

**The Health Coverage Tax Credit
Was Accurately Processed
During the 2004 Filing Season**

December 2004

Reference Number: 2005-40-017

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.



DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

INSPECTOR GENERAL
for TAX
ADMINISTRATION

December 10, 2004

MEMORANDUM FOR COMMISSIONER, WAGE AND INVESTMENT DIVISION

Gordon C. Milbourn III

FROM: Gordon C. Milbourn III
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report - The Health Coverage Tax Credit Was
Accurately Processed During the 2004 Filing Season
(Audit # 200440013)

This report presents the results of our review of the processing of the Health Coverage Tax Credit (HCTC, or credit). The overall objective of this review was to determine whether tax returns claiming the HCTC were processed efficiently and accurately during the 2004 Filing Season.¹

The HCTC was established by the Trade Act of 2002² to help certain displaced workers and certain retirees pay for their health insurance. The credit covers 65 percent of the cost of qualified health insurance premiums for eligible individuals and their qualified family members. Taxpayers can receive the credit through advance payments made by the Federal Government directly to the insurer, by claiming the credit on their tax returns, or by a combination of these methods. Our review focused on the processing of the credit claimed on the tax returns. The advance payment process was covered in a separate review by the Government Accountability Office.

In summary, the Internal Revenue Service (IRS) accurately processed returns claiming the credit during the 2004 Filing Season. To minimize erroneous payments, the IRS placed an eligibility indicator on the accounts of potentially eligible taxpayers. This indicator helped prevent over 8,000 ineligible taxpayers from receiving the credit. In addition, the IRS had accurate procedures, controls, and computer programming to ensure returns claiming the HCTC were processed correctly. The IRS also started post-processing reviews of returns with the credit to verify taxpayers were qualified to receive the credit. The methodology used to select these returns was acceptable, and

¹ The period between January and mid-April when most individual income tax returns are filed.

² Pub. L. No. 107-210, 116 Stat 933.

the processes and procedures used for these reviews were sufficient to effectively work the cases.

While the IRS processing of the credit was accurate, we identified processing improvements that could be made. Because the credit amount is combined with other credits on a single line of the U.S. Individual Income Tax Return (Form 1040), manual processing is required to calculate and input the correct credit amount to the IRS return processing system. We also had concerns regarding the post-processing reviews of the credit. First, the IRS function performing the reviews did not have some necessary procedures. This issue was reported to the IRS, and corrective actions have been taken. Second, the legislation that created the credit needs clarification regarding how to properly disallow the credit when taxpayers do not qualify for it. As the statute is written, it appears the credit is not subject to the normal examination process and the IRS can deny the credit without performing an examination; however, special collection requirements apply. This could result in taxpayer rights not being adequately protected and may reduce the possibility that the disallowed credit would be collected.

We recommended the Commissioner, Wage and Investment (W&I) Division, add a specific line for the HCTC to the Form 1040, transcribe information from the Health Coverage Tax Credit (Form 8885) attachment to the Form 1040, and implement pre-refund systemic validity and compliance checks. We also recommended the Commissioner, W&I Division, review the legal status of HCTC disallowances and determine if action by the Congress is necessary.

Management's Response: IRS management stated that while, in concept, they do not disagree with our recommendations and recognize that all of the recommended actions may result in more efficient processing, they can take action on only two of them at this time. IRS management agreed to implement pre- and post-refund validity and compliance checks for Tax Year 2004. IRS management also agreed to work with the IRS Office of Chief Counsel to find appropriate methods for collecting erroneous payments within the context of the existing law. IRS management did not agree to add a specific line for the HCTC to the Form 1040 or to transcribe information from the Form 8885. Management's complete response to the draft report is included as Appendix IV.

Office of Audit Comment: We understand the rationale behind IRS management's decision to not implement one of our recommendations. IRS management stated that although they see the benefit of adding a line for the HCTC, there is no space on the current Form 1040. Furthermore, without a new line for the HCTC, there would be no need to transcribe the Form 8885 information because it would not enhance the current process. While we still believe adding a specific line to the Form 1040 and transcribing the information from the Form 8885 would improve the administration and enforcement of the HCTC Program, we accept IRS management's explanation for not implementing the recommendation stated above.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Michael R. Phillips, Assistant Inspector General for Audit (Wage and Investment Income Programs), at (202) 927-0597.

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The Health Coverage Tax Credit Was Accurately Processed During the 2004 Filing Season

Background

The Health Coverage Tax Credit (HCTC, or credit) was created by the Trade Act of 2002¹ to help certain displaced workers and certain retirees pay for health insurance. Generally, taxpayers eligible to claim the credit fall into one of two categories:

- Trade-affected workers who have lost their jobs because of increased imports or a shift in production to another country. These taxpayers must be classified as Trade Adjustment Assistance (TAA) or Alternative Trade Adjustment Assistance eligible.²
- Individuals whose pensions are being paid by the Pension Benefit Guaranty Corporation (PBGC), are at least 55 years of age, and are not entitled to Medicare.

The credit covers 65 percent of the cost of qualified health insurance premiums for eligible individuals and qualified family members. To receive the credit, the taxpayer must be enrolled in a qualified health insurance plan.

Taxpayers can receive the credit through an advance payment option, where the Federal Government pays 65 percent of the health insurance premiums directly to the insurer, or by claiming the credit on their Federal income tax returns. Taxpayers can also receive the credit through a combination of the two.

This credit is refundable, meaning taxpayers can claim the credit on their tax returns and receive a refund even if they did not owe any taxes or earn any income. The credit could first be claimed for the month of December 2002, with Tax Year (TY) 2003 being the first full year for the credit. The credit is administered by the Internal Revenue Service (IRS) HCTC Program Office, in conjunction with other Federal Government and state agencies and private industry.

Taxpayers claimed and received \$30.5 million of the credit on TY 2003 returns³ and received an additional \$7 million of advance payments during Calendar Year 2003. The

¹ Pub. L. No. 107-210, 116 Stat 933.

² Employees must be certified as TAA eligible by the Department of Labor.

³ Through May 31, 2004.

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HCTC Program Office reported the startup administration costs for the Program as being approximately \$69 million through April 30, 2004, and projected annual operational costs are \$40 million.

The IRS initially expected approximately 250,000 taxpayers would be eligible for the credit. However, the number of taxpayers claiming the credit on their TY 2003 returns was less than 17,000.⁴ The IRS is conducting research to determine the reasons for the difference in numbers, but this research has not been finalized. In addition, an audit was recently conducted by the Government Accountability Office that addresses this issue.

This review was performed at the HCTC Program Office in the IRS National Headquarters in Washington, D.C.; the Wage and Investment (W&I) Division Compliance Site in Austin, Texas; and the W&I Division Submission Processing Sites in Fresno, California, and Memphis, Tennessee, during the period March through August 2004. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Returns Claiming the Credit Were Accurately Processed During the 2004 Filing Season

The IRS accurately processed returns claiming the credit during the 2004 Filing Season.⁵ We determined that eligibility indicators were correctly posted, tax returns claiming the credit were accurately and efficiently processed, and post-processing actions were sufficient.

The IRS instituted an eligibility indicator on taxpayer accounts to prevent erroneous payments

The HCTC Program Office instituted various controls to ensure only eligible taxpayers would receive the credit and help minimize erroneous payments. The most important of these controls was an indicator placed on potentially eligible taxpayers' accounts. Taxpayers potentially eligible for the

⁴ Taxpayers that claimed and received the credit on their TY 2003 returns through May 31, 2004.

⁵ The period between January and mid-April when most individual income tax returns are filed.

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credit were reported to the HCTC Program Office by the PBGC and the states' workforce agencies. The credit was disallowed during return processing if a taxpayer attempted to claim the credit without the indicator being present on his or her account.

We compared the number of potentially eligible taxpayers reported to the HCTC Program Office with the number of indicators actually placed on taxpayer accounts and determined that they matched. Placing this indicator on taxpayer accounts helped prevent over 8,000 ineligible taxpayers from receiving the credit.

Controls were in place to accurately process returns claiming the credit

During the 2004 Filing Season, returns claiming the credit were computer identified and then manually processed. The computer programming logic used to identify these returns was accurate, and the procedures used by the processing functions to manually process the returns were accurate. In addition, we verified that other controls implemented by the HCTC Program Office were working. These included a control that verified if taxpayers claiming the credit met age requirements and controls related to electronic filing.

Appropriate post-processing actions were taken to identify and assess ineligible taxpayers

In addition to the controls implemented to prevent ineligible claims for the credit during return processing, the HCTC Program Office also started post-processing reviews of returns to verify that taxpayers claiming the credit had a qualifying health plan. Even if taxpayers were reported as potentially eligible for the credit, they must also have a qualifying health plan. We reviewed the methodology used to select these returns for review and determined it was adequate. We also analyzed the processes and procedures used to review these returns and determined that they were sufficient to ensure the cases were reviewed effectively.

Although the IRS accurately processed returns claiming the credit and took appropriate post-processing actions, improvements could be made to both of these areas.

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Automating the Manual Processing of Tax Returns With the Credit Could Improve Efficiency

Currently, returns claiming the credit are computer identified and then manually processed. The credit is claimed on Line 67 (Other Payments) of the U.S. Individual Income Tax Return (Form 1040). Other credits and payments can be claimed on this line as well, and the amounts are combined into a single total. In addition, the information on the Health Coverage Tax Credit (Form 8885) attachment to the return is not transcribed into the IRS return processing system.

Because there is no separate line item or total specifically for the credit and information from the Form 8885 is not transcribed, manual processing is required to verify and input the credit amount into the IRS return processing system. In accordance with the IRS strategic goal of improving agency operations by reengineering business processes, this process should be automated to increase efficiency and effectiveness.

Since the credit amount is not identified during initial return processing, systemic computer validity checks cannot be performed and employees must manually verify the return. This increases the possibility of manual input errors and increases resource costs to process these returns. Furthermore, compliance checks to ensure taxpayers are not overclaiming the credit cannot be implemented using the current information input from the return.

Recommendations

To more efficiently process returns claiming the credit, the Commissioner, W&I Division, should:

1. Insert a specific line on the Form 1040 for the credit and transcribe the information on Form 8885.

Management's Response: Although IRS management sees the benefit of adding the line, there is not space on the current Form 1040. Further, the relatively small number of taxpayers who are potentially eligible for the HCTC does not justify the elimination or consolidation of other lines to make room for a separate HCTC line at this time. Without a new line for the HCTC, there would be no need to transcribe the Form 8885 information because it would not enhance the current process. IRS management did agree to consider

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including a line for the credit on future revisions of Form 1040. The IRS is currently exploring options to redesign the Form 1040 to give more flexibility in implementing new statutory reporting requirements and reduce taxpayer burden.

Office of Audit Comment: We understand and accept the rationale behind IRS management's decision to not implement this recommendation at this time. We still believe adding a specific line to the Form 1040 and transcribing the information from the Form 8885 would improve the administration and enforcement of the HCTC Program; therefore, we encourage the IRS to pursue adding a line for the HCTC on future revisions of the Form 1040.

2. If Form 8885 information is transcribed, develop and implement appropriate systemic validity and compliance checks using the transcribed information. For example, a math check could be programmed to verify that the taxpayer properly computed his or her credit as 65 percent of the total premium amount paid.

Management's Response: Although IRS management will not transcribe Form 8885 information, the IRS agreed to implement systemic validity and compliance checks that do not require transcription.

Concerns Were Identified With the Post-processing Reviews of the Credit

Some returns claiming the credit were reviewed after the credit had been allowed during return processing. This was done so the IRS could verify that the taxpayer had a qualifying health plan. Because of the specific statutory language that created the credit, the IRS is treating credits disallowed during these reviews as erroneous refunds. The IRS should be using special erroneous refund procedures⁶ to collect the disallowed credits, and we identified two concerns related to these special procedures.

⁶ Erroneous refunds have requirements for collection different from those for regular tax assessments, and they have a unique statute of limitations. Accordingly, special procedures are required when processing these cases.

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The IRS function reviewing returns claiming the credit did not have complete procedures

The function verifying eligibility for the credit had procedures sufficient to ensure cases were reviewed effectively. However, these procedures did not contain instructions to properly process the cases after the credit was disallowed and the review closed. This resulted in the function not taking additional actions necessary to resolve the cases. We reported this issue to the HCTC Program Office during March 2004. This omission was caused by an oversight during the development of the original instructions.

If cases had been processed without following erroneous refund procedures, affected taxpayers could have been subject to inappropriate collection actions. Because this issue was rapidly identified and corrected, we have no indication any taxpayers were affected.

Management Action: After we reported this issue to the HCTC Program Office, it immediately began implementing interim procedures for these cases. In addition, permanent procedures are now being incorporated into the relevant Internal Revenue Manual.⁷

The legislation that created the credit needs clarification

The statute governing the credit does not specify how to disallow and recover erroneous credits. All other refundable credits are specifically addressed in the Internal Revenue Code⁸ as being subject to deficiency procedures,⁹ which means they can be disallowed by the IRS only through a formal examination. However, the HCTC was not expressly included with the other credits in the statute. Accordingly, the IRS has taken the position that the credit can be disallowed without performing an examination and the

⁷ The official procedures of the IRS.

⁸ I.R.C. § 6211(b)(4)(A).

⁹ Deficiency procedures are used by the IRS during a formal examination. A deficiency is the difference between the tax amount computed by the IRS and the tax amount actually reported by the taxpayer on his or her return. Tax assessment amounts proposed under deficiency procedures can be appealed to the U.S. Tax Court.

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amount disallowed should be classified as an erroneous refund.

Erroneous refunds have different, much more restrictive, collection requirements than those applied to typical examination assessments. We believe classification of HCTC disallowances as erroneous refunds could compromise the collectibility of the assessments. For example, credit amounts that have been determined to be erroneous can be collected only through limited actions, and the statute of limitations for collection expires sooner than for normal examination assessments. Accordingly, it is logical to assume that some of the erroneous credit amounts issued may never be recovered. However, because the Program is so new there are no historical data to determine collectibility rates.

In addition, there is the potential that taxpayer rights may not be adequately protected. Taxpayers are given certain rights during the normal examination process, including the right to file a petition with the Tax Court. However, taxpayers that have the HCTC denied do not have this right. In fact, according to the IRS these taxpayers have no formal right of appeal at any level, although it has indicated it will allow courtesy appeals.

Due to our concerns about collectibility and taxpayer rights, we believe it would be appropriate for the IRS to review this issue further. We understand that any changes would have to be implemented via legislation and that this would have an affect on other aspects of the Program, including advance payments.

Recommendation

To help clarify the legal status of certain post-processing actions, the Commissioner, W&I Division, should:

3. Coordinate with the HCTC Program Office and the Office of Chief Counsel to review the issue of the legal status of HCTC disallowances and to determine if action by the Congress is necessary.

Management's Response: IRS management has been working with the Office of Chief Counsel to find

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appropriate methods for collecting erroneous payments within the context of the existing law. IRS management has addressed many of these issues with the Office of Chief Counsel and will maintain that dialogue and further determine the need for and/or the possibility of legislative clarification in this area.

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Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of our review was to determine whether tax returns claiming the Health Coverage Tax Credit (HCTC, or credit) were processed efficiently and accurately during the 2004 Filing Season.¹ This included determining the sufficiency of post-processing reviews to verify eligibility. We did not include the advance payment process in our review because it was covered in a separate review by the Government Accountability Office.

To accomplish our objective we:

- I. Determined if the HCTC eligibility indicator was properly placed on taxpayer accounts by obtaining the number of potentially eligible taxpayers from the HCTC Program Office and comparing it with the number of taxpayer accounts with an indicator. These accounts were identified by a computer data extract, using the indicator as the criteria.
- II. Determined if the Submission Processing Error Resolution System (ERS) and Unpostable functions accurately and efficiently processed returns claiming the credit.
 - A. Reviewed and verified whether the computer logic used by the two functions was correctly programmed. This was accomplished by analyzing relevant computer documentation and reviewing judgmental samples of 63 returns with the credit that were computer identified and referred to the ERS and Unpostable functions. The samples of 63 returns consisted of 36 returns selected from the ERS functions and 27 returns selected from the Unpostable functions in the Fresno, California, and Memphis, Tennessee, Submission Processing Sites on various days. We were unable to accurately determine the population of tax returns processed by these functions on those days. Judgmental samples were used because we did not plan to project the results.
 - B. Reviewed the procedures used by the ERS and Unpostable functions to verify whether they adequately enabled employees to accurately and efficiently process returns claiming the credit.
 - C. Verified the accuracy of the HCTC information posting to taxpayer accounts. This was accomplished by obtaining a computer extract of all returns with the credit being processed each week from January 1, 2004, through May 31, 2004. This information was reviewed for accuracy, including determining if limit checks on the credit were working properly and if other controls were in place and working properly.

¹ The period between January and mid-April when most individual income tax returns are filed.

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- III. Determined if post-processing reviews of returns for eligibility were sufficient to identify and assess returns for taxpayers that were not eligible for the credit.
 - A. Interviewed HCTC Program personnel to determine their selection process and analyzed their methodology to determine if it was valid.
 - B. Reviewed the process and procedures used to review the returns for eligibility.

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Appendix II

Major Contributors to This Report

Michael R. Phillips, Assistant Inspector General for Audit (Wage and Investment Income Programs)

Scott A. Macfarlane, Director

Richard J. Calderon, Audit Manager

Steven D. Stephens, Lead Auditor

Bonnie G. Shanks, Auditor

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Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
Deputy Commissioner for Services and Enforcement SE
Commissioner, Small Business/Self-Employed Division SE:S
Deputy Commissioner, Small Business/Self-Employed Division SE:S
Deputy Commissioner, Wage and Investment Division SE:W
Director, Communications and Liaison, Small Business/Self-Employed Division SE:S:C&L
Director, Compliance, Wage and Investment Division SE:W:CP
Director, Customer Account Services, Wage and Investment Division SE:W:CAS
Director, Health Coverage Tax Credit Program, Wage and Investment Division SE:W:HCTC
Director, Strategy and Finance, Wage and Investment Division SE:W:S
Chief, Performance Improvement, Wage and Investment Division SE:W:S:PI
Director, Submission Processing, Wage and Investment Division SE:W:CAS:SP
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Office of Management Controls OS:CFO:AR:M
Audit Liaisons:
 Chief, Customer Liaison, Small Business/Self-Employed Division SE:S:COM
 Senior Operations Advisor, Wage and Investment Division SE:W:S

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Appendix IV

Management's Response to the Draft Report



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
ATLANTA, GA 30308

RECEIVED

NOV 22 2004

NOV 22 2004

MEMORANDUM FOR ACTING DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

Henry O. Lamar, Jr.
Commissioner, Wage and Investment Division

SUBJECT:

Draft Audit Report -- The Health Coverage Tax Credit Was
Accurately Processed During the 2004 Filing Season
(Audit # 200440013)

I appreciate your positive recognition of our efforts to ensure returns claiming the Health Coverage Tax Credit (HCTC, or credit) were processed accurately during the 2004 filing season. As you know, we took many steps to improve our ability to process returns that included claims for the HCTC. One critical step in this process was the implementation of a Master File indicator for those taxpayers known to be potentially eligible for the credit. As your report notes, this indicator helped prevent payment for 8,000 claims to ineligible individuals.

While you found returns claiming the credit were processed accurately and post-processing actions were taken appropriately, you also identified opportunities to improve processes in both of these areas. While, in concept, we do not disagree with your recommendations and recognize that all of the recommended actions may result in more efficient processing, we can only take action on two of them at this time.

Specifically, you recommend that we insert a line on the Form 1040 for the HCTC credit and transcribe the Health Coverage Tax Credit, Form 8885. At present, we are unable to implement this recommendation. Although we see the benefit, there is not space on the current Form 1040. Further, the relatively small number of taxpayers who are potentially eligible for the HCTC do not justify the elimination or consolidation of other lines to make space for a separate HCTC line at this time. Without a new line for the HCTC on Form 1040 for tax years 2004 and 2005, there is no need to transcribe information on the Form 8885 because it would not enhance the current manual process.

We will consider including a line for the credit on future revisions of Form 1040. The IRS is currently exploring options to redesign the Form 1040 to give us more flexibility in implementing new statutory reporting requirements and reduce taxpayer burden. Potential use of the Other Adjustments to Income, Credits,

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Taxes, and Payments, Schedule O, to report Form 1040 deductions and credits used less frequently is being explored for Tax Year 2006. However, implementation of the Schedule O is not yet definite. The possibility that this schedule may provide us with a separate line to report the HCTC is contingent upon its approval. We will also consider other options for providing a separate line for HCTC on the 1040 as they arise. We will revisit the need for and benefits of transcribing the Form 8885 if the decision is made to add a line for the HCTC to the Form 1040 in tax year 2006.

You also recommend if Form 8885 is transcribed, we develop and implement appropriate systemic validity and compliance checks using the transcribed information. We agree with your recommendation to develop and implement appropriate systemic validity and compliance checks and will do so even without transcription, as transcription is not required for these checks to be in place.

In your report, you raise a concern regarding the IRS' limited ability to disallow and recover erroneous credits and the impact this may have on collectibility and taxpayer rights. You specifically note taxpayers who claim the HCTC have no formal right of appeal at any level. While an individual whose claim is disallowed cannot request reconsideration through the IRS Appeals function, they have an avenue established by the HCTC Program, the Pension Benefit Guaranty Corporation (PBGC), and the Department of Labor, if their Trade Adjustment Assistance/Alternative Trade Adjustment Assistance or PBGC ineligibility is the basis of the disallowance. In this case, the IRS directs the individual to their state workforce agency (SWA) or the PBGC to request proof of their eligibility for the periods they claimed the credit in advance or on the tax return. Because the IRS must rely on the SWAs and the PBGC for the initial eligibility determination, an appeal decision by these entities becomes, by extension, an IRS decision.

You recommend that we coordinate with the HCTC Program Office and the Office of Chief Counsel to review the issue of the legal status of HCTC disallowances and to determine if action by the Congress is necessary. We have addressed many of these issues with the Office of Chief Counsel within the context of the existing law and will maintain that dialogue and further determine the need for and/or the possibility of legislative clarification in this area.

Our specific responses to your recommendations are attached.

We appreciate your observations. Together we will continue to work towards an HCTC Program that promotes compliance without deterring eligible taxpayers from claiming the credit they deserve. In closing, please express my appreciation to your staff for their assistance in making our 2004 Filing Season a success.

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If you have any questions, please contact me at (404) 338-7060 or members of your staff may contact Keith Taylor, Director, Health Coverage Tax Credit Program, at (202) 962-0763.

Attachment

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Attachment

RECOMMENDATION 1

To more efficiently process returns claiming the credit, the Commissioner, W&I Division should: Insert a specific line on the Form 1040 for the credit and transcribe the information on Form 8885.

Corrective Action

Although we see the benefit of adding the line, there is not space on the current Form 1040. Further, the relatively small numbers of taxpayers who are potentially eligible for the HCTC do not justify the elimination or consolidation of other lines to make room for a separate HCTC line at this time.

IMPLEMENTATION DATE

N/A

RESPONSIBLE OFFICIAL

N/A

CORRECTIVE ACTION MONITORING PLAN

N/A

RECOMMENDATION 2

If Form 8885 is transcribed, develop and implement appropriate systemic validity and compliance checks using the transcribed information. For example, a math check could be programmed to verify that the taxpayer properly computed his or her credit as 65 percent of the total premium amount paid.

Corrective Action

We agree with your recommendation to implement systemic validity and compliance checks and will do so even without transcription as it is not required for these checks to be in place. We have implemented pre and post refund validity and compliance checks for tax year 2004 without transcription. Specifically, cases will be identified before the return is processed using an unallowable code when the credit is over a certain dollar amount. The case will then be forwarded to Compliance for review before allowing the credit. In the post-refund scenario, cases will automatically be routed to Compliance for classification and examination using criteria based on dollar value. These processes will continue for TY 2005.

IMPLEMENTATION DATE

January 1, 2005 for tax year 2004

RESPONSIBLE OFFICIAL

Keith Taylor, Director, HCTC Program

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CORRECTIVE ACTION MONITORING PLAN

All programming requests for pre and post validity checks have been submitted. We will monitor the status monthly to ensure the programming remains on target for completion by January 2005.

RECOMMENDATION 3

To help clarify the legal status of certain post-processing actions, the Commissioner, W&I Division, should coordinate with the HCTC Program Office and the Office of Chief Counsel to review the issue of the legal status of HCTC disallowances and to determine if action by the Congress is necessary.

Corrective Action

We have been working with Counsel to find appropriate methods for collecting erroneous payments within the context of the existing law. As a result, we are about to implement the special erroneous refund collection requirements you refer to in your report. In these cases, the IRS will request repayment from anyone who received the credit and is later determined to be ineligible for it. There is no authority for penalty assessment but interest will begin to accrue 21 days after the date of the letter requesting the repayment. In appropriate cases, taxpayer refunds may also be subject to offset. Also, as previously noted, individuals cannot appeal an HCTC disallowance through the IRS Appeals function. However, if they disagree they will be referred to their state workforce agency or the PBGC to obtain the necessary proof of eligibility that is relied upon by IRS in making these determinations.

As we develop more experience with the disallowance and recovery of HCTC claims, we will be better able to determine which processes work well and which do not. We have addressed many of these issues with the Office of Chief Counsel and will maintain that dialogue and further determine the need for and/or the possibility of legislative clarification in this area.

IMPLEMENTATION DATE

September 15, 2005

RESPONSIBLE OFFICIAL

Keith Taylor, Director, HCTC

CORRECTIVE ACTION MONITORING PLAN

As we implement the collection process, we will continue to consult with the Office of Chief Counsel to further determine the need for and/or the possibility of legislative clarification in this area.