustments compared to 32 percent that claimed two children.

Table 5b presents the amount of adjustments made based on the certification process for the test group compared to adjustments made through the standard examination process for the control group. Through the certification process, 30 percent of the claimed amount was denied, compared to 3 percent that was denied through the ordinary examination process in the control group. While a higher proportion of taxpayers claiming one child had adjustments, the adjustment amount for those claiming two children was higher (in part because the credit amount for taxpayers with two children can be larger). The adjustments for two children totaled over \$6 million dollars compared to \$4.8 million in adjustments for claims of one child.

Table 5b: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Status for the Test and Control Groups (money amounts are in thousands of dollars)

	Test Groups			Control Group		
	Amount Claimed	Amount Adjusted	Amount Allowed	Amount Claimed	Amount Adjusted	Amount Allowed
I. Amount of Claims						
Claimed EITC	\$36,210	\$10,887	\$25,323	\$41,191	\$1,357	\$39,834
With Children	\$36,044	\$10,880	\$25,164	\$41,089	\$1,357	\$39,732
<i>Claimed one child</i>	<i>\$14,141</i>	<i>\$4,791</i>	<i>\$9,350</i>	<i>\$15,083</i>	<i>\$402</i>	<i>\$14,681</i>
<i>Claimed two children</i>	<i>\$21,903</i>	<i>\$6,089</i>	<i>\$15,814</i>	<i>\$26,005</i>	<i>\$955</i>	<i>\$25,051</i>
Without Children	\$166	\$7	\$159	\$103	\$0	\$103
II. Percents						
	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent
Claimed EITC	100%	30%	70%	100%	3%	97%
With Children	100%	30%	70%	100%	3%	97%
<i>Claimed one child</i>	<i>39%</i>	<i>34%</i>	<i>66%</i>	<i>37%</i>	<i>3%</i>	<i>97%</i>
<i>Claimed two children</i>	<i>60%</i>	<i>28%</i>	<i>72%</i>	<i>63%</i>	<i>4%</i>	<i>96%</i>
Without Children	*	4%	96%	*	0%	100%

Note: Percentage detail may not add to total due to rounding.

*Less than 0.5 percent

Table 6a, on the following page, presents the outcome of the certification process for the test group subsamples. The 41 percent of Schedule B subsample with adjustments is significantly different from the 34 percent of the Schedule A – English and the 32 percent of Schedule A – Spanish. However, the Schedule A – English and the Schedule A – Spanish adjustment figures are not significantly different from one another.

Table 6b presents the adjustment amounts for the test subsamples. For both Schedule A subsamples, 30 percent of the claimed amounts were denied for a total of \$10.3

Table 6a: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Status for the Test Groups by Subsample

	Test Groups								
	Schedule A-English			Schedule B			Schedule A-Spanish		
	Number of Returns	Number with Adjustments	Number without Adjustments	Number of Returns	Number with Adjustments	Number without Adjustments	Number of Returns	Number with Adjustments	Number without Adjustments
I. Number of Returns									
Claimed EITC With Children	15,174	5,102	10,072	681	277	404	625	201	424
<i>Claimed one child</i>	7,694	2,707	4,987	354	162	192	318	112	206
<i>Claimed two children</i>	7,480	2,395	5,085	327	115	212	307	89	218
II. Percents	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent
Claimed EITC With Children	100%	34%	66%	100%	41%	59%	100%	32%	68%
<i>Claimed one child</i>	51%	35%	65%	52%	46%	54%	51%	35%	65%
<i>Claimed two children</i>	49%	32%	68%	48%	35%	65%	49%	29%	71%

Note: Percentage detail may not add to total due to rounding.

Table 6b: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Status for the Test Groups by Subsample

	Test Groups								
	Schedule A-English			Schedule B			Schedule A-Spanish		
	Amount Claimed	Amount Adjusted	Amount Allowed	Amount Claimed	Amount Adjusted	Amount Allowed	Amount Claimed	Amount Adjusted	Amount Allowed
I. Amount of Claims									
Claimed EITC With Children	\$33,162	\$9,909	\$23,254	\$1,519	\$566	\$953	\$1,363	\$405	\$957
<i>Claimed one child</i>	\$12,999	\$4,330	\$8,669	\$625	\$284	\$340	\$518	\$177	\$341
<i>Claimed two children</i>	\$20,164	\$5,579	\$14,585	\$895	\$281	\$613	\$845	\$228	\$617
II. Percents	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent
Claimed EITC With Children	100%	30%	70%	100%	37%	63%	100%	30%	70%
<i>Claimed one child</i>	39%	33%	67%	41%	46%	54%	38%	34%	66%
<i>Claimed two children</i>	61%	28%	72%	59%	31%	69%	62%	27%	73%

Note: Detail may not add to total due to rounding.

million dollars. The Schedule B subsample had a higher proportion (37 percent) of the claims denied.

The differences between the subsamples shown in Tables 6a and 6b are due in part to the differences in the certification materials provided to each group and in part to the fact that all taxpayers in the Schedule B subsample were subject to mandatory validation, whereas only 10 percent of the Schedule A subsamples (both English and Spanish) were subject to this process. A more detailed discussion of the effects of the mandatory validation process is provided in Section V.D.4. Table 20 in that section shows the impact of mandatory validation on the outcome of the certification process.

V.D.2 Qualifying Child Residency Certification Study, Characteristics

This section of the report looks at the characteristics of the study taxpayers and their returns. This includes the method of tax return filing, i.e. whether the return was filed electronically or on paper, use of a paid preparer, filing status, age, gender, and demand for Spanish language materials and assistance. It also presents information on the outcome of certification for selected characteristics.

Table 7a presents information on the filing medium. Over three-quarters of taxpayers in the test and control group filed electronically. Moreover, of those taxpayers who filed EITC claims with qualifying children, about 81 percent of the test group and 84 percent of the control group filed electronically. These percentages are higher than the percentage of all EITC claimants who file electronically and also of those EITC claimants with qualifying children who file electronically. During calendar year 2004 about 69 percent of all EITC claimants filed electronically as did about 75 percent of EITC claimants with qualifying children.

Table 7a. EITC Qualifying Child Residency Certification Study: Tax Year 2003 Filers' Filing Medium

	Test Groups		Control Group	
	All Tax Return Filers	Claimed EITC with Qualifying Child	All Tax Return Filers	Claimed EITC with Qualifying Child
I. Number of Returns				
Filed Electronically	16,655	13,339	18,033	15,490
Filed on Paper	5,129	3,141	4,389	3,046
Total	21,784	16,480	22,422	18,536
II. Number of Returns as Percent of Total				
Filed Electronically	76%	81%	80%	84%
Filed on Paper	24%	19%	20%	16%
Total	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

The percentage of tax return filers in the test groups who filed on paper was slightly higher than the corresponding percentage for the control group (24 percent versus 20 percent). Taxpayers who claimed EITC with qualifying children also showed this pattern. About 19 percent of taxpayers who claimed EITC with qualifying children in the test group filed on paper compared with 16 percent in the control group. Because the certification

forms were available only for paper filing and the documentation was paper, it would be expected that some taxpayers chose to file their return on paper along with the certification material rather than filing the return electronically and the certification material on paper.

Table 7b presents, by filing medium, the outcome of the certification process for the test groups compared to the outcome of standard processing including the ordinary examination process for the control group. The average amount of EITC claimed by taxpayers who file electronically is higher than the average amount for paper filers for both the test and control. The difference in the averages for electronic filers versus paper filers in the test group is \$168, while the difference in the control group is \$258. In the test group, electronically filed returns have slightly larger amounts of their claim denied compared to paper filers (\$683 versus \$564).

Table 7b: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Status for Taxpayers Claiming EITC with Qualifying Child(ren) by Filing Medium

	Test Groups			Control Group		
	Number of Returns	Average Amount Claimed	Average Amount Allowed	Number of Returns	Average Amount Claimed	Average Amount Allowed
Filed Electronically	13,339	\$2,219	\$1,536	15,490	\$2,259	\$2,187
Filed on Paper	3,141	\$2,051	\$1,487	3,046	\$2,001	\$1,922
Total	16,480	\$2,187	\$1,527	18,536	\$2,217	\$2,143

Note: Detail may not add to total due to rounding.

Table 8a presents information on the use of paid preparers. Over three-quarters of taxpayers in the test and control group used paid preparers. Moreover, of those taxpayers who filed EITC claims with qualifying children, about 80 percent of the test group and control group used paid preparers. For TY 2003 about 69 percent of all EITC claimants used paid preparers.

Table 8a: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Filers' Use of Paid Preparer

	Test Groups		Control Group	
	All Tax Return Filers	Claimed EITC with Qualifying Child	All Tax Return Filers	Claimed EITC with Qualifying Child
I. Number of Returns				
Paid Preparer	16,682	13,164	17,434	14,738
Self Prepared	5,102	3,316	4,988	3,798
Total	21,784	16,480	22,422	18,536
II. Number of Returns as Percent of Total				
Paid Preparer	77%	80%	78%	80%
Self Prepared	23%	20%	22%	20%
Total	100%	100%	100%	100%

Note: Percentage detail may not add to total due to rounding.

Table 8b presents the outcome of the certification process by preparation method for test group taxpayers who claimed EITC with qualifying child(ren). Eighty percent of the test group used paid tax preparers and 81 percent of the total EITC claims were made on returns prepared by paid preparers. The share of paid preparer returns with adjustments was

disproportionate to their share of total returns. Similarly, the share of the total amount of adjustments on returns with paid preparers was disproportionate to their share of total EITC claims. As noted above, about 80 percent of returns used paid preparers but 83 percent of returns with adjustments used paid tax preparers. Similarly, returns with paid preparers accounted for 81 percent of claims but 84 percent of the adjustments.

Table 8b: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Status for Taxpayers Claiming EITC with Qualifying Child(ren) by Use of Paid Preparer (money amounts are in thousands of dollars)

	Number of Returns	Number with Adjustments	Number without Adjustments	Amount Claimed	Amount Adjustments	Amount Allowed
I. Number of Returns and Amount of Claim						
Paid Preparer	13,164	4,659	8,505	\$29,286	\$9,196	\$20,130
Self Prepared	3,316	921	2,395	\$6,758	\$1,724	\$ 5,034
Total	16,480	5,580	10,900	\$36,044	\$10,880	\$25,164
II. Percent of Total						
Paid Preparer	80%	83%	78%	81%	84%	80%
Self Prepared	20%	17%	22%	19%	16%	20%
Total	100%	100%	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

Tables 9a and **9b** present information on the TY 2003 filing status of taxpayers who have filed returns for TY 2003 and are in the test and control groups. **Table 9a** shows that, for the test group, 83 percent (13,622) of those who claimed the EITC with qualifying children filed as head of household. In large part, this high percentage reflects the effect of removing from the sample taxpayers where IRS could systemically determine that the qualifying child claimed by the taxpayer likely met the residency requirement.

Table 9a. EITC Qualifying Child Residency Certification Study: Number of Returns by Filing Status for Tax Year 2003

	Test Groups		Control Group	
	All Tax Return Filers	Claimed EITC with Qualifying Child	All Tax Return Filers	Claimed EITC with Qualifying Child
Single	3,934	1,315	2,991	1,428
Married Filing Jointly	2,393	1,543	2,212	1,506
Married Filing Separately	109	N/A	83	N/A
Head of Household	15,348	13,622	17,136	15,602
Total	21,784	16,480	22,422	18,536

Note: Detail may not add to total due to rounding.

The study population was drawn from TY 2002 EITC claimants with qualifying children whose residency could not be systemically certified. **Table 9b** compares the TY 2003 filing status of the test and control group returns to this TY 2002 information. As reported in the table, for both the test and control groups, the percentage of taxpayers who filed as married filing jointly and claimed the EITC with qualifying children (9 percent and

8 percent, respectively) in TY 2003 was greater than the percentage for the TY 2002 study population (5 percent).

Table 9b: EITC Qualifying Child Residency Certification Study: Percent of Returns by Filing Status for Tax Year 2003

	Test Groups		Control Group		Study Population: TY 2002
	All Tax Return Filers	Claimed EITC with Qualifying Child	All Tax Return Filers	Claimed EITC with Qualifying Child	
Single	18%	8%	13%	8%	9%
Married Filing Jointly	11%	9%	10%	8%	5%
Married Filing Separately	1%	N/A	0%	N/A	0%
Head of Household	70%	83%	76%	84%	85%
Total	100%	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

Tables 10a and 10b present the filing status distributions for TYs 2002 and 2003. **Table 10a** presents the information for all return filers and **Table 10b** for return filers claiming EITC with qualifying children.

As shown in Table 10a, about 77 percent of all filers in the test group (including those not claiming the EITC) and 83 percent of all filers in the control group maintained the same filing status from the previous year. For the test group taxpayers who filed in both years, 13 percent filed as head of household for TY 2002 and filed as single for TY 2003. For those filers included in the control group, however, only about 8 percent changed their filing status from head of household to single.

Table 10a: EITC Qualifying Child Residency Certification Study: Filing Status Distribution for Tax Years 2002 and 2003, All Tax Return Filers

Tax Year 2002 Filing Status	Test Groups				Control Group			
	Tax Year 2003 Filing Status				Tax Year 2003 Filing Status			
	Single	Married Filing Jointly	Head of Household	Total	Single	Married Filing Jointly	Head of Household	Total
Single	5%	1%	3%	9%	5%	0%	3%	9%
Married Filing Jointly	0%	5%	0%	6%	0%	5%	1%	5%
Head of Household	13%	6%	67%	86%	8%	5%	73%	86%
Total	18%	11%	70%	100%	13%	10%	76%	100%

Note: Detail may not add to total due to rounding.

As shown in **Table 10b**, about 89 percent of those taxpayers who claimed the EITC with qualifying children maintained the same filing status from the previous year for the test group as did 88 percent of the control group.

These tables highlight that the filing status distributions appear to have changed between TY 2002 and TY 2003 for both the test and control groups. Results from **Tables 10a and 10b** indicate that some taxpayers in the test group did not claim that they

maintained a household for children, opting instead to file their tax return as single. These taxpayers also appear not to have claimed EITC with children.

Table 10b: EITC Qualifying Child Residency Certification Study: Filing Status Distribution for Tax Years 2002 and 2003, Filers Claiming EITC with Qualifying Child(ren)

Tax Year 2002 Filing Status	Test Groups				Control Group			
	Tax Year 2003 Filing Status				Tax Year 2003 Filing Status			
	Single	Married Filing Jointly	Head of Household	Total	Single	Married Filing Jointly	Head of Household	Total
Single	5%	0%	3%	8%	4%	0%	4%	9%
Married Filing Jointly	0%	5%	1%	5%	0%	4%	1%	5%
Head of Household	3%	4%	79%	86%	3%	3%	80%	86%
Total	8%	9%	83%	100%	8%	8%	84%	100%

Note: Detail may not add to total due to rounding.

Table 11 presents the outcome of the certification process by characteristics of the taxpayer. Taxpayers filing as Head of Household had a disproportionate number of adjustments, accounting for 80 percent of claims but 84 percent of adjustments. Likewise, 62 percent of EITC claims were on returns where the primary taxpayer was male (for joint filers the first taxpayer listed is considered “primary”), while 68 percent of adjustments were for male taxpayers. There is no apparent disparity in the number of adjustments by age category.

Table 11: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Outcome of Certification Process by Characteristics of Taxpayers for Test Groups

	Test Groups					
	Number of Returns	Number with Adjustments	Number without Adjustments	Percent of Total Returns	Percent of Total with Adjustments	Percent of Total without Adjustments
I. Number of Returns						
Filing Status						
Single	1,921	534	1,387	11%	10%	12%
Married Filing Jointly	1,586	371	1,215	9%	7%	10%
Head of Household	13,701	4,679	9,022	80%	84%	78%
Total	17,208	5,584	11,624	100%	100%	100%
Gender						
Male	10,658	3,814	6,844	62%	68%	59%
Female	6,550	1,770	4,780	38%	32%	41%
Total	17,208	5,584	11,624	100%	100%	100%
Age						
Under 20	159	69	90	1%	1%	1%
20-30	5,456	1,865	3,591	32%	33%	31%
31-40	5,059	1,553	3,506	29%	28%	30%
41-50	4,134	1,333	2,801	24%	24%	24%
Over 50	2,400	764	1,636	14%	14%	14%
Total	17,208	5,584	11,624	100%	100%	100%

Note: Detail may not add to total due to rounding.

Spanish Language Interest

Table 12 presents the interest expressed by taxpayers for Spanish language forms and assistance. More than 1,000 test group taxpayers, or about four percent, requested forms or communication in Spanish. About 75 percent, or 712, of these taxpayers, requested that all communication be in Spanish.

Table 12: EITC Qualifying Child Residency Certification Study: Interest in Spanish Language Forms and Assistance for Test Groups

	Test Groups	
	Number	Percent
No request for Spanish forms or assistance	23,932	96%
Request for Spanish forms or assistance	1,114	4%
<i>Request for Spanish version of Notice or Form 8836</i>	93	*
<i>Taxpayer responds in Spanish</i>	78	*
<i>Taxpayer requests Spanish-speaking assistor</i>	231	1%
<i>Taxpayer requests all communication in Spanish</i>	712	3%
Total	25,046	100%

Note: Percentage detail may not add to total due to rounding.

**Less than 0.5 percent*

As described earlier, the IRS sent the Schedule A - Spanish subsample of 1,000 taxpayers letters and forms in both English and Spanish. Of this group, only 8 responded in Spanish. However, IRS received 70 other responses in Spanish from taxpayers in the other subsamples who called and requested the forms in Spanish.

Population Mobility

IRS was interested in understanding the importance of transience or mobility of the population that was selected for the qualifying child study. There are no data that exactly portray the extent of transience in this population of EITC claimants, but several items are suggestive. For instance, about 6 percent of the letters IRS sent to taxpayers in December 2003 were returned as undeliverable, even though addresses were current as of the spring of 2003. More dramatically, almost half (46 percent) of the taxpayers selected for the follow-up telephone survey could not be reached by mail or telephone. And, of the taxpayers who were surveyed, about 7 percent responded that they lived at their current address for less than six months. Taken together, these observations suggest that these EITC claimants are a highly mobile population of taxpayers.

V.D.3 Qualifying Child Residency Certification Study, Response from Taxpayers in the Test Groups

This section of the report presents the test groups' responses to certification, the type of documents submitted to substantiate residency, and the acceptance rate of particular document types and sources. As described earlier, certification required taxpayers to submit Form 8836 and documents substantiating that the taxpayer and child met the EITC qualifying child residency requirement. Each time the IRS received forms and/or documents from a taxpayer, this receipt was recorded in the certification database. Summary

information about each document also was recorded. In addition, the certification materials mailed to the test taxpayers included the special certification toll-free phone number to call for assistance. Each telephone call received from a taxpayer was recorded in the database as long as the taxpayer identified himself or herself during the call.

Taxpayers could submit any combination of documents described in Form 8836 or in the Third Party Affidavit. The residency requirement would be fulfilled if they showed, when taken in combination, that the taxpayer and child lived together for more than half of 2003. In order to be accepted by IRS, all documents submitted to prove residency had to show the child's or taxpayer's name, the address, and the dates at that address. It was not necessary for the taxpayer's and child's names to be on the same piece of documentation.

Individual documents were reviewed by tax examiners for acceptability. As was explained earlier in the report, for the IRS to accept an item, documents had to include the required information, statements or letters needed to be on official letterhead, Third Party Affidavits had to be filled out completely and signed, and all information had to be legible. In reviewing documents, tax examiners did not contact the document provider to verify the authenticity of the document or that the provider had personal knowledge of the residency of the taxpayer and child; rather the examiners focused on identifying acceptable documents on which to base the decision of whether the taxpayer met the EITC residency requirement. Thus, this first-level review involved weeding out documents that did not contain the required information, were not from allowable sources, or were clearly of suspicious origin.

A second level of document validation was conducted on a subset of test group cases. This second level review, called mandatory validation, involved contact with the document provider. Ten percent of the Schedule A subsample taxpayers (both English and Spanish) and 100 percent of the Schedule B subsample taxpayers were included in mandatory validation. For this validation, a core group of lead tax examiners in the certification unit conducted additional validation of the documents that were initially accepted by the tax examiners. This validation involved contact with the document provider to verify that the document was issued or authored by the organization or individual listed on the document and, for letters and affidavits, that the document provider had records or personal knowledge of the residency of the taxpayer and child.

In mandatory validation, the IRS validated a sufficient number of documents to ensure the validity of the EITC claim. Due to workload constraints, not all documents were validated. Thus in cases where taxpayers sent multiple documents covering the same or overlapping time periods, mandatory validation only covered those documents accepted during the initial review by the tax examiners sufficient to establish that the residency requirement was met.

For records, mandatory validation involved verifying that the organization existed. For mandatory validation of letters or affidavits, the lead tax examiners attempted to contact the letter writer or affiant by telephone to verify that the individual had provided the documentation and had the personal knowledge or records to support the residency determination. For Schedule B subsample taxpayers, mandatory validation included the

verification of at least one affidavit from a friend, neighbor, or family member if the taxpayer submitted this type of documentation.

When a document could not be verified in mandatory validation, that document's acceptability indicator on the certification database was changed from "accept" to "reject". Tax examiners used the documents found to be acceptable after both the initial review and mandatory validation to decide whether the taxpayer satisfied the residency requirement.

If the combination of documents originally submitted by taxpayers did not support the residency requirement (for example, if they did not cover the time period of more than half the year) the IRS corresponded with taxpayers and requested additional documentation. Also, if a document was not accepted, either in the initial review or in mandatory validation, and the remaining accepted documents submitted by the taxpayer did not support the residency requirement, the IRS also corresponded with the taxpayer to request additional documentation. Taxpayers were certified for residency when they provided accepted documents that showed that the taxpayer and child lived together for more than half the year.

As noted earlier in the report, mandatory validation appears to affect the certification process and outcome. Therefore, part of the differences shown in the tables in this section may be due to the fact that all taxpayers in the Schedule B subsample were subject to mandatory validation, whereas only 10 percent of the Schedule A subsamples (both English and Spanish) were subject to this process. A more detailed discussion and analysis of the effects of mandatory validation is provided in Section V.D.4.

Results

Table 13 presents, by subsample, the number and percent of responses and whether the response was a phone call, written response (including faxes) or both. About 5 percent of taxpayers who did not file a return for TY 2003 responded. Overall, about 62 percent of test taxpayers responded to the IRS about certification. This pattern is not surprising because only taxpayers claiming EITC with qualifying children were required to certify.

For taxpayers who claimed EITC with children, 89 percent responded to the IRS with 83 percent responding in writing. Thus only 11 percent of taxpayers who claimed EITC with children had no known contact with IRS about certification. About 10 percent of taxpayers who filed a return but did not claim EITC or claimed EITC without qualifying children made some contact with IRS. About half of these taxpayers telephoned the IRS but did not send any materials.

Table 13: EITC Qualifying Child Residency Certification Study: Test Group Responses to IRS

Response	Test Groups			Total
	Schedule A- English	Schedule B	Schedule A- Spanish	
I. Number of Taxpayers				
Any Response	14,072	630	580	15,282
<i>Called and Sent Written Material</i>	9,415	430	386	10,231
<i>Sent Written Materials Only</i>	3,523	151	137	3,811
<i>Called Only</i>	1,134	49	57	1,240
No Response	8,536	349	396	9,281
Grand Total	22,608	979	976	24,563
Did Not File Tax Return for TY 2003				
Any Response*	121	4	6	131
No Response	2,427	91	130	2,648
Total	2,548	95	136	2,779
Filed Tax Return for TY 2003				
Any Response	13,951	626	574	15,151
<i>Called and Sent Written Material</i>	9,398	429	385	10,212
<i>Sent Written Materials Only</i>	3,501	151	135	3,787
<i>Called Only</i>	1,052	46	54	1,152
No Response	6,109	258	266	6,633
Total	20,060	884	840	21,784
Claimed EITC with Children				
Any Response	13,471	608	555	14,634
<i>Called and Sent Written Material</i>	9,286	422	382	10,090
<i>Sent Written Materials Only</i>	3,352	147	132	3,631
<i>Called Only</i>	833	39	41	913
No Response	1,703	73	70	1,846
Total	15,174	681	625	16,480
Claimed One Child				
Any Response	6,733	308	277	7,318
<i>Called and Sent Written Material</i>	4,421	191	170	4,782
<i>Sent Written Materials Only</i>	1,837	93	82	2,012
<i>Called Only</i>	475	24	25	524
No Response	961	46	41	1,048
Total	7,694	354	318	8,366
Claimed Two Children				
Any Response	6,738	300	278	7,316
<i>Called and Sent Written Material</i>	4,865	231	212	5,308
<i>Sent Written Materials Only</i>	1,515	54	50	1,619
<i>Called Only</i>	358	15	16	389
No Response	742	27	29	798
Total	7,480	327	307	8,114
Claimed EITC without Children or Did Not Claim EITC*				
Any Response	480	18	19	517
<i>Called and Sent Written Material</i>	112	7	3	122
<i>Sent Written Materials Only</i>	149	4	3	156
<i>Called Only</i>	219	7	13	239
No Response	4,406	185	196	4,787
Total	4,886	203	215	5,304

Response	Test Groups			Total
	Schedule A- English	Schedule B	Schedule A- Spanish	
II. Percent of Total Responses				
Any Response	62%	64%	59%	62%
<i>Called and Sent Written Material</i>	42%	44%	40%	42%
<i>Sent Written Materials Only</i>	16%	15%	14%	16%
<i>Called Only</i>	5%	5%	6%	5%
No Response	38%	36%	41%	38%
Grand Total	100%	100%	100%	100%
Did Not File Tax Return for TY 2003				
Any Response*	5%	4%	4%	5%
No Response	95%	96%	96%	95%
Total	100%	100%	100%	100%
Filed Tax Return for TY 2003				
Any Response	70%	71%	68%	70%
<i>Called and Sent Written Material</i>	47%	49%	46%	47%
<i>Sent Written Materials Only</i>	17%	17%	16%	17%
<i>Called Only</i>	5%	5%	6%	5%
No Response	30%	29%	32%	30%
Total	100%	100%	100%	100%
Claimed EITC with Children				
Any Response	89%	89%	89%	89%
<i>Called and Sent Written Material</i>	61%	62%	61%	61%
<i>Sent Written Materials Only</i>	22%	22%	21%	22%
<i>Called Only</i>	5%	6%	7%	6%
No Response	11%	11%	11%	11%
Total	100%	100%	100%	100%
Claimed One Child				
Any Response	88%	87%	87%	87%
<i>Called and Sent Written Material</i>	57%	54%	53%	57%
<i>Sent Written Materials Only</i>	24%	26%	26%	24%
<i>Called Only</i>	6%	7%	8%	6%
No Response	12%	13%	13%	13%
Total	100%	100%	100%	100%
Claimed Two Children				
Any Response	90%	92%	91%	90%
<i>Called and Sent Written Material</i>	65%	71%	69%	65%
<i>Sent Written Materials Only</i>	20%	17%	16%	20%
<i>Called Only</i>	5%	5%	5%	5%
No Response	10%	8%	9%	10%
Total	100%	100%	100%	100%
Claimed EITC without Children or Did not Claim EITC*				
Any Response	10%	9%	9%	10%
<i>Called and Sent Written Material</i>	2%	3%	1%	2%
<i>Sent Written Materials Only</i>	3%	2%	1%	3%
<i>Called Only</i>	4%	3%	6%	5%
No Response	90%	91%	91%	90%
Total	100%	100%	100%	100%

* Data combined to avoid disclosure of information for specific taxpayers.

Note: Percentage detail may not add to total due to rounding.

Table 14 presents the distribution of the number of telephone calls made to the IRS for taxpayers who made at least one call and who identified themselves to the IRS. As a part of the Qualifying Child Study, the IRS captured data on the number of calls received from taxpayers. While the IRS captures information on the number of telephone calls, only about half can be associated with the taxpayers who made the calls, because taxpayers do not have to identify themselves to ask general questions about processes. For those calls that could be associated with specific taxpayers, those who received Schedule B tended to call more often than those who received Schedule A. As will be shown later, the higher call volume among Schedule B filers was due in part to mandatory validation.

Table 14: EITC Qualifying Child Residency Certification Study: Distribution of Number of Telephone Calls Made to IRS per Taxpayer as Percent of Taxpayers Who Made Calls

Number of Calls per Taxpayer	Test Groups			Total
	Schedule A-English	Schedule B	Schedule A-Spanish	
1	30%	23%	33%	30%
2-3	32%	29%	30%	32%
4-6	20%	22%	18%	20%
7-10	10%	13%	10%	10%
11 or more	8%	13%	9%	8%
Total	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

Table 15 presents the distribution of document types that each subsample of taxpayers sent to the IRS. The distribution of types of documents is generally the same for the three subsamples. The table shows that 38 percent of documents submitted by taxpayers in the test group were records, 20 percent were official letters, and 42 percent were affidavits from third parties.

The top three sources of all documents (records, letters, and affidavits) submitted were schools, landlords and property managers, and social service or government agencies. About 23 percent of all documents came from schools, about 14 percent were from landlords and property managers, and 11 percent were from social service and government agencies.

While the distribution of document types is generally the same for the three subsamples, the distribution of sources for the Schedule B affidavit is significantly different from the Schedule A affidavit subsamples. Twenty-one percent of the Schedule B subsample chose Neighbor, Family Member, or Friend as their sources compared to one percent or less for the Schedule A subsamples. This difference reflects the fact that only a limited set of individuals could complete Schedule A. The instructions for this schedule included a list of the eligible parties that did not include Neighbor, Family Member, or Friend. Conversely, the instructions for the Schedule B included a list of those who could *not* provide the affidavit (i.e., the taxpayer, the taxpayer’s spouse, the taxpayer’s dependent or EITC qualifying child, and the parent of the EITC qualifying child). Anyone else with personal knowledge of the taxpayer’s situation could furnish a Schedule B affidavit.

Table 15: EITC Qualifying Child Residency Certification Study: Distribution of Documents Submitted by Type of Document—Document Type as Percent of Total

Document Type and Source	Test Groups			Total
	Schedule A-English	Schedule B	Schedule A-Spanish	
Records				
<i>School</i>	11%	9%	9%	10%
<i>Health Care Provider</i>	6%	6%	7%	6%
<i>Landlord or Property Manager</i>	3%	3%	2%	3%
<i>Social Service or Government Agencies</i>	8%	9%	7%	8%
<i>Court Official or Attorney</i>	2%	1%	2%	2%
<i>Utility Bills</i>	3%	4%	3%	3%
<i>Other</i>	6%	5%	6%	6%
Total	38%	37%	36%	38%
Statement/Letter				
<i>School</i>	6%	5%	6%	6%
<i>Health Care Provider</i>	2%	2%	4%	2%
<i>Child Care Provider</i>	1%	1%	1%	1%
<i>Landlord or Property Manager</i>	2%	2%	2%	2%
<i>Social Service or Government Agencies</i>	2%	1%	1%	2%
<i>Utility Bills</i>	1%	1%	1%	1%
<i>Employer</i>	2%	2%	2%	2%
<i>Other</i>	4%	5%	5%	4%
Total	20%	19%	22%	20%
Affidavit				
<i>School</i>	7%	5%	8%	7%
<i>Health Care Provider</i>	3%	1%	3%	3%
<i>Child Care Provider</i>	6%	5%	7%	6%
<i>Landlord or Property Manager</i>	9%	4%	10%	9%
<i>Social Service or Government Agencies</i>	1%	**	**	1%
<i>Court Official or Attorney</i>	1%	**	**	1%
<i>Employer</i>	7%	3%	7%	7%
<i>Neighbor, Family Member, Friend</i>	1%	21%	**	2%
<i>Other</i>	6%	3%	7%	6%
Total	42%	43%	42%	42%
Grand Total	100%	100%	100%	100%

** Less than 0.5%.

Note: Detail may not add to total due to rounding.

Table 16 presents the distribution of the number of documents submitted by taxpayers who submitted at least one document. Taxpayers were required to submit documentation that showed that they met the EITC qualifying child residency requirement. It was up to each taxpayer, however, to decide which documents to submit to meet this requirement. Because taxpayers had to show that they lived with their children for more than half the year and, in some cases, were certifying more than one child, it is not

unexpected that taxpayers submitted multiple documents. In some cases, taxpayers submitted multiple documents for the same child for the same or overlapping time periods.

Table 16: EITC Qualifying Child Residency Certification Study: Distribution of Number of Documents Submitted per Taxpayer as Percent of Taxpayers Who Submitted Documents

Number of Documents per Taxpayer	Test Groups			Total
	Schedule A-English	Schedule B	Schedule A-Spanish	
1	38%	32%	40%	38%
2-3	37%	35%	34%	36%
4-6	19%	21%	20%	19%
7 or more	6%	11%	6%	6%
Total	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

As is shown in the table, nearly two-thirds of taxpayers submitting documents provided more than one. About 38 percent of taxpayers submitted only one document, while 6 percent submitted seven or more documents.

As the distributions in Table 16 show, those taxpayers in the Schedule B subsample tended to submit more documents than those in the Schedule A subsamples. This may be a result of the fact that all taxpayers in the Schedule B subsample were subject to mandatory validation whereas only 10 percent of taxpayers in the Schedule A subsamples were subject to this second level document verification.

It could also be the result of the different styles of the two Third Party Affidavits. As mentioned previously, only a limited set of individuals could complete Schedule A and the schedule included checkboxes for each type of affiant as well as a list of the eligible parties in the instructions. Because the Schedule B could be submitted by a broader range of individuals, it did not include the checkboxes and the instructions included a list of the individuals who could *not* provide the affidavit (i.e., the taxpayer, the taxpayer’s spouse, the taxpayer’s dependent or EITC qualifying child, and the parent of the EITC qualifying child). This could have led taxpayers to seek out multiple parties to provide affidavits.

As noted earlier, documentation submitted by taxpayers to substantiate the residency of the taxpayer and child was reviewed by specially trained tax examiners in the EITC test certification unit in Kansas City. Individual documents were checked for completeness and acceptability and the entire set of documents from a taxpayer was reviewed to ensure that the documentation for the period of joint residency (taxpayer and qualifying child) covered more than half the year. A subset of taxpayers was subject to mandatory validation of their documents.

A total of 1,703 documents for 1,412 taxpayers were verified in the mandatory validation process. The validated documents included 178 records and 1,525 letters and affidavits. Because only 10 percent of the Schedule A subsample taxpayers were included in mandatory validation, only about 6% of the documents submitted by this subsample and accepted during the initial tax examiner review were verified in mandatory validation. For

Schedule B subsample taxpayers—all of whom were part of mandatory validation—about 54 percent of all initially accepted documents were validated, including about 82 percent of affidavits from friends, neighbors, or family members.

Table 17 presents data on the mandatory validation process by document type. About 98 percent of records were accepted by this second level of review, while about 77 percent of letters and about 92 percent of affidavits were validated¹¹. Further analysis of the validation rate for the sources of the affidavits shows that the rate for these documents from friends, neighbors, or family members was 85 percent. This is lower than the overall affidavit rate of 92 percent. The most common reason that letters and affidavits for all types were not accepted during mandatory validation was that the letter writer or affiant could not be contacted. The second most common reason was that the letter writer or affiant did not have personal knowledge of the residency of the taxpayer and child.

Table 18 presents document acceptance rates by type of document. These rates are shown both pre-mandatory validation, based on the initial tax examiner review of documents, and post-mandatory validation, based on the initial tax examiner review and mandatory validation for the subset of documents that were part of the mandatory validation process. The table shows that mandatory validation has almost no effect on the acceptance rates for both the Schedule A English and Spanish subsamples due to the relatively small percentage of taxpayers and documents validated for these subsamples.

The results for the Schedule B subsample, however, are quite different from those for the Schedule A subsamples. The Schedule B subsample pre-mandatory validation and post-mandatory validation acceptance rates for records are identical because 100 percent of the records selected for mandatory validation were validated. The rates for letters and affidavits, however, are different. Because such a high percentage of these types of documents went through mandatory validation, for which the average acceptance rate was about 84 percent, the post-mandatory validation acceptance rates are lower than the pre-mandatory validation rates.

The results from the mandatory validation process and the effect of this process on document acceptance rates suggest that mandatory validation may have had different effects on each of the subsamples. Therefore the outcome of certification for the subsamples may not be calculated by simply comparing the test and control groups. The mandatory validation process appears to have added a new step to the certification process—one that affected all taxpayers who were subject to it. This issue is addressed more fully in Section V.D.4.

¹¹ Since letters and affidavits were not separately identified in the mandatory validation database, they were broken out using information from the certification database.

Table 17: EITC Qualifying Child Residency Certification Study: Mandatory Validation Document Verification Rates by Document Type

Document Type	Test Groups											
	Schedule A-English			Schedule B			Schedule A-Spanish			Total		
	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total
Records	3%	97%	100%	0%	100%	100%	0%	100%	100%	2%	98%	100%
Statement/Letter	22%	78%	100%	28%	72%	100%	30%	70%	100%	23%	77%	100%
Affidavit	6%	94%	100%	12%	88%	100%	8%	92%	100%	8%	92%	100%

Table 18: EITC Qualifying Child Residency Certification Study: Document Acceptance Rates Pre- and Post-Mandatory Validation, by Document Type

Document Type	Test Groups											
	Schedule A-English			Schedule B			Schedule A-Spanish			Total		
	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total
I. Document Acceptance Rates Pre-Mandatory Validation												
Records	51%	49%	100%	57%	43%	100%	52%	48%	100%	52%	48%	100%
Statement/Letter	43%	57%	100%	42%	58%	100%	47%	53%	100%	43%	57%	100%
Affidavit	17%	83%	100%	18%	82%	100%	14%	86%	100%	17%	83%	100%
II. Final Document Acceptance Rates Post-Mandatory Validation												
Records	51%	49%	100%	57%	43%	100%	52%	48%	100%	52%	48%	100%
Statement/Letter	44%	56%	100%	51%	49%	100%	48%	52%	100%	45%	55%	100%
Affidavit	18%	82%	100%	24%	76%	100%	14%	86%	100%	18%	82%	100%

Table 19 on the following page presents the total number of documents submitted by type and source of document. It does this by subgroup and by whether the document was accepted or not based on both the initial review by the tax examiner and mandatory validation for those included in mandatory validation. Taxpayers in the Schedule B subgroup had fewer documents accepted than those in the Schedule A subgroup. This trend holds across both document types and sources, with the exception of affidavits from Neighbor, Family Member, or Friend. This source was generally not accepted for taxpayers in the Schedule A subsamples (both English and Spanish), which requested affidavits only from those sources listed on the Schedule A affidavit and did not include neighbors, family, or friends (except as these categories overlapped with the stated categories).

The overall acceptance rate of documents was 64 percent. Affidavits had the highest acceptance rate of 82 percent, followed by letters with an acceptance rate of 55 percent, and records with a rate of 48 percent. It seems reasonable for affidavits to have a higher acceptance rate than either letters or records because the affidavits were special forms with dedicated lines for all the required information. Therefore, as long as the affidavit was filled out completely, it would contain all the required information to be accepted. With respect to letters and records, it is possible that taxpayers did not understand or disregarded the instructions indicating that the documentation needed to include names, addresses, and dates.

The Qualifying Child Study pioneered the use of affidavits to support the determination of the residency of the qualifying children in the EITC claim. In general, the affidavits seemed to provide a reliable way to substantiate claims in this context.

V.D.4 Qualifying Child Residency Certification Study, The Effect of Mandatory Validation on Certification Outcomes

As discussed previously, documents for a subset of the study taxpayers were subject to mandatory validation. Ten percent of the Schedule A subsample taxpayers (both English and Spanish) and 100 percent of the Schedule B subsample taxpayers were selected for this process. The focus of mandatory validation differed from that of the initial document review. The initial document review concentrated primarily on identifying useable documents on which to base the decision about whether the taxpayer met the EITC residency requirement. Documents that did not contain the required information, were not from allowable sources, or were clearly of suspicious origin were rejected. Mandatory validation, however, focused on verifying that a document was actually issued or authored by the organization or individual listed on the document and—for letters and affidavits—that the document author had records or personal knowledge of the residency of the taxpayer and child.

Because the documents from taxpayers included in mandatory review were subject to greater scrutiny than those of the other taxpayers in the study, mandatory validation may have affected the outcome of certification for the two groups. Furthermore, because 100 percent of the Schedule B subsample taxpayers but only 10 percent of the Schedule A (both English and Spanish) subsample taxpayers were included in mandatory validation, the results for Schedule B subsample taxpayers may not be directly comparable to those for

Table 19: EITC Qualifying Child Residency Certification Study: Documents Submitted by Type and Source by Test Groups

Document Type and Source	Test Groups											
	Schedule A-English			Schedule B			Schedule A-Spanish			Total		
	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total
I. Number of Documents Submitted												
Records												
<i>School</i>	1,392	1,918	3,310	77	73	150	50	59	109	1,519	2,050	3,569
<i>Health Care Provider</i>	1,084	846	1,930	52	43	95	52	35	87	1,188	924	2,112
<i>Landlord or Property Manager</i>	333	596	929	21	21	42	10	18	28	364	635	999
<i>Social Service or Government Agencies</i>	1,470	1,046	2,516	88	56	144	50	44	94	1,608	1,146	2,754
<i>Court Official or Attorney</i>	232	333	565	11	10	21	14	10	24	257	353	610
<i>Utility Bills</i>	542	449	991	37	28	65	20	15	35	599	492	1,091
<i>Other</i>	1,102	651	1,753	59	29	88	36	33	69	1,197	713	1,910
Total	6,155	5,839	11,994	345	260	605	232	214	446	6,732	6,313	13,045
Statement/Letter												
<i>School</i>	666	1,194	1,860	33	47	80	30	42	72	729	1,283	2,012
<i>Health Care Provider</i>	308	431	739	21	15	36	21	24	45	350	470	820
<i>Child Care Provider</i>	168	283	451	8	9	17	10	6	16	186	298	484
<i>Landlord or Property Manager</i>	199	468	667	20	18	38	5	20	25	224	506	730
<i>Social Service or Government Agencies</i>	221	324	545	10	12	22	9	9	18	240	345	585
<i>Utility Bills</i>	139	107	246	7	4	11	9	3	12	155	114	269
<i>Employer</i>	239	380	619	12	14	26	7	19	26	258	413	671
<i>Other</i>	866	343	1,209	50	33	83	43	24	67	959	400	1,359
Total	2,806	3,530	6,336	161	152	313	134	147	281	3,101	3,829	6,930

Document Type and Source	Test Groups											
	Schedule A-English			Schedule B			Schedule A-Spanish			Total		
	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total
Affidavit												
<i>School</i>	354	2,000	2,354	16	60	76	10	93	103	380	2,153	2,533
<i>Health Care Provider</i>	123	712	835	4	13	17	3	33	36	130	758	888
<i>Child Care Provider</i>	296	1,742	2,038	21	66	87	14	70	84	331	1,878	2,209
<i>Landlord or Property Manager</i>	418	2,326	2,744	12	60	72	7	116	123	437	2,502	2,939
<i>Social Service or Government Agencies</i>	72	399	471	*	*	*	*	*	*	72	399	471
<i>Court Official or Attorney</i>	19	183	202	0	5	5	0	5	5	19	193	212
<i>Employer</i>	229	2,044	2,273	8	42	50	10	81	91	247	2,167	2,414
<i>Neighbor, Family Member, Friend</i>	356	31	387	92	245	337	*	*	*	448	276	724
<i>Other</i>	466	1,320	1,786	14	38	52	32	53	85	512	1,411	1,923
Total	2,333	10,757	13,090	167	529	696	76	451	527	2,576	11,737	14,313
Grand Total	11,294	20,126	31,420	673	941	1,614	442	812	1,254	12,409	21,879	34,288

II. Percents (Row Percent)

Records

<i>School</i>	42%	58%	100%	51%	49%	100%	46%	54%	100%	43%	57%	100%
<i>Health Care Provider</i>	56%	44%	100%	55%	45%	100%	60%	40%	100%	56%	44%	100%
<i>Landlord or Property Manager</i>	36%	64%	100%	50%	50%	100%	36%	64%	100%	36%	64%	100%
<i>Social Service or Government Agencies</i>	58%	42%	100%	61%	39%	100%	53%	47%	100%	58%	42%	100%
<i>Court Official or Attorney</i>	41%	59%	100%	52%	48%	100%	58%	42%	100%	42%	58%	100%
<i>Utility Bills</i>	55%	45%	100%	57%	43%	100%	57%	43%	100%	55%	45%	100%
<i>Other</i>	63%	37%	100%	67%	33%	100%	52%	48%	100%	63%	37%	100%
Total	51%	49%	100%	57%	43%	100%	52%	48%	100%	52%	48%	100%

Document Type and Source	Test Groups											
	Schedule A-English			Schedule B			Schedule A-Spanish			Total		
	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total
Statement/Letter												
<i>School</i>	36%	64%	100%	41%	59%	100%	42%	58%	100%	36%	64%	100%
<i>Health Care Provider</i>	42%	58%	100%	58%	42%	100%	47%	53%	100%	43%	57%	100%
<i>Child Care Provider</i>	37%	63%	100%	47%	53%	100%	63%	38%	100%	38%	62%	100%
<i>Landlord or Property Manager</i>	30%	70%	100%	53%	47%	100%	20%	80%	100%	31%	69%	100%
<i>Social Service or Government Agencies</i>	41%	59%	100%	45%	55%	100%	50%	50%	100%	41%	59%	100%
<i>Utility Bills</i>	57%	43%	100%	64%	36%	100%	75%	25%	100%	58%	42%	100%
<i>Employer</i>	39%	61%	100%	46%	54%	100%	27%	73%	100%	38%	62%	100%
<i>Other</i>	72%	28%	100%	60%	40%	100%	64%	36%	100%	71%	29%	100%
Total	44%	56%	100%	51%	49%	100%	48%	52%	100%	45%	55%	100%
Affidavit												
<i>School</i>	15%	85%	100%	21%	79%	100%	10%	90%	100%	15%	85%	100%
<i>Health Care Provider</i>	15%	85%	100%	24%	76%	100%	8%	92%	100%	15%	85%	100%
<i>Child Care Provider</i>	15%	85%	100%	24%	76%	100%	17%	83%	100%	15%	85%	100%
<i>Landlord or Property Manager</i>	15%	85%	100%	17%	83%	100%	6%	94%	100%	15%	85%	100%
<i>Social Service or Government Agencies</i>	15%	85%	100%	*	*	*	*	**	*	15%	85%	100%
<i>Court Official or Attorney</i>	9%	91%	100%	0%	100%	100%	0%	100%	100%	9%	91%	100%
<i>Employer</i>	10%	90%	100%	16%	84%	100%	11%	89%	100%	10%	90%	100%
<i>Neighbor, Family Member, Friend</i>	92%	8%	100%	27%	73%	100%	*	*	*	62%	38%	100%
<i>Other</i>	26%	74%	100%	27%	73%	100%	38%	62%	100%	27%	73%	100%
Total	18%	82%	100%	24%	76%	100%	14%	86%	100%	18%	82%	100%
Grand Total	36%	64%	100%	42%	58%	100%	35%	65%	100%	36%	64%	100%

* Data suppressed to avoid disclosure of information for specific taxpayers.

** Less than 0.5 percent.

Note: Detail may not add to total due to rounding.

the Schedule A subsamples because of the potential effect of the mandatory validation process itself on certification.

To demonstrate that mandatory validation did have an effect on certification, this section of the report presents the study results using a different breakout of study cases than was used in prior sections. The cases are grouped by whether or not they were part of mandatory validation. For those cases that were part of mandatory validation, the Schedule A – English and Schedule A- Spanish subsample cases are grouped together and the Schedule B cases are grouped by themselves.

Table 20a on the following page presents the outcome of the certification process broken out by those taxpayers not subject to mandatory validation, Schedule A (both English and Spanish) taxpayers subject to mandatory validation and Schedule B taxpayers (all of whom were subject to mandatory validation). The percent of mandatory validation cases with adjustments (both Schedule A with 38 percent and Schedule B with 41 percent) is significantly higher than the 33 percent for returns that were not subject to this process. The difference in the proportion of returns with adjustments between the Schedule A mandatory validation taxpayers and Schedule B taxpayers is not significant.

Table 20b presents the amount of adjustments broken out by the mandatory validation groups. For EITC claims with qualifying children, the ratio of adjustments to claims for returns not subject to mandatory validation is 29 percent compared to 34 percent for the Schedule A mandatory subgroup. These two ratios are significantly different. The corresponding ratio for the Schedule B subgroup is 37 percent. This is not significantly different from the Schedule A mandatory validation subgroup. This suggests that the mandatory validation process had a significant impact on the outcome of the certification process. It also indicates that the differences in outcomes between Schedule B and Schedule A taxpayer subsamples in general can be attributed largely to the fact that all Schedule B subsample taxpayers were subject to mandatory validation whereas only 10 percent of the Schedule A subsample taxpayers were. Thus the Schedule B taxpayers received a different treatment in the form of mandatory validation than the majority of the Schedule A taxpayers.

The mandatory validation component of the certification process appears to have uncovered some problems with documents that could not be identified by the initial review. However, since the most common reason that letters or affidavits were rejected was because the letter writer or affiant could not be contacted, it could also have led to the denial of some claims by eligible taxpayers who did not follow-up to provide a replacement document.

Table 20a: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Status for the Mandatory Validation Subgroups within the Test Groups

	Test Groups								
	Non-Mandatory Validation Cases			Mandatory Validation Cases					
	Schedule A-English and Spanish			Schedule A-English and Spanish			Schedule B		
	Number of Returns	Number with Adjustments	Number without Adjustments	Number of Returns	Number with Adjustments	Number without Adjustments	Number of Returns	Number with Adjustments	Number without Adjustments
I. Number of Returns									
Claimed EITC With Children	14,230	4,699	9,531	1,569	604	965	681	277	404
<i>Claimed one child</i>	7,221	2,508	4,713	791	311	480	354	162	192
<i>Claimed two children</i>	7,009	2,191	4,818	778	293	485	327	115	212
II. Percents	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent
Claimed EITC With Children	100%	33%	67%	100%	38%	62%	100%	41%	59%
<i>Claimed one child</i>	51%	35%	65%	50%	39%	61%	52%	46%	54%
<i>Claimed two children</i>	49%	31%	69%	50%	38%	62%	48%	35%	65%

Note: Detail may not add to total due to rounding.

Table 20b: EITC Qualifying Child Residency Certification Study: Tax Year 2003 Return Status for the Mandatory Validation Subgroups within the Test Groups (money amounts are in thousands of dollars)

	Test Groups								
	Non-Mandatory Validation Cases			Mandatory Validation Cases					
	Schedule A-English and Spanish			Schedule A-English and Spanish			Schedule B		
	Amount Claimed	Amount Adjusted	Amount Allowed	Amount Claimed	Amount Adjusted	Amount Allowed	Amount Claimed	Amount Adjusted	Amount Allowed
I. Amount of Claims									
Claimed EITC With Children	\$31,081	\$9,147	\$21,934	\$3,444	\$1,167	\$2,277	\$1,519	\$566	\$953
<i>Claimed one child</i>	\$12,185	\$4,012	\$8,173	\$1,331	\$495	\$837	\$625	\$284	\$340
<i>Claimed two children</i>	\$18,896	\$5,135	\$13,761	\$2,113	\$673	\$1,440	\$895	\$281	\$613
II. Percents	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent	Column Percent	Row Percent	Row Percent
Claimed EITC With Children	100%	29%	71%	100%	34%	66%	100%	37%	63%
<i>Claimed one child</i>	39%	33%	67%	39%	37%	63%	41%	46%	54%
<i>Claimed two children</i>	61%	27%	73%	61%	32%	68%	59%	31%	69%

Note: Detail may not add to total due to rounding.

Table 21 presents, by mandatory validation subgroup, the distribution of the number of telephone calls made to the IRS for taxpayers who made at least one call and who identified themselves to the IRS. As a part of the Qualifying Child Study, the IRS captured data on the number of calls received from taxpayers. While the IRS captures information on the number of telephone calls, only about half can be associated with the taxpayers who made the calls, because taxpayers do not have to identify themselves to ask general questions about processes.

Table 21: EITC Qualifying Child Residency Certification Study: Distribution of Number of Telephone Calls Made to IRS per Taxpayer as Percent of Taxpayers Who Made Calls, by Mandatory Validation Subgroups

Number of Calls per Taxpayer	Test Groups			Total
	Non-Mandatory Validation Cases	Mandatory Validation Cases		
	Schedule A-English & Spanish	Schedule A-English & Spanish	Schedule B	
1	31%	27%	23%	30%
2-3	32%	27%	29%	32%
4-6	20%	21%	22%	20%
7-10	10%	12%	13%	10%
11 or more	7%	13%	13%	8%
Total	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

For those calls that could be associated with taxpayers, those who were in the mandatory validation process tended to call more often than those who were not regardless of whether they received Schedule A or Schedule B. About 46 percent of the Schedule A mandatory validation subgroup taxpayers and 48 percent of the Schedule B subsample taxpayers made four or more telephone calls to the IRS. This compares with 37 percent of the Schedule A non-mandatory validation subgroup taxpayers. This indicates the mandatory validation process primarily drove the difference in call numbers, not the Schedule A or B difference.

Table 22 presents, by mandatory validation subgroup, the distribution of documents by type of document sent to the IRS for each of the mandatory validation subgroups. The table shows that there are no significant differences in the distributions of documents submitted between subgroups.

Table 22: EITC Qualifying Child Residency Certification Study: Distribution of Documents Submitted by Mandatory Validation Subgroup and Type of Document—Document Type as Percent of Total

Document Type	Test Groups			Total
	Non-Mandatory Validation Cases	Mandatory Validation Cases		
	Schedule A-English & Spanish	Schedule A-English & Spanish	Schedule B	
Records	38%	39%	37%	38%
Statement/Letter	20%	20%	19%	20%
Affidavit	42%	41%	43%	42%
Total	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

Table 23 presents, by mandatory validation subgroup, the distribution of the number of documents submitted by taxpayers who submitted at least one document. For returns not in mandatory validation, 25 percent submitted four or more documents, compared to 32 percent of the Schedule A and Schedule B subsample taxpayer in mandatory validation. Those who received Schedule B, all of whom were subject to mandatory validation, tended to submit more documents than those who in the Schedule A subsamples who were part of mandatory validation. However, being part of the mandatory validation process tended to result in taxpayers submitting more documents and appears to be a more important factor in affecting the distribution of the number of documents submitted than is the affidavit subsample. It is logical that mandatory validation would increase the number of documents submitted by taxpayers because it increases the chance that a particular document would not be accepted resulting in the taxpayer having to submit additional documentation to replace the rejects document(s).

Table 23: EITC Qualifying Child Residency Certification Study: Distribution of Number of Documents Submitted per Taxpayer as Percent of Taxpayers Who Submitted Documents, by Mandatory Validation Subgroups

Number of Documents per Taxpayer	Test Groups			Total
	Non-Mandatory Validation Cases	Mandatory Validation Cases		
	Schedule A-English & Spanish	Schedule A-English & Spanish	Schedule B	
1	39%	32%	32%	38%
2-3	36%	36%	35%	36%
4-6	19%	23%	21%	19%
7 or more	6%	9%	11%	6%
Total	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

Table 24 presents the percent of documents accepted by the IRS (this includes both those accepted by the examiner and those accepted in mandatory validation). Taxpayers who received Schedule B had fewer documents accepted than those who received Schedule A regardless of whether the Schedule A taxpayer was in the mandatory validation process or not.

Table 24: EITC Qualifying Child Residency Certification Study: Distribution of Documents Accepted as Percent of Total Submitted by Type

Document Type	Test Groups								
	Non-Mandatory Validation Cases			Mandatory Validation Cases					
	Schedule A-English & Spanish			Schedule A-English & Spanish			Schedule B		
	Rejected	Accepted	Total	Rejected	Accepted	Total	Rejected	Accepted	Total
Records	51%	49%	100%	52%	48%	100%	57%	43%	100%
Statement/Letter	45%	55%	100%	43%	57%	100%	51%	49%	100%
Affidavit	17%	83%	100%	20%	80%	100%	24%	76%	100%
Total	36%	64%	100%	37%	63%	100%	42%	58%	100%

Note: Detail may not add to total due to rounding.

V.D.5 Qualifying Child Residency Certification Study, Taxpayer Costs and Experience

Another focus of this test was to learn how certification affected the time and out-of-pocket costs associated with making an EITC claim. The taxpayer survey included questions about time spent on the return and related activities, the cost of a paid tax preparer, and the amount of other out-of-pocket expenses. Because it would be difficult for taxpayers to separate certification time and costs from time and costs associated with preparing and filing their returns, the test/control group design of the study was used to address this issue. Rather than asking specific questions about burden associated with certification, the difference between the test and control group responses is used to estimate the time and money cost of certification-related activities. In looking at these comparisons however, it should be noted that the majority of the control group returns were not subject to examination. Thus, the comparison primarily is between the certification process versus no treatment, as opposed to certification process versus examination.

Table 25 presents some highlights from the survey results. The percentages of taxpayers who said they filed a tax return, claimed the EITC, and claimed the EITC with qualifying children are broadly consistent with the IRS administrative data reported in Table 4.

V.D.5.a Taxpayer Costs

Being subject to certification appears to increase the amount of time taxpayers expend to make an EITC claim. As reported in Table 25, test group taxpayers reported spending an average of 6.9 hours on their return. Control group taxpayers reported spending about 2.6 hours less, or 4.3 hours. Being subject to certification also appears to increase the likelihood that taxpayers will have to take time off from work to prepare their tax return or to complete the certification process. About 18 percent of test group respondents reported taking time off from work to obtain information to prepare their returns. For the control group, only 9 percent reported taking time off from work to obtain needed information.

Based on the survey data it appears that both test and control group taxpayers who used paid tax preparers paid roughly the same amount for those services. On average the test group reported paying \$136 and the control group reported paying \$132 for tax return preparation. Because the certification requirement was tested on a small number of geographically dispersed taxpayers, it is not surprising that professional tax preparers would not have changed their fee schedules to include an additional charge for certification-related work.

Table 25: EITC Qualifying Child Residency Certification Study: Highlights from Survey Results

Survey Question	Response	Percent of	
		Test	Control
<i>Did you file a 2003 income tax return this year?</i>	Yes	90%	91%
	No	10%	9%
	Don't know	0%	0%
<i>Did you claim EITC on your income tax return for 2003?</i>	Yes	71%	74%
	No	15%	9%
	Don't know	4%	8%
	Other*	11%	9%
<i>For 2003, did you claim the Earned Income Tax Credit with children?</i>	Yes	68%	72%
	No	2%	2%
	Other*	30%	26%
<i>Did you take any time off from work to obtain information you needed for your income tax return, including claiming the EITC?</i>	Yes	18%	9%
	No	71%	80%
	Other*	11%	11%
		Average response	
		Test Groups	Control Group
<i>Roughly how much time did you spend on your return? Please include time for gathering your papers, talking with a tax preparer, getting copies of documents and talking with the IRS.</i>		6.9 hours	4.3 hours
<i>You said you used a paid tax preparer to help you complete your income tax return. Roughly how much did that cost?</i>		\$136	\$132
<i>[Excluding your paid tax preparer,] Roughly how much money did you spend on your return? Please include transportation costs and money spent gathering papers or getting copies of documents.</i>		\$36	\$28
		Test Groups: % who answered very or somewhat	
		Difficult	Easy
<i>How difficult or easy was it to understand the new EITC forms and instructions? Would you say it was...</i>		41%	40%
<i>How difficult or easy was it to decide which documents to use? Would you say it was...</i>		41%	43%
<i>How difficult or easy was it to get the documents you needed to respond to the EITC requirements?</i>		34%	52%
<i>How difficult or easy was it to get assistance from the IRS?</i>		39%	48%
<i>How difficult or easy was it to respond to IRS requests for additional information?</i>		32%	53%
		Percent of	
		Test Groups	Control Group
<i>Do you think taxpayers should be required to prove they meet the EITC requirements before they receive the Earned Income Tax Credit?</i>	Yes	64%	59%
	No	30%	36%
	Don't know	3%	4%
	Other*	3%	1%

* Other includes inapplicable or no response.

With respect to costs other than for preparers, test group taxpayers reported on average about \$36 of other out-of-pocket cost compared with \$28 for control group taxpayers, indicating costs were slightly higher for the test group taxpayers. These costs, however, reflect only the cost of return filing, including certification. Some of the control group returns were subject to examination and therefore would have additional costs associated with this process.

V.D.5.b Taxpayer Opinions About Certification

The taxpayer survey included several questions designed to capture taxpayers' opinions about the certification process. Taxpayers seem to be fairly evenly split in their assessment of the difficulty or ease of completing several of the activities associated with certification.

Taxpayers also appear not to object to the concept of proving eligibility prior to receiving the EITC. About 64 percent of the test group and 59 percent of the control group taxpayers thought that taxpayers should be required to prove they meet the EITC requirements before they received the EITC. About 30 percent of the test group answered no to this question, as did about 36 percent of the control group.

V.D.6 Qualifying Child Residency Certification Study, IRS Costs and Return on Investment

One of the key factors that will ultimately determine whether the IRS proceeds with a broad certification requirement for EITC claimants is the program's Return on Investment (ROI). In other words, the IRS must weigh the costs of administering certification with the benefits certification generates and then compare these results with other potential investment options.

Conducting such an analysis requires that the IRS determine an operating model for a fully fleshed-out program and then estimate the costs and benefits associated with this model. However, the test on which this report is focused sought to evaluate how a certification requirement might affect EITC error and participation rates. The test was not designed to develop an operating model for certification implementation. Thus, this report will not attempt to develop a comprehensive ROI calculation from which decisions about full implementation of a certification program may be made. Instead, it will look at the ROI associated with the TY 2003 Certification Test and discuss the factors that will need to be considered to develop ROI calculations for a full-scale certification process.

V.D.6.a TY 2003 Certification Test Return on Investment

In its simplest form, return on investment is the return in dollars generated from each dollar invested. The IRS attempted to follow this approach in determining ROI for certification. However, because of the nature of tax administration, the IRS has modified the benefits portion of the calculation to incorporate some forms of taxpayer behavior – essentially capturing the deterrent effects of certification. Moreover, the methodology also

adjusts for payments that should have been made to taxpayers who were inappropriately deterred by the certification requirement.

This approach is in keeping with the EITC mission, which commits the IRS to consider not only the reduction in erroneous payments but also the effect on eligible taxpayers when evaluating potential new policies or processes.

Cost of the Test

The total cost to administer the Qualifying Child Certification Test for TY2003 is \$6.6 million. This figure includes expenditures for technology enhancements, contractor support, labor to conduct the certification reviews through the deficiency procedures, and administrative overhead. It reflects the cost to create a special, stand-alone unit in Kansas City, Missouri with dedicated staff and a dedicated information system to administer the test. It also includes staff training and the maintenance and storage costs associated with test data and paperwork. Finally, it includes the test's business process and information systems planning, development and implementation costs. The largest cost component is the labor cost of \$3.6 million, which is about 54 percent of the total cost.

Many of the costs drivers associated with the test would be significantly different in a full-scale implementation. For example, it is unlikely there would be a separate unit or a dedicated staff to administer a full-scale program. Instead, the certification program would be part of a larger tax administration unit. Furthermore, the test does not allow for the economies of scale that would result from having a larger number of taxpayers subject to certification (e.g., spreading the fixed costs of a data system over a larger group of taxpayers). For these reasons, it is not possible to extrapolate the cost of the test to a larger population.

Benefits from the Test

As noted above, calculating the test's benefits involves estimation of several different components. The most straightforward component of the benefit calculation is the amount of revenue protected during the certification process itself. In other words, the dollar amount of refunds that was denied to individuals who claimed the credit and attempted to certify but were unsuccessful. As discussed elsewhere, this figure is \$10.9 million.

The second component is the amount of erroneous EITC claims that would have been made but were deterred by the certification requirement. This estimate is determined by offsetting the total amount of EITC claims that were deterred by the certification requirement by the amount that should have been claimed by eligible taxpayers. Specifically, this is

1. the dollar amount of EITC claims that would otherwise have been made by individuals who did not claim EITC as a result of certification—in other words, all

taxpayers who were deterred by the certification process from claiming the credit regardless of whether they were eligible or ineligible for the credit.

Minus

2. the dollar amount of EITC that would have been claimed by individuals eligible for the EITC but who were deterred by the certification process from claiming the credit.

As noted earlier (see Section V.C.), one goal of the certification process was to increase taxpayers' awareness and understanding of the EITC qualifying child residency requirement. This feature was intended to help taxpayers make the correct decision about claiming the EITC at the time of filing. However, an unintentional consequence of the certification program could be to deter eligible taxpayers from claiming the credit. This could happen for several reasons. A taxpayer may feel that the certification process is too complicated and difficult to maneuver and therefore decide not to claim the EITC. Alternatively, taxpayers may be confused by the information and conclude that they are ineligible for EITC when, in fact, they actually are eligible. In both instances, the certification process may inadvertently deter taxpayers from claiming the EITC.

Table 26 presents the disposition of taxpayers in the study subject to the certification process. As was shown previously (see Table 3), 67 percent of the test group claimed the EITC with qualifying children in TY 2003 and 33 percent did not.

The 67 percent of the test group who claimed EITC with qualifying children consists of taxpayers who documented the residency of their qualifying children and those who did not. About 44 percent of the test group were taxpayers who claimed EITC with qualifying children in TY 2003 and certified that their children met the qualifying child residency requirement. About 23 percent of the test group were taxpayers who claimed EITC with qualifying children on their income tax returns but did not adequately document that the children met the residency requirement.

Table 26: EITC Qualifying Child Residency Certification Study: Test Groups' Tax Year 2003 Return Filing Status and Eligibility

Status	Percent of Test Groups
Non-Claimants*	33%
For Reasons Unrelated to Certification	26%
Deterred by Certification, Eligible for EITC	2.0%-2.5%
Deterred by Certification, Ineligible for EITC	5.0%-4.5%
Claimants with Qualifying Children	67%
Eligible	44%
Ineligible	23%
Total	100%

Note: Detail may not add to total due to rounding.

**Includes taxpayers who claim EITC without qualifying children*

Based on the behavior of the control group, an estimated 26 percent of the test group were taxpayers who would not have claimed the EITC with qualifying children in TY 2003 even without a certification requirement. A similar degree of annual turnover among EITC claimants is observed in the general EITC population and is not unique to this study.

The portion of taxpayers deterred from claiming EITC because of the certification requirement can be estimated by comparing the difference in the percentages of non-claimants in the control and test groups. Based on this calculation (33 percent minus 26 percent), it can be inferred that the certification process deterred about 7 percent of the test group from claiming EITC with qualifying children. Using the survey data for the test group and control group taxpayers, the IRS estimates that about 2.0 to 2.5 percent of the test population was eligible for EITC but deterred by the certification process. This estimate is derived by comparing the test and control group responses to survey questions designed to give a rough estimate of eligibility. Thus, around 4.5 to 5.0 percent of the test population was appropriately deterred from claiming the EITC.

The IRS used administrative and survey data from the certification test to estimate the amount of EITC that would have been claimed by eligible taxpayers who were deterred at \$1.1 to \$1.4 million. The total amount of EITC claims deterred from all taxpayers, both eligible and ineligible, was \$4.3 million. Thus, the amount of erroneous EITC claims that were deterred was between \$2.9 and \$3.2 million.

To determine the net benefit of the TY 2003 Certification Test, we added the revenue protected through the certification process to the amount of EITC that would have been claimed from ineligible taxpayers who were deterred by the certification requirement – a total of \$13.8 to \$14.1 million. From here, estimating the ROI for the test is relatively straightforward. Estimated costs are \$6.6 million and estimated benefits are \$13.8 to \$14.1 million—yielding an ROI of about \$2.10 for every one dollar invested.

Again, this figure cannot be extrapolated to a larger population without significant modification. Moreover, the ROI calculation leaves out other important factors, such as taxpayer burden, which would need to be considered. The ROI also should not be looked at in isolation; but should be compared to the ROI of other potential uses of the same resources.

V.D.6.b Estimating ROI for a Fully-Implemented Certification Requirement

The IRS has not yet defined how a broad implementation of certification might be structured and implemented. Before we can do this, numerous decisions about the process must be made. Without a better sense of an end-state certification program, a robust ROI cannot be estimated.

The IRS is working to identify these key decision points and their effects on the ROI calculation. Here are some of the open questions that must be resolved before making a decision on whether to implement certification:

- How many taxpayers would be asked to certify?
- How often would they be asked to certify?
- How would certification be embedded in or linked to existing exam processes? Would it be a stand-alone program or would it become intertwined with other exam activities?
- Are there alternatives to an examination-type process for dealing with taxpayers who do not provide adequate documentation to certify residency?
- What options does the IRS have to streamline the process? Can certification be automated? Can certification, or at least some portion of it, be accomplished electronically?
- What communications tools and outreach work can the IRS employ to reduce the number of eligible but deterred taxpayers?
- What can the IRS do to address issues associated with the high degree of mobility of EITC claimants?
- What role can or should tax professionals play in this process?
- Could third-parties be allowed to collect certification information for submittal to the IRS?
- How might certification document review be streamlined to improve efficiency?
- What other steps can IRS take to reduce burden on taxpayers who are asked to certify?

In order to determine the best approach from an ROI standpoint, IRS intends to develop scenarios of possible implementation models for certification. These scenarios will be evaluated not only on their ability to maximize ROI but also on their impact on participation and overall EITC error. The objective is to produce an option or set of options that represent the best contribution a certification requirement could make to the overall EITC mission of maximizing participation and minimizing error and fraud.

This analysis will require a significant amount of work. To that end, the IRS has begun a separate project to develop options for implementation. In addition, the IRS has begun a second test of a certification requirement on TY 2004 returns and will need to weigh the results of this and any future tests, the implementation scenarios and any additional or research before making an ultimate determination about certification.

VI. EITC Filing Status Study

The TY 1999 EITC compliance study identified filing status errors as a major contributor to EITC overclaims. Many EITC claimants improperly filed as single or head of household, when they should have filed as either married filing jointly or married filing separately. In numerous cases, using the proper filing status would have substantially reduced the amount of EITC received or made those taxpayers ineligible for the credit altogether.

The Filing Status Study, like the Qualifying Child Study, examined a sample of EITC claimants who may have a high likelihood of filing returns with EITC overclaims. These are taxpayers who previously filed as married (either jointly or separately) and filed as single or head of household for TY 2002. The Filing Status Study investigated the impact of requiring EITC taxpayers to document marital status in order to validate the filing status claimed on their tax return. The study was also designed to test whether a third-party locator service is helpful in identifying taxpayers who may be married and living together but not using the proper filing status.

Taxpayers randomly selected for inclusion in the Filing Status Study were not contacted prior to filing their TY 2003 returns (accordingly, there is no need for a control group to compare filing behavior). When they filed these returns, if they claimed EITC with qualifying children and filed as single or head of household, the EITC portions of their refunds were held by the IRS, and they were asked to provide additional information about marital status. The information requested included documentation of marital status, such as a divorce decree, legal separation papers, or other documentation. IRS examiners used the information furnished by claimants as the sole basis for determining whether the taxpayer's actual marital status was consistent with the filing status claimed on the tax return.

VI.A EITC Filing Status Study Sample Development

In determining the sample frame for the Filing Status Study, the IRS removed the Qualifying Child Study sample frame of 400,000 returns from the 1.6 million returns that comprised the 10 percent random sample of the eligible EITC population. Taxpayers who filed as married filing jointly in TY 2002 were also removed, as were single or head of household returns where the taxpayer had not filed as married filing separately or married filing jointly at least once in the prior three years. The same exclusions were applied to the Filing Status Study sample as were applied to the Qualifying Child Study sample. For example, returns for taxpayers already subject to other treatments by the IRS, such as examination, and returns for taxpayers located in combat or disaster zones were removed from the sample frame. The sample frame for the Filing Status Study consisted of taxpayers filing as single or head of household. From the sample frame (roughly 69,000 taxpayers), a random sample of 36,000 was drawn.

VI.B EITC Filing Status Study Evaluation

As explained above, the Filing Status Study involved notifying taxpayers in the study, after they filed their return, that they needed to provide additional information about their marital status if they filed as single or head of household and claimed EITC with qualifying children. IRS tax examiners reviewed the documents a taxpayer submitted and made a determination whether the taxpayer's actual marital status was consistent with the filing status claimed on the tax return. Taxpayers were provided repeated opportunities to provide additional documentation if the original documentation sent to the IRS was determined to be incomplete or insufficient to confirm their filing status. Once the filing status was confirmed the EITC was allowed and the amount remitted to the taxpayers.

The IRS evaluated the Filing Status Study to determine if it achieved its operational objectives and to assess the impact on compliance. Section VI.C contains results. Examples of administrative data collected for the study include tax return information, data on contacts and documentation related to the study, and data on whether the filing status was confirmed or not. The data reflect taxpayer filings through the end of December 2004 and processing through late May 2005. At the time of the analysis, there were still 105 cases in processing. The final results for these cases were estimated based on their current status and these estimated outcomes are included in the results.

Data from a third party locator service was also analyzed to see if it was helpful in identifying taxpayers who may be married and living together but not using the proper filing status. A new selection algorithm was developed based on the results of this analysis and is being tested for TY 2004.

VI.C EITC Filing Status Study, Status, and Results

IRS selected a sample of 36,000 taxpayer returns to be included in this study. The selected taxpayers had claimed the EITC and filed as single or head of household in TY 2002 but had filed as married filing jointly or separately in at least one of the three previous years.

The disposition of the Filing Status Study sample is presented in **Table 27**. As part of the Filing Status Study, the IRS required those 26,553 taxpayers who filed as single or head of household and claimed EITC with qualifying children in TY 2003 to document marital status. There were 3,748 taxpayers who filed as single or head of household and did not claim EITC or claimed EITC without qualifying children, and 3,137 taxpayers who filed as married for TY 2003; the IRS did not require these two taxpayer groups to document marital status. The IRS excluded 653 taxpayers from the study after they had been selected because these taxpayers were in combat or disaster areas, or their returns were selected for examination on other issues.

Table 27: EITC Filing Status Study: Study Group's Tax Year 2003 Return Status

	Number of Returns	Percent of Total
Final Sample	26,553	
Did Not Yet File Tax Return for TY 2003	1,909	5%
Filed Tax Return for TY 2003	34,091	95%
<i>Single or Head of Household Filing Status and claimed EITC with Qualifying Children</i>	26,553	74%
<i>Single or Head of Household Filing Status and did not claim EITC or claimed EITC without qualifying children</i>	3,748	10%
<i>Married Filing Status</i>	3,137	9%
<i>Excluded – Other (combat, audit)</i>	653	2%
Total	36,000	100%

Note: Percentage detail may not add to total due to rounding.

Table 28 presents the amount of claims and adjustments made. Taxpayers who filed as single or head of household and claimed EITC with qualifying children had \$58.3 million in claims after math error processing. Of this, \$11.9 million, or 20 percent, was disallowed because the taxpayers were unable to provide documentation to support their filing status of single or head of household. In these cases, the IRS treated the taxpayer as married.

Table 28: EITC Filing Status Study: Amount Claimed and Adjustments for Study Group (money amounts are in thousands of dollars)

Adjusted Sample Amount EITC Claimed per Taxpayer	\$58,549
Amount EITC Claimed Disallowed in Processing (math error)	\$231
Final Sample Claims	\$58,317
Amount EITC Claimed Disallowed in Exam Process (adjustments)	\$11,873
Total EITC Claimed Allowed	\$46,444

Note: Detail may not add to total due to rounding.

Table 29 presents the number of returns with adjustments and the amount of those adjustments by filing status. Both the number and the amount of the adjustments were distributed proportionately between single and head of household filers. Single filers account for 6 percent of the study population as well as 6 percent (\$744,000) of the total adjustments. Head of household filers account for 94 percent of the study population and their adjustments of \$11,129,000 made up 94 percent of the total adjustments. Overall, about 22 percent of returns were adjusted.

Table 29: EITC Filing Status Study: Tax Year 2003 Outcome of Filing Status Review (money amounts are in thousands of dollars)

	Number of Returns	Number with Adjustments	Number without Adjustments	Amount Claimed	Amount Adjustments	Amount Allowed
I. Number of Returns and Amount of Claim						
Final Sample	26,553	5,711	20,842	\$58,317	\$11,873	\$46,444
Single filer	1,631	356	1,275	\$3,501	\$744	\$2,756
Head of Household Filer	24,922	5,355	19,567	\$54,816	\$11,129	\$43,688
II. Number of Returns and Amount of Claims as Percent of Final Sample						
Final Sample	100%	100%	100%	100%	100%	100%
Single filer	6%	6%	6%	6%	6%	6%
Head of Household Filer	94%	94%	94%	94%	94%	94%

Note: Detail may not add to total due to rounding.

Table 30 presents information on the filing medium for taxpayers who filed as single or head of household for TY 2003 and claimed the EITC with qualifying children. While 76 percent of the returns were filed electronically, 80 percent of the adjustments were made on electronically filed returns. In other words, about 18 percent of returns filed

on paper were adjusted (1,130 of 6,251) whereas 23 percent of returns filed electronically were adjusted (4,581 of 20,302).

Table 30: EITC Filing Status Study: Filing Medium for Study Group (money amounts are in thousands of dollars)

	Number of Returns	Number with Adjustments	Number without Adjustments	Amount Claimed	Adjustments	Amount Allowed
I. Number of Returns and Amount of Claim						
Filed Electronically	20,302	4,581	15,721	\$45,599	\$9,674	\$35,925
Filed on Paper	6,251	1,130	5,121	\$12,718	\$2,199	\$10,519
Total	26,553	5,711	20,842	\$58,317	\$11,873	\$46,444
II. Percent of Total						
Filed Electronically	76%	80%	75%	78%	81%	77%
Filed on Paper	24%	20%	25%	22%	19%	23%
Total	100%	100%	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

Table 31 presents information on the use of paid preparers. Of the study group, 70 percent used paid preparers, but this group accounted for 77 percent of the amount of adjustments. This is a consequence of the fact that 23 percent of paid preparer returns were adjusted (4,313 of 18,633) compared with only 18 percent for self-prepared (1,398 of 7,920). This indicates that taxpayers using paid preparers have a more difficult time claiming their proper filing status and the correct amount of EITC than those who prepare their returns themselves.

Table 31: EITC Filing Status Study: Study Group's Use of Paid Preparer for Tax Year 2003 Filers (money amounts are in thousands of dollars)

	Number of Returns	Number with Adjustments	Number without Adjustments	Amount Claimed	Adjustments	Amount Allowed
I. Number of Returns and Amount of Claim						
Paid Preparer	18,633	4,313	14,320	\$42,049	\$9,195	\$32,854
Self Prepared	7,920	1,398	6,522	\$16,268	\$2,678	\$13,591
Total	26,553	5,711	20,842	\$58,317	\$11,873	\$46,444
II. Percent of Total						
Paid Preparer	70%	76%	69%	72%	77%	71%
Self Prepared	30%	24%	31%	28%	23%	29%
Total	100%	100%	100%	100%	100%	100%

Note: Detail may not add to total due to rounding.

Table 32 presents the characteristics of taxpayers in the study group along with their claims and associated adjustments. As stated earlier, the sample frame for the Filing Status Study excluded the sample population for the Qualifying Child Study. The reason for the large number of females in the Filing Status Study is because the Qualifying Child

Study sample frame includes a relatively larger proportion of the male head of household filers.

Table 32: EITC Filing Status Study: Outcome of Certification Process by Characteristics of Study Group Taxpayers

	Number of Returns	Number with Adjustments	Number without Adjustments	Percent of Total Returns	Percent of Total with Adjustments	Percent of Total without Adjustments
I. Number of Returns and Amount of Claim						
Gender						
Male	773	134	639	3%	2%	3%
Female	25,780	5,577	20,203	97%	98%	97%
Total	26,553	5,711	20,842	100%	100%	100%
Age						
Under 20	11	4	7	*	*	*
20-30	6,838	1,717	5,121	26%	30%	25%
31-40	11,712	2,549	9,163	44%	45%	44%
41-50	6,835	1,204	5,631	26%	21%	27%
Over 50	1,157	237	920	4%	4%	4%
Total	26,553	5,711	20,842	100%	100%	100%

Note: Detail may not add to total due to rounding.

* Less than 0.5 percent.

The distribution in the Filing Status Study of adjustments by age is disproportionate to the share in the study population. The 20-30 year olds make up 26 percent of the population but had 30 percent of the adjustments. Conversely, 26 percent of the study population was 41-50 years old, but this group accounted for only 21 percent of the adjustments. This indicates that younger people are more likely to incorrectly claim the wrong filing status on their income tax return and consequently, more likely to have made an erroneous claim for EITC than older people.

Table 33 presents the interest expressed by taxpayers in the Filing Status Study for Spanish language forms and assistance. Only about two percent of the study population requested assistance or communication in Spanish.

Table 33: EITC Filing Status Study: Study Group's Interest in Spanish Language Forms and Assistance

	Number	Percent
No request for Spanish forms or assistance	26,025	98%
Request for Spanish forms or assistance	528	2%
Request for Spanish version of Notice	21	*
Taxpayer responds in Spanish	36	*
Taxpayer requests Spanish-speaking assistor	162	1%
Taxpayer requests all communication in Spanish	309	1%
Total	26,553	100%

Note: Percentage detail may not add to total due to rounding.

* Less than 0.5%

Table 34 presents the number of responses and whether it was a phone call, written response (including faxes) or both. The IRS received some kind of response from 92 percent of the 26,553 taxpayers in the study group. Almost two-thirds of the study group called the IRS and about 90 percent sent written material. Taxpayers who did not respond to the IRS request for documentation of their filing status did not receive their EITC claim.

Table 34: EITC Filing Status Study: Study Group Claimant Responses to IRS

	Number	Percent
Any Response	24,558	92%
<i>Called and Sent Written Material</i>	<i>16,145</i>	<i>61%</i>
<i>Sent Written Materials Only</i>	<i>7,662</i>	<i>29%</i>
<i>Called Only</i>	<i>751</i>	<i>3%</i>
No Response	1,995	8%
Total	26,553	100%

Note: Percentage detail may not add to total due to rounding.

Table 35 presents the distribution of the number of calls made to the IRS for taxpayers who made at least one call and who identified themselves to the IRS. As part of the Filing Status Study, the IRS captured data on the number of calls received from taxpayers. While the IRS captures information on the number of telephone calls, only about 70 percent of those calls can be associated with a specific taxpayer. This is because taxpayers do not have to identify themselves in order to ask general questions about the notice they received. For those calls that could be associated with specific taxpayers, the majority (70 percent) made 3 or fewer calls. However, about 12 percent of the study group taxpayers made 7 or more calls.

Table 35: EITC Filing Status Study: Study Group Distribution of Number of Telephone Calls Made to IRS per Taxpayer as Percent of Taxpayers Who Made Calls

Number of Calls per Taxpayer	
1	35%
2-3	35%
4-6	18%
7-10	7%
11 or more	5%
Total	100%

Table 36 depicts, for the Filing Status Study, the distribution of documents by type of document and the source. Records accounted for 77 percent of the documents submitted while 23 percent were official statements or letters. The most frequently submitted documents were divorce decrees. They accounted for about 35 percent of all documents submitted.

Table 36: EITC Filing Status Study: Study Group Distribution of Documents Submitted by Type and Source of Document

Document Type and Source	
Records	
<i>School</i>	1%
<i>Health Care Provider</i>	2%
<i>Landlord or Property Manager</i>	7%
<i>Social Service or Government Agencies</i>	5%
<i>Court Official or Attorney</i>	3%
<i>Divorce Decree</i>	35%
<i>Insurance Policy</i>	3%
<i>Utility Bills</i>	9%
<i>Other</i>	11%
Total	77%
Statement/Letter	
<i>School</i>	1%
<i>Health Care Provider</i>	1%
<i>Landlord or Property Manager</i>	5%
<i>Social Service or Government Agencies</i>	2%
<i>Court Official or Attorney</i>	1%
<i>Insurance Policy</i>	1%
<i>Utility Bills</i>	3%
<i>Employer</i>	2%
<i>Other</i>	8%
Total	23%
Grand Total	100%

Note: Detail may not add to total due to rounding.

Table 37 presents the distribution of the number of documents submitted by taxpayers in the Filing Status Study. (This table covers taxpayers who sent in at least one document.) The majority (68 percent) sent in only one document. The rest sent more than one document. Taxpayers may have sent multiple documents for various reasons. It could be that the IRS did not accept the initial documentation, it may have taken a combination of documents to substantiate their marital status, or the taxpayer may simply have sent more documents than were necessary.

Table 37: EITC Filing Status Study: Study Group Distribution of Number of Documents Submitted per Taxpayer as Percent of Taxpayers Who Submitted Documents

Number of Documents per Taxpayer	
1	68%
2-3	19%
4-6	10%
7 or more	3%
Total	100%

Table 38 presents the document type and source and whether it was accepted or not. Acceptable documentation must have shown that the taxpayer was divorced, legally

separated, or lived apart from his/her spouse for the last six months of 2003. Not surprisingly, Divorce Decrees were the document most likely to be accepted. They were accepted 95% of the time. Documentation from Landlord or Property Managers were also accepted the majority of the time (76 percent acceptance rate for records, 78 percent acceptance rate for statements or letters).

Table 38: EITC Filing Status Study: Total Number of Documents Submitted by Type for Study Group Taxpayers

Document Type and Source	Number of Documents			Percent of Documents		
	Rejected	Accepted	Total	Rejected	Accepted	Total
Records						
<i>School</i>	211	102	313	67%	33%	100%
<i>Health Care Provider</i>	396	393	789	50%	50%	100%
<i>Landlord or Property Manager</i>	660	2,097	2,757	24%	76%	100%
<i>Social Service or Government Agencies</i>	837	1,179	2,016	42%	58%	100%
<i>Court Official or Attorney</i>	384	912	1,296	30%	70%	100%
<i>Divorce Decree</i>	668	13,078	13,746	5%	95%	100%
<i>Insurance Policy</i>	419	887	1,306	32%	68%	100%
<i>Utility Bills</i>	1,554	2,103	3,657	42%	58%	100%
<i>Other</i>	1,589	2,592	4,181	38%	62%	100%
Total	6,718	23,343	30,061	22%	78%	100%
Statement/Letter						
<i>School</i>	126	91	217	58%	42%	100%
<i>Health Care Provider</i>	185	193	378	49%	51%	100%
<i>Landlord or Property Manager</i>	408	1,426	1,834	22%	78%	100%
<i>Social Service or Government Agencies</i>	270	436	706	38%	62%	100%
<i>Court Official or Attorney</i>	112	251	363	31%	69%	100%
<i>Insurance Policy</i>	146	221	367	40%	60%	100%
<i>Utility Bills</i>	523	644	1,167	45%	55%	100%
<i>Employer</i>	226	680	906	25%	75%	100%
<i>Other</i>	1,743	1,323	3,066	57%	43%	100%
Total	3,739	5,265	9,004	42%	58%	100%
Grand Total	10,457	28,608	39,065	27%	73%	100%

Note: Detail may not add to total due to rounding.

VI.D Return on Investment of Filing Status Test

Administration of the filing status test cost approximately \$10.6 million. Of this figure, approximately, \$5.5 million is attributable to “start-up” costs while \$5.1 million is direct labor needed to actually conduct the reviews of the returns. Revenue protected through the process totaled approximately \$12 million – most of which resulted from adjustments to returns of taxpayers who could not verify their claimed filing status. Thus, the return on investment for the test was approximately \$1 for each \$1 invested if all costs are considered. If the fixed or “start-up” costs are removed, to more closely approximate the ongoing cost of continuing the exact same process on an ongoing basis, the ROI is \$2.3 for each \$1 invested. However, these figures cannot be used to project a potential ROI should the IRS implement a filing status documentation requirement.

As with the qualifying child certification test, the filing status test was not structured to identify the most efficient business process. Nor was the test designed to produce an estimate of the ROI that could be expected should the IRS implement some sort

of filing status documentation requirement. In fact, a review of the test by the Treasury Inspector General for Tax Administration (TIGTA) suggested a number of potential changes to the selection process that offer potential for better identifying non-compliant taxpayers. These recommendations coincided with modifications the IRS had already been considering. Thus, for TY 2004, the IRS is conducting a much modified filing status test using a different selection methodology on a smaller group of taxpayers. We will outline the results of this test in a subsequent report.

VII. EITC Automated Underreporter Study

The EITC Compliance Study indicated that income misreporting is among the three most common errors made by taxpayers in claiming the EITC. The Automated Underreporter (AUR) Study was an IRS initiative to focus compliance efforts on taxpayers who claim EITC but are either ineligible because their true income is too high or eligible but overclaim the EITC because of misreported income. The IRS receives information returns from third-party payers who report certain taxpayer income (e.g., wages on a Form W-2 or non-employee compensation on a Form 1099). However, because it takes several months to process and compile, this third-party information is unavailable for matching with tax returns until September and, therefore, cannot be used for income verification when a taxpayer's return is filed and the EITC is paid during the filing season. This limits the ability of the IRS to identify misreported income at the time a return is filed and prevent EITC overclaims during return processing.

Beginning in 2003, the IRS initiated a study that used tax returns filed in TY 2002 to identify, through document matching, EITC claimants with a high likelihood of income reporting errors. The study had two objectives:

- To observe the impact of applying EITC income criteria to AUR-selected cases in order to determine the overall impact on EITC claims; and
- To use the resulting EITC data to update the AUR case selection method so that it identifies EITC claimants with a higher likelihood of income reporting errors.

The AUR study was not a new program and did not create new procedures. In the past, AUR normally would work about 300,000 cases where EITC was claimed, but these cases were not selected specifically to address income misreporting that affected the EITC claim. The focus of the study was to improve the method of selecting these 300,000 cases to specifically address EITC overclaims due to misreported income.

VII.A EITC Automated Underreporter Study Design

The IRS selected 300,000 taxpayers who claimed the EITC and for whom there were indications of income misreporting for TY 2002.¹ These taxpayers were selected

¹ Under normal AUR processing criteria, IRS would have selected approximately the same number of cases that contained an EITC claim for usual AUR follow-up.

from a population of approximately 1.2 million cases in the TY 2002 AUR inventory.² These EITC cases were drawn from AUR inventory based on AUR processing site, the taxpayer’s filing status, the number of children claimed, the EITC claim amount, and the taxpayer’s previous AUR case history. In this study, the IRS did not hold refunds or EITC claims because the returns had already gone through the initial processing months before the information documents were matched to the returns.

VII.B EITC Automated Underreporter Study, Status and Results

The AUR study has been completed with the closure of 299,084 cases. **Table 39** contains information about the disposition of the AUR cases. As noted in earlier reports, all 300,000 cases had been screened as of June 2004. Although the identification of inventory and the initial selection of AUR workload are automated, a tax examiner manually reviews each case. This manual review, referred to as “screening,” sometimes results in a case being closed (“screened-out”) in AUR at this stage. Notices were sent to 261,189 taxpayers inquiring about seemingly misreported income amounts.

Table 39. Automated Underreporter Study: Final as of May 2005

Case Status	Number of Cases
Total Number of Cases in AUR EITC Test	300,000
Number of Cases Screened	300,000
Number of Cases Screened-Out	38,811
Number of Notices Sent	261,189
Total Number of Notice Cases Closed	260,273
Number of Cases Closed With No Change	42,727
Number of Cases Closed With Assessment	216,118
Number of Cases Transferred to Another Operation	1,428

Through the end of May 2005, AUR had closed 299,084 of the 300,000 cases. The remaining cases that have not yet closed are in the statutory notice phase and most of these are in bankruptcy which prevents the IRS from completing work on the case. The disposition of the closures is as follows:

- During the screening phase, 38,811 cases were screened-out; and
- During the response phase, 42,727 were closed without a change to the taxpayer’s return or the EITC, 216,118 cases were closed with an assessment, and 1,428 were transferred to another IRS operation—such as Examination.

Final data from May indicate a reduction or disallowance in EITC of approximately \$250 million and an increase in tax—net of offsetting withholding amounts—of approximately \$134 million. This translates into about \$1,474 per notice case. Both the overall screen-out rate and no-change rates for the study cases, 13 percent and 16 percent respectively are lower than the overall average AUR rates. For cases where EITC was adjusted, the

² The AUR study differs from the Qualifying Child and Filing Status studies in that the taxpayer returns are selected from a different tax year (2002 for AUR and 2003 for the others).

average change was a \$1,157 reduction in the credit. This is an increase of about 17 percent over the average reduction of \$988 for TY 2001

AUR is using the information from this study to improve their workload selection methodology. They also have used information from this study to develop a soft-notice program for selected cases that would not otherwise be worked in AUR. In addition, through this study, AUR identified a sizeable set of issues consolidated under the label of “identity theft” where taxpayers indicated that the information documents associated with their TINs did not belong to them and it appeared that another individual or individuals were using the study taxpayers’ TINs. This is an issue that the IRS is pursuing.

VII.C Return on Investment for Automated Underreporter Study

Unlike the qualifying child certification and filing status tests, the Automated Underreporter Study did not involve a test of a new business process. Instead, the study focused on a change in the way EITC cases were selected for AUR review. In the past, approximately 300,000 cases with EITC claims were part of the AUR program. However, the cases were not selected with any special emphasis on EITC. Rather, the IRS applied an internally-developed algorithm to all tax returns. This algorithm placed no special emphasis on EITC claims. For TY 2002, the IRS essentially reversed this approach – first by culling out all returns with EITC claims and then by applying a special, EITC-focused algorithm to select 300,000 cases for the AUR program.

Because the study was essentially a review of a potential new selection methodology, a return on investment calculation is somewhat premature. The selection methodology for this study, TY 2002, focused on the expected change to EITC and did not incorporate expected changes to tax, other credits, or prepayments. For TY 2003 and subsequent years, the focus has been broadened to incorporate these other items, and therefore, better characterizes the overall impact of the underreported income on revenue. Information from these subsequent studies will provide a better picture of the effect of the change in methodology on revenue in general, rather than on EITC only.

Based on EITC changes only, however, the EITC-specific AUR approach for TY 2002 was an improvement over past practice. The TY 2002 EITC cases had lower than average screenout and no change rates. In addition, for cases where the EITC was changed, the average EITC assessment increased 17 percent from TY 2001 to TY 2002. The average TY 2001 EITC reduction was \$988 compared to \$1,157 for TY 2001 or a 17 percent increase. The total EITC revenue protected from the test was approximately \$250 million.

VIII. Conclusion

This final report fulfills the mandate of the Consolidated Appropriations Act, 2005. It provides an overview of the three EITC initiatives being tested—Qualifying Child Certification, Filing Status, and Automated Underreporter. The data indicate that efforts have, in the aggregate, uncovered many millions of dollars of apparent erroneous claims. The results also point up the need for further testing in the qualifying child and filing status

areas, to better detect EITC claims that may be erroneous without imposing substantial burden on compliant taxpayers.