

GAO

Report to the Chairman, Committee on
Finance, U.S. Senate, and the
Chairman, Committee on Ways and
Means, House of Representatives

June 1990

INFORMATION RETURNS

Correcting Taxpayer Identification Is Possible Without Disclosing Tax Data



141689

179

General Government Division

B-239874

June 5, 1990

The Honorable Lloyd Bentsen
Chairman, Committee on Finance
United States Senate

The Honorable Dan Rostenkowski
Chairman, Committee on Ways and Means
House of Representatives

This report responds to Section 7714 of the Omnibus Budget Reconciliation Act of 1989. Section 7714 requires that we, in consultation with the Secretary of the Treasury or his delegate, study ways to resolve, with the least disclosure of return information possible, discrepancies between taxpayer identification numbers (TIN) and names on information returns and the same information in Internal Revenue Service (IRS) records.

Each year as part of IRS' Information Returns Program, banks and other financial institutions (called "payors") file information returns with IRS. These returns report interest and dividend income payments made by the payors to individuals (called "payees").¹ IRS matches the income on the information returns with that reported by payees on their tax returns. This allows IRS to identify taxpayers who have potentially failed to report all their interest and dividend income. For IRS' matching program to be successful, information about payees on information returns must be accurate. Of the 407 million interest and dividend returns processed for calendar year 1988 (totaling \$511 billion), IRS was unable to match about 20 million, or 5 percent, of the returns. In these cases, the payee's name and/or TIN, which is usually a Social Security number, did not match information in either Social Security or IRS files.

When IRS cannot make a match, it sends the payee's identification number back to payors for them to obtain correct identification numbers and to update their files. In the past, payors have complained that IRS does not provide them with enough information to determine why a mismatch occurred. Payors say that knowing if the mismatch was caused by variations in the payee's name or a transposition error, for example, would make it easier for them to submit correct information the following year. IRS believes that providing payors with specific information would constitute an unauthorized disclosure of taxpayer information.

¹ Although payors sometimes report interest and dividend income payments made to businesses, IRS does not have an Information Returns Program for businesses.

In its Commissioner's 1989 Study of Civil Penalties, IRS recommended that the law be changed to allow it to provide payors with the information they need to correct information returns. Congress—through the Omnibus Budget Revenue Reconciliation Act of 1989—asked us to determine if other options were available.

Results in Brief

There are three things IRS could do, without legislative changes, to help payors resolve incorrect information returns and improve the effectiveness of the Information Returns Program.

First, IRS should ask payors to obtain information on payee name changes not reported to the Social Security Administration (e.g., those due to marriage) when payees open an account with the payor. Payors should then include both names on information returns sent to IRS. IRS, which uses Social Security data in its matching process, is unable to match many information returns because the payee's name differs from the name on record at the Social Security Administration. This is the primary cause of mismatches. Because IRS already can use multiple names in its matching process, the name changes obtained through the payors would allow IRS to match more information returns and eventually reduce the number of incorrect TINs sent back to payors.

Second, IRS should expand its plans to correct taxpayer names on income tax returns. Currently, IRS uses Social Security data to verify TINs and names on income tax returns. Beginning in 1991, IRS plans to adopt procedures that will allow it to update taxpayer accounts using the name reported on the tax return even though it differs from a name on Social Security records. These procedures should benefit the Information Returns Program because the additional taxpayer names will become part of the data base used to match information returns. IRS plans to apply this procedure only to primary filers (those whose names appear on the first name line of a tax return). Based on discussions with IRS officials and statistics reported by IRS Internal Audit, we believe that including the names of secondary filers (those whose names appear on the second line of a joint return) would further benefit IRS' matching program and reduce the number of incorrect TINs returned to payors.

Third, IRS should tell payors when there is no current record of a particular TIN in IRS or Social Security files. This information would help payors isolate the reason why some TINs are incorrect. Moreover, according to IRS' Office of Chief Counsel, this practice does not constitute a disclosure of taxpayer information. IRS attempted to provide this

service for calendar year 1986 and 1987 information returns but because of a computer programming error decided to discontinue it. IRS has since corrected the problem but has not resumed sending payors this information.

Background

When IRS receives information returns from payors, it matches the payee's name and TIN on the information returns against information from Social Security and IRS files. Social Security files show the names and any name changes associated with Social Security numbers; the IRS file contains similar information about names associated with employer identification numbers.² If IRS obtains a match on both the name and TIN, it considers the TIN valid. IRS then matches the validated information returns against tax returns as part of the Information Returns Program.

Those TINs that IRS is unable to validate against Social Security and IRS files are returned to payors as incorrect. Under the Interest and Dividend Tax Compliance Act of 1983, payors are required to ask payees with incorrect TINs to supply a corrected TIN or certify that the TIN they originally provided was correct. Payors then make whatever corrections are necessary before they submit their next information returns to IRS. If the payee fails to certify the TIN, the act requires payors to withhold and remit to Treasury 20 percent of all interest and dividend payments made to a payee's account until the payee provides a certified TIN.

Information returns fail to validate against Social Security and IRS files for a variety of reasons. For example, the payee could provide the wrong TIN to the payor, a payor could make an error when transcribing the TIN or payee's name on an information return, or a payee's name might differ from that associated with the same TIN in Social Security or IRS files. This last reason is one of the more difficult problems to resolve because it may not be due to any error on the information return. For example, IRS would consider the information return incorrect if a recently married woman opened a savings account under her married name but did not notify the Social Security Administration of her name change.

At about the same time that IRS sends its lists of incorrect TINs to payors, it also tries internally to correct the TINs it was unable to validate. For

²An employer identification number is a 9-digit number assigned to a business by IRS.

calendar year 1988 returns, IRS was able to correct about 34 percent of the returns it could not validate.³

In the past, payors have asked IRS to provide more information to explain why TINs are returned as incorrect. Payors contend that knowing how IRS was able to correct some of these TINs would help them make their own corrections. Payors state that it would be helpful to know, for example, whether a TIN failed to match IRS files because of a problem with the TIN itself or because of a problem with the payee's name.

Although IRS would like to provide more information to payors, it believes that to do so might result in an unauthorized disclosure of taxpayer information. Section 6103 of the Internal Revenue Code establishes the general rule of confidentiality and prohibits the disclosure of taxpayer information in the absence of specific statutory authority. IRS' Office of Chief Counsel has concluded that no subsection of 6103 provides explicit authority for IRS to disclose corrected TINs to payors. Moreover, IRS is concerned that even where it has presumably determined that a TIN is correct, it cannot guarantee that the TIN has not been mistakenly associated with some other taxpayer. Thus, IRS runs the risk of disclosing someone else's name or identification number to the payor.

Objective, Scope and Methodology

To meet the requirement of the Omnibus Budget Reconciliation Act of 1989 (Section 7714), our objective was to determine what options exist, without a legislative change, to help payors provide correct names and TINs to IRS.

To determine what options exist to help payors, we relied on our past work that addressed ways to correct TINs, reviewed IRS Internal Audit reports, reviewed IRS statistics compiled on information returns for calendar year 1988, and interviewed officials in the IRS National Office and Central Region. We also interviewed representatives of trade associations for the banking and securities industries, savings institutions, credit unions, and insurance companies to solicit their opinions about what could be done to resolve incorrect TINs.

³Because IRS does not maintain separate records for interest and dividend information returns, the 34 percent correction rate includes other types of information returns, such as reports on employee earnings (Form W-2) and reports on miscellaneous income (Form 1099-MISC).

We reviewed Section 6103 of the Internal Revenue Code to determine what type of information IRS can disclose to payors. We also obtained a legal opinion from the IRS Office of Chief Counsel and made our own legal analysis of the section. To further clarify IRS' responsibilities regarding the disclosure of taxpayer information, we interviewed officials at IRS' National Office in the Offices of the Assistant Commissioner (Examination) and Chief Counsel (Disclosure Litigation).

Time constraints did not permit our obtaining agency comments on this report. Instead, the views of responsible agency officials were sought during the course of our work and are incorporated where appropriate. We did our work from March to May 1990 in accordance with generally accepted government auditing standards.

IRS Should Encourage Payors to Provide More Information About Payee Name Changes

Upon their receipt of an IRS list of incorrect TINs, payors are required to attest to due diligence in obtaining a corrected payee TIN or a certification that the TIN originally provided was correct. Payors are not required to obtain correct names, yet many of the TINs listed are considered incorrect because the names associated with them on the information returns are not the same as the names associated with them in Social Security or IRS files. As part of a review we completed in 1988,⁴ payors told us that they should not be asked to serve as enforcement agents for resolving incorrect TINs resulting from circumstances beyond their control, such as name changes that were not provided to Social Security. They suggested that those problems should be resolved by IRS or the Social Security Administration. While we agree that name mismatches are many times outside payors' control, these types of mismatches continue to pose a problem for both the IRS Information Returns Program and payors.

Of the 407 million interest and dividend information returns processed by IRS for calendar year 1988, IRS could not validate 20 million against Social Security or IRS files. Using IRS' statistics, we estimate that about 16 percent of the 20 million were considered incorrect even though the TIN on the information returns exactly matched a TIN in Social Security and IRS files. IRS considered these returns incorrect because the name on the return did not match the name in those files.

⁴Tax Administration: Accuracy of Taxpayer Identification Numbers on Information Returns Can Be Improved (GAO/GGD-88-110, September 6, 1988).

Even though payors may not be responsible for name mismatches, they end up having to deal with the problem because name mismatches are returned to them for resolution and possible backup withholding. Therefore, we believe payors would respond positively if IRS did more to encourage them to obtain name change information when payees open new accounts. Such information could then be included on the payor's information return for that payee, allowing IRS—whose matching program is set up to accept multiple name lines—to match the information return against its files. And payors would avoid dealing with an incorrect TIN at a later date.

IRS officials believe that they are actively trying to get payors to obtain name change information. For example, TIN certification instructions for existing and new accounts ask payors to obtain payee name changes.⁵ We believe IRS could do more to encourage payors to obtain name changes, for example by making public service announcements and including in its lists of incorrect TINs a message on the importance of obtaining name changes.

IRS Should Expand Plans to Correct Names on Income Tax Returns

Another way IRS could reduce the number of name mismatches in the Information Returns Program would be to expand its plans to correct taxpayer names on income tax returns. IRS uses the same approach in validating taxpayer names and identification numbers on income tax returns that it does in validating information returns. That is, before tax return information is entered onto taxpayers' accounts at IRS' Martinsburg Computer Center, the taxpayer's name and identification number are matched against Social Security data. When the name and number do not match these data, the return is sent back for correction to the IRS service center that originally processed it. At the service centers, the documents are reviewed to identify and correct any IRS errors. If there are no such errors and the problem cannot be corrected internally by IRS, the taxpayer is then contacted to obtain the information needed to correct the problem.

Currently, corrections made by the service centers only resolve the immediate problem—getting IRS' processing system to update the taxpayer's account. In 1991, however, on the basis of a report issued in

⁵IRS instructions for Form W-9 (Request for Taxpayer Identification Number and Certification), which payors are supposed to send to payees with incorrect TINs, state, "... if you have changed your last name, for instance, due to marriage, without informing the Social Security Administration of the name change, please enter your first name and both the last name shown on your social security card and your new last name."

1989 by IRS' Internal Audit Division, IRS plans to begin adding corrections made by service centers to its file of Social Security information. Thus, the next time IRS receives a tax return with the same name problem, the system should update the account. Moreover, the type of corrections that will be added to its Social Security data base file will help resolve name mismatches on information returns. This planned correction process would benefit the Information Returns Program even more if it were expanded to include secondary filers on joint income tax returns. Because IRS' processing system enters income tax return information to the accounts of primary filers, its current correction plans focus only on the primary filers. Secondary filers, however, account for over half the name mismatches on information returns. Of the 4 million calendar year 1988 information returns on which IRS corrected a name, about 2.9 million involved names of secondary filers.

IRS should be able to update secondary filer data easily with minimal changes to existing procedures. Currently, when the name of a secondary filer on a tax return does not match against Social Security files, IRS sends a notice advising the taxpayer to contact Social Security and provide IRS with the information needed to update the taxpayer's account. When IRS receives the updated information, it could add the information to its Social Security data base, much as it plans to do when adding data on primary filers.

The process to add this information will primarily be a manual one and will increase IRS' costs. However, according to IRS officials, the costs should begin to decrease after the first year because many of the names corrected should not require corrections in subsequent years. IRS officials believe that they can expand the process to correct the names of secondary filers. However, they want to see how the process works with primary filers for the first year before including secondary filers.

IRS Should Tell Payors When a TIN Is Not in Social Security or IRS Files

When IRS validates information returns against Social Security and IRS files, it separates the returns into those with incorrect TINs and those with correct TINs. Among the incorrect TINs are those returns with no record of the payee's TIN in Social Security or IRS files.

To help payors determine why it considered some of the TINs incorrect on calendar year 1986 and 1987 information returns, IRS attempted to tell payors which TINs were not in Social Security or IRS files. Unfortunately, according to the TIN Penalty Program Coordinator in IRS' National Office, a programming error resulted in IRS overstating the number of

such TINs and probably hindered more than helped payors' attempts to resolve the incorrect TINs. She said the programming error that overstated the data for calendar year 1986 and 1987 information returns stemmed from IRS' failure to run the incorrect TINs against the IRS file of employer identification numbers—an error that has since been corrected. Because of the bad experience, IRS, according to the coordinator, decided to discontinue sending payors the data.

We believe that IRS should resume sending payors data about TINs that are not in Social Security or IRS files. IRS' Office of Chief Counsel has determined that these data can be shared without risking an unauthorized disclosure of taxpayer information. And we believe providing the data would help payors resolve incorrect TINs. IRS officials agree; they said that the lists of incorrect TINs for calendar year 1989 information returns will identify TINs not currently on Social Security or IRS files.

Conclusions

There are nonlegislative options available to help payors submit correct information returns. Payors can obtain name changes to prevent having to resolve incorrect TINs at a later date. IRS can reduce the number of incorrect TINs sent back to payors for resolution and can supply payors additional information to help them determine why a TIN was considered incorrect. These options do not address all the reasons an information return might be incorrect, but they do address one of the problems that payors find most difficult to resolve—when a payee's name differs from that shown in Social Security and IRS files.

Recommendations to the Commissioner of Internal Revenue

We recommend that the IRS Commissioner

- encourage payors to obtain information from payees about name changes not reported to Social Security when they open new accounts and to include the names on information returns,
- expand IRS' plans to correct names of primary filers on income tax returns to include secondary filers, and
- tell payors when a TIN is not in Social Security or IRS files when providing lists of incorrect TINs to payors.

We will send copies of this report to the Commissioner, Internal Revenue Service, and other interested parties. Major contributors to this report

are listed in the appendix. If you have any questions on this report, please contact me on 275-6407.

Jennie S. Stathis

Jennie S. Stathis
Director, Tax Policy
and Administration Issues

Major Contributors to This Report

**General Government
Division, Washington,
D.C.**

Lynda Willis, Assistant Director, Tax Policy and
Administration Issues

**Cincinnati Regional
Office**

Bob Lidman, Regional Management Representative
Deborah Smith, Evaluator-in-Charge

Requests for copies of GAO reports should be sent to:

**U.S. General Accounting Office
Post Office Box 6015
Gaithersburg, Maryland 20877**

Telephone 202-275-6241

The first five copies of each report are free. Additional copies are \$2.00 each.

There is a 25% discount on orders for 100 or more copies mailed to a single address.

Orders must be prepaid by cash or by check or money order made out to the Superintendent of Documents.

**United States
General Accounting Office
Washington, D.C. 20548**

**Official Business
Penalty for Private Use \$300**

**First-Class Mail
Postage & Fees Paid
GAO
Permit No. G100**
