



*Requests for Employer Identification  
Numbers Were Processed Correctly and  
Unused Numbers May Not Pose As Great a  
Risk As Anticipated*

**August 23, 2006**

**Reference Number: 2006-30-117**

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.

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TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

August 23, 2006

**MEMORANDUM FOR** COMMISSIONER, WAGE AND INVESTMENT DIVISION

**FROM:**

*Michael R. Phillips*

Michael R. Phillips

Deputy Inspector General for Audit

**SUBJECT:**

Final Audit Report – Requests for Employer Identification Numbers  
Were Processed Correctly and Unused Numbers May Not Pose As  
Great a Risk As Anticipated (Audit #200530032)

This report presents the results of our review of the Internal Revenue Service's (IRS) controls over the various methods and procedures used during the processing of requests for and the issuance of Employer Identification Numbers (EINs). As part of this review, we also determined whether the growth of unused EINs poses a current or future problem for the IRS.

*Synopsis*

EINs are nine-digit numbers assigned by the IRS to sole proprietors, corporations, partnerships, estates, trusts, and other nonindividual entities for tax filing and reporting purposes. Taxpayers can apply for EINs online or by telephone, fax, or mail using an Application for Employer Identification Number (Form SS-4). EIN applications are processed at three IRS campuses.<sup>1</sup> The information provided by taxpayers to the questions on the Form SS-4 is used to establish accounts on the IRS Business Master File.<sup>2</sup>

***While unused EINs may indicate potential compliance abuse, the growth of issued but unused EINs may not pose as great a risk as anticipated.***

In October 2003, the IRS Small Business/Self-Employed Division Research function issued the *EIN Interim Profile Report*, which provided various statistics regarding the growth in the percentage of issued versus

<sup>1</sup> The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

<sup>2</sup> The IRS database that consists of Federal tax-related transactions and accounts for businesses. These include employment taxes, income taxes on businesses, and excise taxes.



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unused EINs. This report stated that the IRS issued 9.3 million new EINs in Calendar Years 2000 through 2002. As of September 1, 2003, 4.2 million of those EINs were unused. EINs issued unnecessarily affect resources, create burden on taxpayers, and may signal compliance abuse or abusive-scheme activity.<sup>3</sup>

The IRS Customer Account Services function monitors EIN growth rates and was concerned that EIN requests and the number of unused EINs were increasing. They requested our assistance to determine whether EIN application processing procedures and controls were effective and efficient. The Customer Account Services function also wanted the audit team to help them determine if the number of issued but unused EINs posed a risk to the IRS.

During this review, we found few processing errors in our analysis of a sample of processed EIN applications. The controls over the various methods and procedures used during the processing of requests for and the issuance of EINs appeared to be effective and efficient.

This report presents a profile of the characteristics identified in our sample of processed EIN applications. We agree with the IRS that unused EINs may potentially signal noncompliance for new businesses or abusive-scheme activity. However, because the growth of unused EINs may not be as great as anticipated, the risks associated with unused EINs may not be as great. Based on the results of our review, we believe some of the perceived growth may be affected by the methodology used by Small Business/Self-Employed Division researchers, as well as timing factors. Preliminary research may have overstated the number of issued versus unused EINs. However, while we may differ with the conclusions arrived at in the Small Business/Self-Employed research reports with respect to the magnitude of the problem of issued and unused EINs, we do support recommendations put forward in their reports.

### Response

We made no recommendations in this report. However, key IRS management officials reviewed the report prior to issuance.

Copies of this report are also being sent to the IRS managers affected by the report. Please contact me at (202) 622-6510 if you have any questions or Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-8500.

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<sup>3</sup> Resources are used and taxpayers are burdened when unnecessary notices are sent to taxpayers by the IRS, or they are contacted by Compliance staff.



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## *Abbreviations*

BMF	Business Master File
CAS	Customer Account Services
EIN	Employer Identification Number
IRS	Internal Revenue Service
LLC	Limited Liability Company
SB/SE	Small Business/Self-Employed
S Corporation	Small Business Corporation
TIGTA	Treasury Inspector General for Tax Administration



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## *Background*

Employer Identification Numbers (EINs) are nine-digit numbers assigned by the Internal Revenue Service (IRS) to sole proprietors, corporations, partnerships, estates, trusts, and other nonindividual entities for tax filing and reporting purposes. Taxpayers can apply for EINs online<sup>1</sup> or by telephone, fax, or mail using an Application for Employer Identification Number (Form SS-4). EIN applications are processed at the IRS Brookhaven Campus in Holtsville, New York, the Cincinnati Campus in Cincinnati, Ohio, and the Philadelphia Campus in Philadelphia, Pennsylvania.<sup>2</sup> The information provided by taxpayers or their representatives to the questions on the Form SS-4 is used to establish accounts on the IRS Business Master File (BMF).<sup>3</sup>

In October 2003, the IRS Small Business/Self-Employed (SB/SE) Division Research function issued the *EIN Interim Profile Report*, which provided various statistics regarding the growth in the percentage of issued versus unused EINs.<sup>4</sup> This report stated that the IRS issued 9.3 million new EINs in Calendar Years 2000 through 2002 and as of September 1, 2003, 4.2 million of those EINs were unused.<sup>5</sup>

As the administering authority for the EIN process, the Customer Account Services (CAS) function monitors EIN growth rates. EINs issued unnecessarily affect resources, create burden on taxpayers, and may signal compliance abuse or abusive-scheme activity.<sup>6</sup> Since EIN requests and the number of unused EINs were increasing and the trend potentially suggested that more taxpayers were requesting EINs strictly for banking purposes and not to satisfy IRS filing requirements, CAS function management requested the assistance of the Treasury Inspector General for Tax Administration (TIGTA) Office of Audit to determine whether EIN application

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<sup>1</sup> An EIN issued online is referred to as an I-EIN.

<sup>2</sup> The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

<sup>3</sup> The IRS database that consists of Federal tax-related transactions and accounts for businesses. These include employment taxes, income taxes on businesses, and excise taxes.

<sup>4</sup> Researchers defined the "Use of an EIN" as a taxpayer who files a Federal income tax return, which is supported and identified on the IRS Master File by the posting of a Federal income tax return. Although an EIN appears unused by the IRS definition, this does not mean the EIN is not used outside the Federal Government domain (e.g., State licensing requirements). Inherent in the current EIN application process is the likelihood of a certain percentage of unused EINs.

<sup>5</sup> In June and August of 2004, the SB/SE Division Research function issued *Who's Requesting EINs? An Analysis of the Growth Rate of Unused Employer Identification Numbers-Project 05.02.002.03*, which provided additional research results.

<sup>6</sup> Resources are used and taxpayers are burdened when unnecessary notices are sent to taxpayers by the IRS, or they are contacted by Compliance staff.



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processing procedures and controls were effective and efficient. The CAS function also wanted the audit team to help them determine whether the number of issued but unused EINs posed a risk to the IRS.

In September 2005, TIGTA auditors completed Phase I of their review of the processing of EIN applications and issued their report.<sup>7</sup> During Phase II of this review, the TIGTA audit team analyzed processed EIN applications selected during Phase I to determine whether the EINs assigned were subsequently used by the applicants and to determine whether the number of issued but unused EINs posed a risk to the IRS.

This review was performed at the IRS Brookhaven Campus in Holtsville, New York, in the EIN Processing Unit during the period September 2005 through May 2006. We also held meetings and obtained information from CAS function staff<sup>8</sup> located at various sites. The audit was conducted in accordance with *Government Auditing Standards*. Detailed information on our audit objectives, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

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<sup>7</sup> *More Effective Procedures Are Needed to Process Taxpayers' Claims That They Did Not Request Employer Identification Numbers Assigned to Them* (Reference Number 2005-30-131, dated September 2005).

<sup>8</sup> SB/SE Division CAS function operations were consolidated under the Wage and Investment Division in 2005.



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## *Results of Review*

### ***Controls Over the Processing of Requests for and the Issuance of Employer Identification Numbers Are Effective and Efficient***

We found few processing errors in our analysis of 311 Forms SS-4 selected in a judgmental<sup>9</sup> sample at the IRS Brookhaven Campus EIN Processing Unit. Tax technicians performed adequate research to determine if applicants were already assigned EINs. They referred difficult or problem applications to supervisors for review. When additional information was necessary to process applications accurately, taxpayers were contacted either by telephone or mail. In most cases, taxpayers' information was input to the Integrated Data Retrieval System<sup>10</sup> correctly and accounts were established on the BMF accurately. The instructions and guidance provided in the Internal Revenue Manual<sup>11</sup> and controls such as managerial and quality case reviews appeared to adequately ensure that applications were processed correctly in most instances. The relatively few processing errors had no material effect on taxpayers or the IRS.

### ***The Growth of Issued but Unused Employer Identification Numbers May Not Pose As Great a Risk As Anticipated***

The October 2003 report issued by the SB/SE Division Research function stated the IRS issued 9.3 million new EINs in Calendar Years 2000 through 2002 and as of September 1, 2003, 4.2 million of those EINs were unused.

Based on the results of our review, we believe this reported growth in the number of issued versus unused EINs may have been overstated in the SB/SE Division's preliminary research.

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<sup>9</sup> A judgmental sample was selected because the Forms SS-4 are available for a limited time only. The IRS processed approximately 3.5 million Forms SS-4 during 2004, but the Forms were generally available only when they were being processed.

<sup>10</sup> The IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.

<sup>11</sup> Internal Revenue Manual 21.7.13.





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**Some basic differences between our study and that of SB/SE Division researchers**

- **Our research began with the taxpayers' original EIN applications.**

Our study began with a judgmental sample of 311 processed Forms SS-4, which were sent to the IRS Holtsville, New York, Campus EIN Processing Unit by fax, mail, or internet in August and September 2004. We made copies of Forms SS-4 after they were processed, but before they were destroyed. This preserved the information taxpayers provided on these forms rather than having to rely on the information posted to taxpayers' accounts, as did the SB/SE Division researchers.

- **We performed a more indepth study of each EIN application.**

Because we began our research at an earlier step in the EIN application process and were reviewing a much smaller number of accounts than SB/SE Division researchers, we were able to expand the depth of our research, which included sending for and examining all the U.S. Individual Income Tax Returns (Form 1040) for Tax Years 2004 and 2005 associated with the EIN applicants. Thus, in many instances, we were able to determine whether applicants who applied for EINs for flowthrough entities (e.g., partnerships or small business corporations (S Corporations)) actually used the EINs or reported the entities listed on their Forms SS-4 on their Forms 1040.

- **We expanded the definition of "Use of an EIN."**

For the purposes of the SB/SE Division research, an "unused" EIN was defined as a taxpayer who had received an EIN during Calendar Years 2000 through 2002 and there was no subsequent posting of a Federal income tax return to that account within the time period defined. Our audit team expanded the definition of "used" to include *any instance* that the EIN was reported to the IRS, and in whatever fashion.<sup>12</sup> We also included taxpayers' use of the EINs in instances which may or may not be considered taxpayers' errors. For example, if an EIN was assigned to an entity initially described by the taxpayer on the Form SS-4 as a partnership and established on the BMF with a U.S. Partnership Return of Income (Form 1065) primary filing requirement, but was subsequently used by the taxpayer on an attachment to Form 1040, Profit or Loss from Business (Schedule C),<sup>13</sup> we considered the EIN as issued and used.

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<sup>12</sup> We included instances in which IRS records indicated that taxpayers met secondary filing requirements (e.g., there was no indication the taxpayers had met their primary filing requirements to file their U.S. Corporation Income Tax Returns (Form 1120), but the taxpayers had filed their Employer's Quarterly Federal Tax Returns (Form 941)).

<sup>13</sup> In some instances, taxpayers listed only the entity names on their Schedules C and the spaces for the EINs on the Schedules C were left blank. We examined the Schedules C and copies of the original Forms SS-4 and determined the entities for which the taxpayers obtained the EINs were in fact being reported on the taxpayers' returns.



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**Filing requirements are not always established based on taxpayers' intentions**

According to Form SS-4, there are a variety of reasons why an application for an EIN is needed, including: starting a new business, hiring employees, banking purposes, creating a trust or pension plan, changing the type of organization or purchasing an ongoing business, and compliance with IRS withholding regulations. Many EINs are obtained for legitimate reasons that do not include the filing of a tax return, such as needing an EIN for banking purposes, for meeting State law requirements as it relates to sales tax issues, or for obtaining State licenses.

Using the information provided by an applicant on Form SS-4, the type of entity and the filing requirements (the types of returns that must be filed with the IRS) are established on the IRS BMF by the campus that processes the EIN request. Subsequent to the IRS determination, the taxpayer is notified of any filing requirements and the appropriate forms to be filed.

The determination of taxpayers' filing requirements and the establishment of these requirements on the BMF may or may not have been made based on dialogue with the EIN applicants. Ultimately, if the EINs are used, the taxpayers decide what forms will be filed. For example, the EIN account may have been established on the BMF as a new business that should file a corporate tax return when, in fact, the taxpayer's intention is to be a Schedule C filer.

The SB/SE Division research reports stated this fact limited their research as they had no way of knowing if the filing requirements initially established on the BMF actually reflected taxpayers' intentions. In other words, their research only detected, for example, that the EINs were not used to file U.S. Corporation Income Tax Return (Form 1120), but could not identify that the EINs were used on taxpayers' Forms 1040, Schedules C instead. Our study did not have this limitation as we had the original EIN applications and the Forms 1040 ultimately filed by the taxpayers.

**Profile of cases in our sample can add to the IRS' knowledge of "unused" EINs**

Figure 1 presents a profile of the cases in our sample by entity type with respect to the issuance of EINs and their subsequent use by taxpayers to file Federal income tax returns.



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**Figure 1: Distribution of Unused EINs by Type of Entity**

<u>Entity Type</u>	<u>EINs Issued</u>	<u>EINs Used</u>	<u>EINs Unused</u>	<u>Percentage of EINs Issued but Unused</u>
<b>Estates</b>	49(16%)	23	26	53%
<b>Trusts</b>	32(10%)	17	15	47%
<b>Sole Proprietors</b>	43(14%)	27	16	37%
<b>S Corporations</b>	47(15%)	41	6	13%
<b>Corporations</b>	39(13%)	27	12	31%
<b>Partnerships</b>	54(17%)	41	13	24%
<b>No Filing Requirements</b>	13(4%)	2	11	85%
<b>Other Entity Type</b>	9(3%)	7	2	22%
<b>Sole Member Limited Liability Companies/Disregarded Entities<sup>14</sup></b>	25(8%)	12	13	52%
<b>Totals</b>	<b>311</b>	<b>197</b>	<b>114</b>	<b>37%</b>

*Source: Review of a judgmental sample of 311 processed EIN applications selected at the IRS Brookhaven Campus EIN Processing Unit.*

**Significant issues illustrated by Figure 1**

- Approximately 37 percent (114 of 311) of the EINs assigned to the applicants in our sample were not used to file returns. Because 4 percent (13 of 311) of the EINs were assigned to entities with no filing requirements, we estimate 33 percent (37 percent minus 4 percent) of the EINs that should have been used were not. Some EINs assigned may be used after the scope of fieldwork in this audit.
- EINs assigned to estates (49 of 311) and trusts (32 of 311) made up 26 percent (81 of 311) of our sample but represented the largest segment (36 percent), or 41 of the 114 issued but unused EINs.
- Sole proprietors made up 14 percent (43 of 311) of our sample; 37 percent (16 of 43) of them did not use the entity names or the EINs assigned to the entities on Schedules C attached to either their Tax Years 2004 or 2005 Forms 1040. We were unable to obtain

<sup>14</sup> A Sole Member Limited Liability Company may be required to include all of its income and expenses on the owner's tax return (IRM 21.7.13.5.4.3.1). A Disregarded Entity is an eligible entity that is treated as an entity that is not separate from its single owner. Its separate existence will be ignored for Federal tax purposes unless it elects corporate tax treatment.



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all the Forms 1040 requested, so we estimate the number of unused EINs issued to sole proprietors is most likely lower than 37 percent.

- Approximately 87 percent (41 of 47) of S Corporations filed their U.S. Income Tax Returns for an S Corporation (Form 1120S).
- Corporations (non-S Corporations) made up 13 percent (39 of 311) of the entities in our sample. Approximately 56 percent (22 of 39) of these corporations did not file Forms 1120. However, 10 corporations that did not file Forms 1120 used their EINs to meet secondary filing requirements on either Employer's Annual Federal Unemployment (FUTA) Tax Returns (Form 940), Employer's Quarterly Federal Tax Returns (Form 941), or schedules attached to their Forms 1040. Therefore, only 31 percent (12 of 39) of the EINs issued to corporations were not used.
- Partnerships made up the single largest entity type in our sample (17 percent, or 54 of 311). Approximately 43 percent (23 of 54) of partnerships did not file Forms 1065 as required. However, 10 of the partnerships that did not file Forms 1065 used the EINs either to meet secondary filing requirements or on schedules attached to their Forms 1040. Therefore, only 24 percent (13 of 54) of the EINs issued to partnerships were not used.
- Approximately 76 percent (41 of 54) of the partnerships that applied for EINs were described as Limited Liability Companies (LLC)<sup>15</sup> on the Forms SS-4 and were established on the BMF with Form 1065 as their primary filing requirement. More than one-half of these LLCs were created for real estate rental/investment/development and management activities.
- Only 3 of the 311 cases in our sample involved household employees and required the filing of Household Employment Taxes (Schedule H).

**Profile of cases in our sample can add to the IRS' knowledge of the behavior patterns of flowthrough entities and sole proprietors**

Certain types of entities (e.g., partnerships) are considered flowthrough entities.<sup>16</sup> Income or losses reported on the Forms 1065 flow through to the partners and are required to be reported on Supplemental Income and Loss Schedules (Schedule E) attached to the partners' Forms 1040. Entities defined as sole proprietors are required to report their income and losses on Schedules C attached to their Forms 1040.

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<sup>15</sup> A limited liability company is an unincorporated business entity, established under state law, in which all owners have limited liability. Thus the LLC is a blend of the corporation and partnership formats.

<sup>16</sup> Flowthrough entities consisted of S Corporations, Partnerships, Sole Member LLCs (also referred to as Single Member LLCs), and Disregarded Entities.



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There were 169 (54 percent) flowthrough and sole proprietor entities in our judgmental sample of 311 cases. We requested the Tax Year 2004 and 2005 Forms 1040 for these taxpayers and determined if the EINs or the entities to which the EINs were assigned appeared on the taxpayers' Forms 1040 in either tax year.

**Significant issues pertaining to flowthrough and sole proprietor entities**

- EINs assigned to flowthrough entities made up 75 percent of the accounts (126 of 169) that required a match to taxpayers' Forms 1040 to determine if taxpayers reported income or losses from these entities as required. Sole proprietors made up the other 25 percent (43 of 169) of the accounts requiring a match.
- Approximately 78 percent of S Corporations that used their EINs to file Forms 1120S reported the EINs or entities on their Forms 1040.<sup>17</sup>
- Partnerships made up the largest entity type (32 percent) of all the flowthrough entities. Approximately 54 percent of the partnerships that used their EINs to meet primary or secondary filing requirements reported the EINs or entities on their Forms 1040.<sup>18</sup>
- Entities described as Sole Member LLCs and Disregarded Entities made up only 15 percent of the flowthrough entities. Approximately 67 percent of the EINs that were used to meet primary or secondary filing requirements were reported by taxpayers on their Forms 1040.<sup>19</sup>
- Sole proprietors reported the EINs or the entity names on their Forms 1040, Schedule C, in 18 (67 percent) of the 27 cases in which we had previously determined the EINs were used.<sup>20</sup> Many taxpayers that did list the entities on their Schedules C did not enter the respective EINs in the appropriate box on the Schedule C Forms.

**Conclusion**

We agree with the IRS that unused EINs may signal noncompliance for new businesses or abusive-scheme activity. However, because the growth of unused EINs may not be as great as anticipated, the risks associated with unused EINs may not be as great. Based on the results of our limited sample of 311 cases, we believe some of the perceived growth may be affected by the methodology used by SB/SE Division researchers, as well as timing factors. As a result, it may

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<sup>17</sup> We anticipate this figure is actually higher, but we were not able to obtain all the Forms 1040 that we requested.

<sup>18</sup> We anticipate this figure is actually higher, but we were not able to obtain all the Forms 1040 that we requested.

<sup>19</sup> We anticipate this figure is actually higher, but we were not able to obtain all the Forms 1040 that we requested.

<sup>20</sup> The difference would consist of cases where taxpayers met secondary filing requirements but not primary filing requirements. We anticipate this figure is actually higher, but we were not able to obtain all the Forms 1040 that we requested.



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be likely that the growth in the number of issued versus unused EINs was overstated in the SB/SE Division's preliminary research.<sup>21</sup>

**We support many of the recommendations endorsed by the SB/SE Division researchers**

Our report presents a profile of the characteristics we identified in our sample of 311 processed EIN applications. While we may differ with the conclusions arrived at in the SB/SE Division research reports with respect to the magnitude of the problem of issued but unused EINs, we do support recommendations put forward in their reports.

- Some BMF accounts (e.g., nonprofit entities like scholarship funds and clubs) are not established with filing requirements. We agree with the conclusion of the SB/SE Division Research function staff that these types of EINs are being used for other than tax purposes and that there will always be a degree of unused EINs. We further agree with their recommendation that perhaps the IRS should consider developing a short Form SS-4, which would allow the IRS to separately account for these entities, while potentially reducing the taxpayer burden associated with current form preparation.
- The IRS has identified the LLC as a possible emerging compliance segment, especially those LLCs designated as "disregarded entities." Because of the number of EIN applicants for entities described as LLCs in our limited sample, especially the number associated with real estate rental/investment/development and management activities, we agree with the conclusion of the SB/SE Division Research function staff that the CAS function could use such information to identify taxpayer trends with respect to this emerging choice of entity and the ensuing filing and compliance issues.
- The SB/SE Division research Reports stated the largest growth rate for newly issued unused EINs appeared within flowthrough entities. We agree with the conclusion of the SB/SE Research function staff that this may have implications for Compliance function operational

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<sup>21</sup> Some of the taxpayers who applied for EINs in the August through September 2004 time period did not use the EINs until they filed their 2005 tax returns in 2006.



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priorities that deal with K-1 matching<sup>22</sup> and questionable structured transactions for “high income taxpayers.”

- Approximately 26 percent (81 of 311) of the applications for EINs in our sample were for estates and trusts, but as of June 2006, 51 percent (41 of 81) of these entities had not filed returns (Forms 1041). We concur with the SB/SE Division Research function staff that these unused EINs for estates and trusts may be a source for the identification of “abusive schemes.”

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<sup>22</sup> An IRS program that matches the information reported on Beneficiary’s Share of Income, Deductions, Credits, etc. (Form 1041, Schedule K-1); Partner’s Share of Income, Deductions, Credits, etc. (Form 1065, Schedule K-1); and Shareholder’s Share of Income, Deductions, Credits, etc. (Form 1120S, Schedule K-1) to taxpayers’ individual income tax returns.



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## **Appendix I**

### *Detailed Objectives, Scope, and Methodology*

The main objective of this audit was to evaluate the IRS controls over the various methods and procedures used during the processing of requests for and the issuance of EINs. As part of this review, we also determined whether the growth of unused EINs poses a current or future problem for the IRS. To accomplish these objectives, we:

- I. Determined whether there are additional steps the IRS could take to ensure the efficiency and effectiveness of the processing of requests for EINs.
  - A. Evaluated the current procedures and controls over the IRS EIN application and issuance process.
    1. Reviewed all pertinent Internal Revenue Manual sections and desk procedures related to the processing of taxpayers' EIN applications.
    2. Identified the key controls and procedures in place for each of the EIN application methods (i.e., online, telephone, fax and mail).
  - B. Gathered and reviewed any information on changes to the EIN application process since the completion of Phase I of the review.
    1. Held interviews with IRS management staff to obtain information and documentation regarding any concerns with the current EIN application and issuance process, as well as inventory processing records for the past year.
    2. Obtained information, reports, or documents regarding any future plans for the processing of EIN applications.
- II. Determined whether the EIN issuance procedures and controls were being followed during the processing of EIN applications and the establishment of new entities on the BMF.<sup>1</sup>
  - A. Analyzed a judgmental sample<sup>2</sup> of 311 EIN applications selected from the IRS EIN application processing functions during Phase I of this review to determine whether

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<sup>1</sup> The IRS database that consists of Federal tax-related transactions and accounts for businesses. These include employment taxes, income taxes on businesses, and excise taxes.

<sup>2</sup> A judgmental sample was selected because the Forms SS-4 are available for a limited time only. The IRS processed approximately 3.5 million Forms SS-4 during 2004, but the Forms were generally available only when they were being processed.





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- applications were processed correctly and account information and filing requirements were properly established on the BMF.
- B. Evaluated whether the current EIN issuance controls and procedures are adequate to ensure the future compliance of new business entities created on the BMF and prevent the issuance of unnecessary EINs.
  - C. Evaluated whether the IRS could take additional steps to increase the effectiveness and efficiency of the EIN application and issuance process, reduce the burden on its BMF customers, and increase the potential for cost savings, increased revenue, and tax compliance.
- III. Using the results of our analysis of the sample of EIN applications, as well as discussions with IRS staff, determined whether issued but unused EINs pose any problems for the IRS.
- A. Analyzed the sample in Step II.A. to identify the accounts established with filing requirements upon the creation of the BMF accounts and issuance of EINs.
    - 1. Performed Integrated Data Retrieval System<sup>3</sup> research to determine whether taxpayers assigned EINs with filing requirements actually filed returns using the assigned EINs.
    - 2. Performed Integrated Data Retrieval System research to determine whether taxpayers assigned EINs with filing requirements that were not used filed returns using other EINs or Social Security Numbers.
  - B. Performed research to determine whether IRS data reflected potential unreported income for the unused EINs identified in our analysis.
  - C. Performed research to identify independent listings (i.e., telephone directories) for the entities established with filing requirements, but no evidence of filing returns.

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<sup>3</sup> The IRS computer system capable of retrieving or updating stored information; it works in conjunction with a taxpayer's account records.



*Requests for Employer Identification Numbers Were Processed Correctly and Unused Numbers May Not Pose As Great a Risk As Anticipated*

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## **Appendix II**

### *Major Contributors to This Report*

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*Requests for Employer Identification Numbers Were Processed Correctly and Unused Numbers May Not Pose As Great a Risk As Anticipated*

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## **Appendix III**

### *Report Distribution List*

Commissioner C  
Office of the Commissioner – Attn: Chief of Staff C  
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Director, Strategy and Finance, Wage and Investment Division SE:W:S  
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