

TDP 15-71

**Management Advisory Report:
Significantly More Individual Taxpayers
Inappropriately Received Disabled Access
Credits for Tax Year 2000 Than for 1999**

January 2002

Reference Number: 2002-30-048

TDP 15-71



INSPECTOR GENERAL
for TAX
ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

January 29, 2002

MEMORANDUM FOR COMMISSIONER ROSSOTTI

Pamela J. Gardiner

FROM: Pamela J. Gardiner
Deputy Inspector General for Audit

SUBJECT: Final Management Advisory Report – Significantly More
Individual Taxpayers Inappropriately Received Disabled Access
Credits for Tax Year 2000 Than for 1999 (Audit # 200230008)

This report presents the results of a computer analysis the Internal Revenue Service (IRS) requested of Tax Year (TY) 2000 U.S. Individual Income Tax Returns (Form 1040) that inappropriately included Disabled Access Credits.¹ Our overall objective was to identify taxpayers who claimed and received the Disabled Access Credit on their TY 2000 Forms 1040 despite indications they had no business ownership or participation.² We also determined whether the IRS was providing taxpayer education, which it had agreed to do, related to this tax credit.

In September 2001, we reported³ that taxpayers were inappropriately receiving the Disabled Access Credit on their TY 1999 Forms 1040. Although the number of taxpayers involved was not great, the issue was significant for two reasons:

¹ A business incentive tax credit enacted to help eligible small businesses comply with the applicable requirements of the Americans with Disabilities Act (ADA) 42 U.S.C. §§ 12101-12212 (1994 & Supp. IV 1998). The ADA is a national mandate for the elimination of discrimination against individuals with disabilities. Section 302(a) of the Act provides that no individual may be discriminated against on the basis of disability in the full and equal enjoyment of the goods, services, and facilities of any place of public accommodation.

² For purposes of our analysis, taxpayers were deemed to have no business ownership or participation if they did not file one of the following schedules with their tax return: Profit or Loss From Business (Schedule C), Profit or Loss From Farming (Schedule F), or Supplemental Income and Loss (Schedule E).

³ *Some Individual Taxpayers Are Inappropriately Receiving Tax Credits Intended for Businesses That Provide Access for Disabled Americans* (Reference Number 2001-30-158, dated September 2001).

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- Many of the taxpayers involved were elderly Americans who were possibly victims of promoters recommending unwise investments in pay telephones and automated teller machines and promising bogus tax credits.
- Based on the media coverage the issue had received,⁴ we believed the problem was most likely increasing.

One of the recommendations in our prior report was for the IRS to analyze the results of our computer analyses for TY 1999, perform similar analyses of TY 2000 returns, and develop a compliance approach to address this issue. To facilitate the IRS' corrective action, we agreed to perform a computer analysis of TY 2000 tax returns.

For TY 2000, the number of tax returns for which the Disabled Access Credit was inappropriately allowed increased 28 percent, as compared to TY 1999. The amount of credit allowed on these returns totaled over \$1.25 million. We also determined that 64 taxpayers inappropriately received the credit for both TYs 1999 and 2000.

As of the date of our review, the IRS was on schedule to add information to its Small Business/Self-Employed Community Website to alert taxpayers about investments in pay telephones and automated teller machines fraudulently promoted as qualifying for the Disabled Access Credit. We discussed another enhancement to the IRS' website with the Project Manager for the IRS' website and the Director, Stakeholder Partnership, Education and Communications. They agreed to work together to provide links from other sections of the IRS' website to the text in the Small Business/Self-Employed section.

The Treasury Inspector General for Tax Administration (TIGTA) has designated this report as Limited Official Use (LOU) pursuant to Treasury Directive TD P-71-10, Chapter III, Section 2, "Limited Official Use Information and Other Legends" of the Department of Treasury Security Manual. Because this document has been designated LOU, it may only be made available to those officials who have a need to know the information contained within this report in the performance of their official duties. This report must be safeguarded and protected from unauthorized disclosure; therefore, all requests for disclosure of this report must be referred to the Disclosure Unit within the TIGTA's Office of Chief Counsel.

We are making no formal recommendations in this report; therefore, no response is required. Please contact me at (202) 622-6510 if you have questions or your staff may call Gordon C. Milbourn III, Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-3837.

⁴ Noelle Knox and Greg Farrell, "Seniors Lose Big in Risky Deals Through Insurance Agents," *USA Today* (February 28, 2001).

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Background

In September 2001, the Treasury Inspector General for Tax Administration (TIGTA) issued a report¹ to the Internal Revenue Service (IRS) discussing taxpayers that inappropriately received the Disabled Access Credit² on their Tax Year (TY) 1999 U.S. Individual Income Tax Returns (Form 1040). Although the number of taxpayers involved was not great, the issue was significant for two reasons:

- Many of the taxpayers involved were elderly Americans who were possibly victims of promoters recommending unwise investments and promising bogus tax credits.
- Based on the media coverage the issue had received,³ we believed the problem was most likely increasing.

One of our recommendations in that report was for the IRS to analyze the results of our computer analyses for TY 1999, perform similar analyses of TY 2000 returns, and develop a compliance approach to address this issue.

To facilitate the IRS' corrective actions, we agreed to perform a computer analysis of the IRS' Individual Returns Transaction File⁴ to identify taxpayers inappropriately receiving the Disabled Access Credit for their TY 2000 Forms 1040.

This report presents the results of our analysis and our assessment of IRS management's progress in completing

¹ *Some Individual Taxpayers Are Inappropriately Receiving Tax Credits Intended for Businesses That Provide Access for Disabled Americans* (Reference Number 2001-30-158, dated September 2001).

² A business incentive tax credit enacted to help eligible small businesses comply with the applicable requirements of the Americans with Disabilities Act (ADA), 42 U.S.C. §§ 12101-12213 (1994 & Supp. IV 1998). The ADA is a national mandate for the elimination of discrimination against individuals with disabilities. Section 302(a) of the Act provides that no individual may be discriminated against on the basis of disability in the full and equal enjoyment of the goods, services, and facilities of any place of public accommodation.

³ Noelle Knox and Greg Farrell, "Seniors Lose Big in Risky Deals Through Insurance Agents," *USA Today* (February 28, 2001).

⁴ The IRS' Individual Returns Transaction File contains information from tax returns filed for the current and two previous years.

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corrective actions planned in response to our prior report. Our work was conducted at the Ogden IRS Center from October through December 2001 in accordance with the President's Council on Integrity and Efficiency's *Quality Standards for Inspections*. Detailed information on our objectives, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

**The Number of Taxpayers
Inappropriately Receiving the
Disabled Access Credit
Significantly Increased for Tax
Year 2000**

In order to qualify for the Disabled Access Credit, taxpayers must incur expenses to bring their businesses into compliance with the ADA. As previously reported, we identified 391 TY 1999 Forms 1040 on which taxpayers were allowed Disabled Access Credits despite their tax returns indicating they had no business ownership or participation.⁵ For TY 2000, the number of tax returns for which the Disabled Access Credit was inappropriately allowed increased 28 percent, to 499 returns. The amount of credit allowed on these returns totaled over \$1.25 million. The IRS issued refunds or allowed taxpayers to apply overpayments to subsequent years' taxes in 374 of these cases. The refunds and overpayments applied totaled over \$1.09 million. On the remaining 125 cases, the Disabled Access Credit was used to offset other taxes on the return, but did not result in an overpayment of taxes for refund or application to subsequent years' taxes.

We also determined that 64 taxpayers inappropriately received the credit for both TYs 1999 and 2000. For the combined years, these 64 taxpayers received credits totaling over \$370,000 (an average of \$5,800 per taxpayer).

As agreed with the IRS, we will provide the data from our computer analysis to appropriate officials in the IRS' Criminal Investigation function and the Office of Strategy.

⁵ For purposes of our analysis, taxpayers were deemed to have no business ownership or participation if they did not file one of the following schedules with their tax return: Profit or Loss From Business (Schedule C), Profit or Loss From Farming (Schedule F), or Supplemental Income and Loss (Schedule E).

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**Taxpayer Education Will be
Provided Regarding
Inappropriately Claiming the
Disabled Access Credit**

Research and Performance Management, Small Business/
Self-Employed Division.

As of the date of our review, the IRS was on schedule to add information to its Small Business/Self-Employed Community Website to alert taxpayers about investments in pay telephones and automated teller machines fraudulently promoted as qualifying for the Disabled Access Credit.

However, because the taxpayers involved, by definition, have no business ownership or participation, in our view they are not likely to be researching this particular IRS website. Therefore, we believe these taxpayers would benefit more from education aimed at individual taxpayers rather than taxpayers who own small businesses or are self-employed. We discussed this issue with the Project Manager for the IRS' website and the Director, Stakeholder Partnership, Education and Communications. They agreed to work together to provide a link from the Wage and Investment and the Tax Professional sections of the IRS' website to the text in the Small Business/Self-Employed section.

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Appendix I

Detailed Objectives, Scope, and Methodology

Our overall objective was to identify taxpayers who claimed and received the Disabled Access Credit on their Tax Year (TY) 2000 U.S. Individual Income Tax Return (Form 1040) despite indications they had no business ownership or participation. We also determined whether the Internal Revenue Service (IRS) was providing taxpayer education, which it agreed to do in response to our prior report,¹ related to this tax credit.

To accomplish our objectives, we performed the following audit tests:

- I. To identify taxpayers who inappropriately claimed and received the Disabled Access Credit on their TY 2000 Forms 1040, and to determine the impact, we:
 - A. Performed a computer analysis of data on the IRS' Individual Returns Transaction File² to identify TY 2000 returns that claimed the Disabled Access Credit but did not include one of the following schedules:
 - Profit or Loss From Business (Schedule C).
 - Profit or Loss From Farming (Schedule F).
 - Supplemental Income and Loss (Schedule E).

The data was accumulated in two separate files. One file included all IRS processing cycles except for cycle 22 (the week starting May 27, 2001). The other file included only cycle 22 data.

- B. Performed validity tests of the data accumulated to ensure that the computer runs accurately identified appropriate returns. We performed a query on the data to identify any duplicate records. Also, we verified the data by selecting a judgmental sample of 13 records using an Excel spreadsheet feature called "data analysis" and matching the records identified to the original IRS files. We ensured that the computer program worked as intended and that the data was accurate.

¹ *Some Individual Taxpayers Are Inappropriately Receiving Tax Credits Intended for Businesses That Provide Access for Disabled Americans* (Reference Number 2001-30-158, dated September 2001).

² The IRS' Individual Returns Transaction File contains information from tax returns filed for the current and two previous years.

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- C. Analyzed the IRS records to identify the number of taxpayers that received the credit but did not have bona fide business reasons for taking the credit. We determined the total amounts of credits received. We also determined the number of taxpayers that received refunds or elected to apply overpayments to subsequent years' taxes and the total amount of the refunds/overpayments applied. In addition, we compared the Social Security Numbers of taxpayers who received the credit for TY 2000 with those receiving the credit for TY 1999 to determine if any taxpayers claimed the credit for both years.

The original data files created by the computer runs included 557 taxpayer records. Each record identified a taxpayer that claimed the Disabled Access Credit but did not include a Schedule C, E, or F with his or her return. We reduced the total number of records by excluding taxpayers that, even though they had claimed the credit, did not actually receive it. We also eliminated records if taxpayers did not receive at least \$50 of Disabled Access Credit. As a result, 499 records were included in the analysis.

- II. To compare the recommendations made in the prior audit report with the actions taken or planned by IRS management, we:
- A. Reviewed the prior final audit report and, for each recommendation, identified management's response.
 - B. Interviewed IRS Small Business/Self-Employed (SB/SE) Division management and, for each recommendation made in the report, determined the actions already taken or planned. This included determining their efforts to educate and/or warn taxpayers about the illegality of taking the credit and about promoters that encourage taxpayers to make fraudulent investments.
 - C. Contacted the Project Manager for the IRS' website and the Director, Stakeholder Partnership, Education and Communications, SB/SE Division, to discuss the need to make education materials available on website sections most likely to be accessed by individual taxpayers.

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Appendix II

Major Contributors to This Report

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Appendix III

Report Distribution List

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Commissioner, Small Business/Self-Employed Division S
Commissioner, Wage and Investment Division W
Director, Compliance, Small Business/Self-Employed Division S:C
Director, Compliance, Wage and Investment Division W:CP
Director, Refund Crimes CIRC
Director, Strategy and Finance, Wage and Investment Division W:S
Director, Strategy, Research and Performance Management, Small Business/Self-Employed
Division S:SR
Director, Stakeholder Partnership, Education and Communications W:CAR:SPEC
Deputy Chief Financial Officer, Department of the Treasury