HEARING BEFORE THE
COMMITTEE ON WAYS AND MEANS
SUBCOMMITTEE ON OVERSIGHT
U.S. HOUSE OF REPRESENTATIVES

"Administration of the First-Time Homebuyer Credit"

October 22, 2009

Washington, DC

Statement of
The Honorable J. Russell George
Treasury Inspector General for Tax Administration

STATEMENT OF
THE HONORABLE J. RUSSELL GEORGE
TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION
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Chairman Lewis, Ranking Member Boustany, and Members of the Subcommittee, I thank you for the opportunity to testify on the Internal Revenue Service's (IRS) administration of the First-Time Homebuyer Credit (Credit). My comments will focus on the Treasury Inspector General for Tax Administration's (TIGTA) oversight of the IRS's efforts to administer the Credit and on recommendations TIGTA has made to improve the administration of the Credit.

Background on the First-Time Homebuyer Credit

The American economy is in the midst of recovering from a severe economic crisis in which millions of Americans have lost their jobs. In light of this economic predicament, the President signed into law on February 17, 2009, the American Recovery and Reinvestment Act of 2009 (Recovery Act), a nationwide effort to create jobs and revitalize the American economy.[1] This legislation represents one of the most ambitious efforts to stimulate the American economy in our Nation's history. Section 1006 of the Recovery Act revised and extended the First-Time Homebuyer Credit originally provided for in the Housing and Economic Recovery Act of 2008 (HERA).[2]

HERA established a new tax credit for first-time homebuyers. The tax credit was intended to address concerns over excess home inventory and falling home prices.[3] The new credit was originally available for a limited time only, applying to taxpayers who purchased a principal residence after April 8, 2008, and before July 1, 2009.[4] HERA allowed eligible taxpayers to claim a Credit equal to ten percent of the purchase price of

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[1] Pub. L. No. 111-5, 123 Stat. 115.
[2] Pub. L. No. 110-289.
[3] Congressional Research Service: *The First-Time Homebuyer Credit: An Economic Analysis* (2009).
[4] Only the purchase of a primary residence located in the United States qualifies for the Credit. Vacation homes and rental properties are not eligible. Taxpayers who owned a primary residence at any time during the three years prior to the date of purchase are not eligible for the Credit. For homes that taxpayers construct, the purchase date is the date they first occupy the home.

the home, limited to $7,500.[5] The Credit was fully refundable, meaning it would be paid out to eligible taxpayers even if they owed no tax or if the Credit exceeded the tax they owed. However, the Credit, as expressed in HERA, served as an interest-free loan to be paid back over a 15-year period beginning two years after the Credit was claimed.

Section 1006 of the Recovery Act extended the First-Time Homebuyer Credit to include purchases made on or after January 1, 2009, and before December 1, 2009; increased the maximum Credit to $8,000; and eliminated the repayment requirement as long as the taxpayer retains the residence for 36 months.[6] Taxpayers qualifying for the revised Credit may claim the $8,000 Credit on either their 2008 or 2009 individual income tax returns.

Benefits and Estimated Costs of the First-Time Homebuyer Credit

Congress allocated $13.6 billion for the First-Time Homebuyer Credit in HERA. The Joint Committee on Taxation estimated that $4.3 billion more would be paid to first-time homebuyers in Fiscal Years 2009 and 2010 as a result of the Recovery Act. As of October 9, 2009, more than 1.2 million tax returns claiming almost $8.5 billion in First-Time Homebuyer Credits had been processed by the IRS.[7]

The President has called on Federal agencies to ensure that Recovery Act funds are used for authorized purposes and every step is taken to prevent instances of fraud, waste, error, and abuse. The IRS has been charged with ensuring that the First-Time Homebuyer Credit is appropriately claimed and properly administered, and the Recovery Act mandates TIGTA to oversee the IRS's Recovery Act efforts.

Purchase Dates and Supporting Documentation for Claiming the First-Time Homebuyer Credit

To claim the Credit, eligible taxpayers must complete and file IRS Form 5405, *First-Time Homebuyer Credit*.[8] The IRS developed this new form for eligible taxpayers to calculate and claim the Credit. This form requires the taxpayer to provide the amount

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[5] The amount of credit is reduced for individuals with modified Adjusted Gross Income (AGI) of more than $75,000 ($150,000 for joint filers), and is zero for those individuals with modified AGI in excess of $95,000 ($170,000 for joint filers).
[6] In addition to Section 1006, the Recovery Act also included a provision to create Recovery.gov. Recovery.gov is a Web site that was created to provide unprecedented transparency about how Recovery Act funds are being used, and increase accountability to guard against fraud, waste, and abuse. Timely and accurate reporting by Federal agencies provides both Congress and taxpayers an ability to track and monitor all Recovery Act funds on Recovery.gov with the level of transparency and accountability envisioned in the Recovery Act. In compliance with the Recovery Act's principles and reporting requirements, TIGTA's initial audit report of the First-Time Homebuyer Credit is publicly available at www.Recovery.gov as well as www.titga.gov, TIGTA's Internet Web site.
[7] According to Recovery.gov, tax relief accounts for approximately $288 billion of the Recovery Act provisions, or about one-third of the benefits expected from the Recovery Act. The President has stated that every taxpayer dollar spent on the economic recovery must be subject to unprecedented levels of transparency and accountability.
[8] See Appendix I on page 12.

of Credit being claimed, the address of the home qualifying for the Credit, and the date the home was purchased. The form was updated after the passage of the Recovery Act to reflect the increased amount of the Credit, as well as to change the allowable period for purchasing a home.

In an attempt to ensure the accuracy of claims for the First-Time Homebuyer Credit, the IRS developed computer programs to reject electronically filed tax returns or temporarily suspend the processing of paper tax returns with the following conditions:

- Claims in excess of the maximum allowable Credit;[9]
- Claims in excess of allowable amounts for those taxpayers with an Adjusted Gross Income exceeding income limitations;[10] or
- Claims without a Form 5405 attached.

During our review of the 2009 Filing Season,[11] we confirmed that IRS programming was effectively identifying the above conditions.[12] However, some key controls were missing to prevent an individual from erroneously or fraudulently claiming the Credit and receiving an erroneous refund of up to $8,000. For example, date of purchase information from electronically filed Forms 5405 was not used to verify eligibility for the Credit until late in the 2009 Filing Season. Furthermore, the IRS did not request that taxpayers attach additional documentation to tax returns to verify eligibility before allowing the Credits. For example, attaching a Form HUD-1, *U.S. Department of Housing and Urban Development Settlement Statement,*[13] received at closing, would enable the IRS to verify the purchase of a residence, the date of purchase, the purchase price, and the location of the residence. Although the submission of additional documentation would not substantiate the taxpayer as a first-time homebuyer, it would provide some level of deterrence for ineligible taxpayers.

In a memorandum that TIGTA issued to the IRS on November 25, 2008, we recommended the IRS ensure that information on each line of the Form 5405 was transcribed for paper returns and that the information from the form be used to validate claims for the First-Time Homebuyer Credit. [14] We also recommended the IRS require that taxpayers attach documentation to substantiate a home purchase in order to verify eligibility for the Credit.

In a response to our memorandum, the IRS disagreed with both of TIGTA's recommendations. Because of the extensive programming requirements and the late passage of HERA, the IRS did not transcribe the information from each line of Form

[9] The maximum allowable credit for claims under HERA is $7,500. The maximum allowable credit for claims under the Recovery Act is $8,000.
[10] See footnote 5 for Adjusted Gross Income limitations.
[11] A filing season is the period from January 1 through April 15 when most individual income tax returns are filed.
[12] *The 2009 Filing Season Was Successful Despite Significant Challenges Presented by the Passage of New Tax Legislation* (Reference Number 2009-40-142, dated September 21, 2009).
[13] See Appendix II on page 15.
[14] See footnote 12.

5405 into its computer system. The IRS responded that other strategies being employed would mitigate our concerns. The IRS also stated that a requirement to supply documentation with the tax return would be burdensome for both the taxpayer and the IRS.

The IRS considers the requirement to supply documentation burdensome because if taxpayers do not provide documentation, the IRS must still process the claim for the Credit. The IRS does not have math error authority to disallow the Credit during processing.[15] The IRS also noted that requiring documentation would preclude many taxpayers from electronically filing their returns. We disagree with the IRS's assertion that requiring documentation would preclude e-filing. Taxpayers claiming the Credit who wish to e-file their returns would still be able to do so, provided they separately mail a paper copy of the additional documentation. Furthermore, requiring taxpayers to provide documentation would discourage abuse of the Credit before it occurs, much in the same way that requiring documentation to substantiate certain noncash charitable contributions discourages abuse.

The law requires that a home be purchased before the Credit may be claimed. However, we identified more than 19,300 electronically filed 2008 tax returns on which taxpayers claimed the First-Time Homebuyer Credit for a home which had not yet been purchased, but allegedly would be in the future. Had the IRS timely implemented our recommendations to both capture and use the purchase date from the Form 5405, these claims would not have been paid. The amount of the Credits inappropriately claimed via e-filing totaled more than $139 million. We have not yet determined the number of paper returns with similar claims.

During the 2009 Filing Season, the IRS implemented computer programming to reject claims electronically filed with a future purchase date. Controls were also implemented to identify and disallow claims filed on paper tax returns with future purchase dates. However, at the time we completed our report, the IRS had not decided whether to go back and review or correct the more than 19,300 electronically filed tax returns with future purchase dates or try to identify paper returns meeting the same criteria that may have been processed before controls were put into place. According to the IRS, the filters and controls they put into place to identify post-refund erroneous claims should identify all erroneous claims, including those with home purchase dates in the future.

The IRS's plans to address this issue are not adequate. The IRS's filters will allow some taxpayers the use of money to which they were not entitled, and may never

[15] Math error authority allows the IRS to assess and send a notice of assessment of additional tax without using deficiency procedures. The procedure called "notice of deficiency" (deficiency procedure) provides the taxpayer with a method of appealing tax and/or penalties to the United States Tax Court prior to their assessment. Math errors include addition and subtraction errors on the tax return, use of the incorrect tax table, omission of information required on the tax return to substantiate an entry, and missing or incorrect Taxpayer Identification Numbers for exemptions and certain Earned Income Tax Credit disallowances.

be entitled. In addition, the criterion used by the IRS will not ensure that a home purchase was made.

We recommended that the IRS initiate actions to determine whether those 19,300 taxpayers known to have claimed the Credit for a future home purchase have actually purchased a home. If not, steps should be taken to recover the erroneous Credits. The IRS agreed with this recommendation. The IRS has identified the issue of taxpayers claiming the Credit for future home purchases as an important element of the overall examination and compliance plan. The IRS agreed to flag these tax returns for necessary follow-up with the taxpayers involved.

Although the IRS does not have authority to reject claims for the Credit made by taxpayers who do not provide documentation, it does have the authority to audit those claims. The fact that a taxpayer could not, or would not, provide the requested documentation, such as a HUD-1 form, would be a strong indicator that the claim for the Credit was highly questionable and may warrant a pre-refund audit.

The IRS also contends that our conclusion that it improperly paid out $139 million to taxpayers claiming the Credit for future purchases is premature because the taxpayers may ultimately purchase a home. The IRS's reasoning on this issue is not correct according to law. At the time the IRS paid the Credit to these taxpayers, the taxpayers did not qualify for the Credit. As noted earlier, the law does not provide for prepayment of the Credit, and by making these payments the IRS did not properly administer the tax law, regardless of whether or not the taxpayers will subsequently purchase a home.

We also recommended that the IRS perform a review to determine the extent to which these improper claims occurred on paper-filed returns. If warranted, the IRS should identify all paper-filed returns claiming First-Time Homebuyer Credits for future purchases and ensure the purchases have taken place or the Credits are recovered. The IRS agreed with this recommendation and stated it would develop a plan to determine and assess the compliance risk associated with paper-filed returns claiming the Credit for future purchases. According to the IRS, the compliance program has already commenced and will extend into calendar year 2010.

Indications of Prior Home Ownership

The law defines a "first-time homebuyer" as any individual (and spouse, if married) who had no ownership interest in a principal residence during the three-year period prior to the purchase of the home to which the Credit applies. TIGTA developed computer programs to identify taxpayers who may not have qualified as first-time homebuyers but claimed First-Time Homebuyer Credits on their 2008 tax returns. As of July 25, 2009, using these computer programs, we identified almost 74,000 First-Time Homebuyer Credit claims attached to an original Form 1040, *U.S. Individual Income Tax*

Return, totaling more than $500 million, that were claimed by taxpayers who had indications of prior home ownership within the preceding three years.[16]

The almost 74,000 taxpayers had entered information on their individual income tax returns for one of the prior three years indicating they may have owned a home. These entries included deductions for home mortgage interest, real estate taxes, deductible points and qualified mortgage insurance premiums. While these entries indicate home ownership, the homes involved may or may not have been the taxpayers' principal residences, so the deductions do not automatically disqualify the taxpayers from receiving the First-Time Homebuyer Credit. However, we believe they warrant scrutiny by the IRS.

The IRS reported that as of May 17, 2009, it had initiated the use of computerized filters to identify such taxpayers for examination. It plans to work the cases identified by these filters before a refund is paid. In such cases, the portion of the taxpayer's refund associated with the First-Time Homebuyer Credit is frozen until the IRS verifies that the taxpayer qualifies for the Credit. The IRS reported that as of May 24, 2009, 10,000 pre-refund cases totaling $75 million were stopped. In addition, during the period that it was developing its computerized filters, the IRS identified 10,000 questionable cases for examination to be worked on a post-refund basis.

We identified more than 70,000 questionable claims for First-Time Homebuyer Credits, totaling almost $480 million, received by the IRS prior to the initiation of its computerized pre-refund examination filters. We reviewed the tax accounts of a random sample of 50 of these taxpayers. None of the accounts had received scrutiny from either the IRS's Questionable Refund Program or the Examination function relative to their claims for the First-Time Homebuyer Credit.

At the time we issued our interim report, the IRS had not decided whether or not the claims for the more than 70,000 Credits will be subject to post-refund examinations. We found that more than 12,000 of the approximately 70,000 Credits were claimed by taxpayers who had claimed the Residential Energy Credit on one of their prior three tax returns.[17] This increases the likelihood that the taxpayers owned a principal residence and do not qualify for the First-Time Homebuyer Credit since the Residential Energy Credit generally is only available for qualified expenditures made on a taxpayer's principal residence.

We recommended that the IRS initiate actions to recover the First-Time Homebuyer Credit, when appropriate, from taxpayers who had previously claimed the Residential Energy Credit, the District of Columbia's First-Time Homebuyer Credit,[18] or

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[16] Some of these questionable claims were filed by IRS employees. These cases were referred to TIGTA's Office of Investigations.
[17] Taxpayers may be eligible to claim a Residential Energy Credit for energy saving improvements made to their homes located in the United States. Taxpayers must reduce the basis of their homes by the amount of any credits allowed.
[18] In an effort to revitalize city neighborhoods, first-time homebuyers in the District of Columbia (the District) have been allowed a credit against their Federal income tax equal to $5,000 since

the Mortgage Interest Credit[19] on their individual income tax returns and develop a plan to review the other questionable claims that were processed prior to the IRS filters being implemented.[20] The IRS agreed with this recommendation and stated that currently all returns are screened for questionable First-Time Homebuyer Credit indicators and stored in a database that will be used to select cases for examination in accordance with the IRS's overall compliance plan.

First-Time Homebuyers Younger Than 18 Years Old

Through July 25, 2009, we identified more than 580 taxpayers younger than 18 years of age who claimed almost $4 million in First-Time Homebuyer Credits. The youngest taxpayers receiving the Credit were four years old. Contract law generally exempts children under the age of 18 from being bound by the terms of a contract. Therefore, it is unlikely that these taxpayers would have entered into an arm's-length transaction for the purchase of a home.

As of May 17, 2009, the IRS implemented examination filters to identify potentially erroneous claims for the First-Time Homebuyer Credit. The age of the taxpayer receiving the Credit was not one of the specific filters implemented by the IRS to screen claims for the Credit on originally filed returns. The IRS believed that its filter identifying taxpayers claiming the Credit who had Adjusted Gross Incomes below certain levels would catch these questionable claims.

One hundred sixty-five (28 percent) of the more than 580 taxpayers under age 18 that we identified claiming the Credit did not meet the IRS's Adjusted Gross Income screening criteria. In 64 of these cases, other IRS filters flagged the claim for further scrutiny. However, 101 of the claims for the First-Time Homebuyer Credit made by children under the age of 18 did not meet any of the IRS screening criteria.[21] The total amount of these Credits was almost $627,000.

We recommended that the IRS add age to the filters for pre-refund examinations of claims for First-Time Homebuyer Credits filed with original returns. The IRS agreed with this recommendation and indicated that it would develop additional age filters to capture residual returns not captured by existing filters.

1997. A first-time homebuyer in the District is any taxpayer that has had no interest in a principal residence in the District within the last year. Non-District residents, including non-District resident homeowners, are eligible to claim the credit for a home purchased in the city.

[19] The Mortgage Interest Credit is intended to help lower-income individuals afford home ownership. If qualified, a taxpayer can claim the credit each year for part of the home mortgage interest paid. Taxpayers may be eligible if they were issued a Mortgage Credit Certificate (MCC) from their State or local government. Generally, an MCC is issued only in connection with a new mortgage for the purchase of a taxpayer's principal residence. The MCC will show the certificate credit rate taxpayers should use to figure the credit. It also will show the certified indebtedness amount. Only the interest on that amount qualifies for the credit.

[20] We are in the process of identifying taxpayers who claimed the District of Columbia's First-Time Homebuyer Credit or the Mortgage Interest Credit in the prior three years as well. Both of these credits apply only to a principal residence.

[21] Sixty-seven of these cases were filed before the IRS screening criteria were put into place, but would not have met the criteria had they been implemented at the time the returns were filed.

First-Time Homebuyers with ITINs

The IRS issues Individual Taxpayer Identification Numbers (ITIN) to help individuals comply with U.S. tax laws and to provide a means to efficiently process and account for tax returns. Only individuals who have valid filing requirements or are filing tax returns to claim refunds of over-withheld taxes are eligible to receive ITINs. ITINs are issued regardless of an individual's immigration status. An ITIN does not indicate that an individual is authorized to live or work in the U.S. To be eligible to work in the U.S., a taxpayer must have a Social Security Number that is valid for work. In calendar year 2006, resident aliens accounted for 93 percent of the total number of ITINs issued. Through July 25, 2009, we identified more than 3,200 taxpayers claiming First-Time Homebuyer Credits totaling over $20.8 million on tax returns filed with ITINs.

The Personal Responsibility and Work Opportunity Reconciliation Act of 1996[22] prohibits aliens residing without authorization in the U.S. from receiving most Federal public benefits.[23] The Recovery Act specifically denies the First-Time Homebuyer Credit to individuals who are nonresident aliens. However, the Recovery Act is silent as to the eligibility for the Credit of resident aliens without a Social Security Number that is valid for work. In a report issued earlier this year, we noted that legislation is needed to clarify whether or not refundable tax credits may be paid to filers without a valid Social Security Number, and if these credits may not be paid, to provide the IRS with additional math error authority to disallow associated claims for the credits.[24]

Amended Returns Claiming the First-Time Homebuyer Credit

Taxpayers have several options to claim the First-Time Homebuyer Credit. One option is to amend their 2008 tax returns. Taxpayers who buy homes after they have already filed their 2008 tax returns but purchased them within the designated time frame can file amended returns. The amended tax returns will allow them to claim the Credit on their 2008 returns without waiting until 2010 to claim them on their 2009 returns.

We believe that amended returns are also vulnerable to erroneous claims for the First-Time Homebuyer Credit. During our audit of the First-Time Homebuyer Credit, we recommended that the IRS implement controls to ensure that taxpayers claiming the Credit on amended tax returns have not owned a principal residence within the prior three years. We suggested that the IRS perform research of historical taxpayer account data to

[22] P.L. 104-193 Section 401(c).
[23] The law defines a Federal public benefit as any grant, contract, loan, professional license, or commercial license provided by an agency of the United States or by appropriated funds of the United States; and any retirement, welfare, health, disability, public or assisted housing, postsecondary education, food assistance, unemployment benefit, or any other similar benefit for which payments or assistance are provided to an individual, household, or family eligibility unit by an agency of the United States or by appropriated funds of the United States. The law provides an exception for specified emergency services and programs.
[24] *Actions Are Needed to Ensure Proper Use of Individual Taxpayer Identification Numbers and to Verify or Limit Refundable Credit Claims* (Reference Number 2009-40-057, dated March 31, 2009)

ensure that taxpayers claiming the Credit do not have indications of prior home ownership that would disqualify them from claiming the Credit.

The IRS agreed with our recommendation and informed us that it was already in the process of developing criteria to identify amended returns with claims for the First-Time Homebuyer Credit for review by its Examination function. The IRS requested and was provided specific cases and details of our criteria for identifying questionable claims for the Credit. The criteria were incorporated into the Internal Revenue Manual on June 16, 2009.[25] Along with the criteria in the Internal Revenue Manual, the IRS enhanced its automated tool used to process amended tax returns. The tool was enhanced to automate research of IRS records for indications of prior home ownership over the past three years and other predetermined criteria that, if present, make the claim questionable.

Claims for Less than the Full Allowable Amount of the Credit

As of July 25, 2009, we identified approximately 48,500 taxpayers who appear to have not claimed or received the full amount of the First-Time Homebuyer Credit to which they may have been entitled. Many of these taxpayers claimed $7,500 rather than $8,000 for homes purchased in calendar year 2009. In our opinion, it is highly unlikely that these taxpayers purchased homes for exactly $75,000. The lesser amounts were claimed most likely because either the taxpayers filed their returns before the Recovery Act was passed or they did not realize that the new law increased the Credit amount to $8,000 for homes purchased in calendar year 2009. As of July 18, 2009, only about 7,900 (16 percent) of these taxpayers have amended their returns to claim the additional $500.

At the time we issued our interim report, the IRS did not plan to contact these taxpayers or to track whether these taxpayers file amended returns. The IRS believed taxpayers are aware of the additional $500 made available as a result of the Recovery Act and would amend their returns if warranted. In our opinion, this approach is not consistent with the intent of the Recovery Act, which is to provide a specified amount to eligible taxpayers in order to stimulate the economy.

For 2007, the IRS developed Package 1040A-3, *Information About Economic Stimulus Payments for Social Security, Veterans, and Other Beneficiaries,* to provide certain taxpayers with information and examples on how to claim their economic stimulus payments. A similar package informing taxpayers of how to amend their First-Time Homebuyer Credit claims may be beneficial.

We also recommended that the IRS monitor the accounts of taxpayers known to have purchased homes in calendar year 2009 and who claimed First-Time Homebuyer Credits of $7,500 to determine if the taxpayers amend their returns. If the taxpayers do not amend their returns, we recommended that the IRS contact these taxpayers to inform

[25] The Internal Revenue Manual (IRM) is the primary, official source of the IRS's instructions to its staff relating to the administration and operation of the IRS. The IRM contains the directions to which employees must adhere when carrying out their responsibilities in administering tax laws or other agency obligations.

them that they may be entitled to an additional refund if the purchase price of their home was greater than $75,000.

The IRS agreed with our recommendation and intends to send notices to taxpayers purchasing homes in calendar year 2009 and claiming a Credit of $7,500 but who have not amended their returns. The notice will inform taxpayers that they may be entitled to an additional refund. We also recommended that the IRS consider providing taxpayers with specific information detailing how to amend their tax returns to claim the full amount of the Credit to which they are entitled. The IRS agreed with this recommendation. The IRS will revise instructions for Form 1040, Form 1040X, *Amended U.S. Individual Income Tax Return*, and Publication 17, *Your Federal Income Tax For Individuals*, to include information to assist taxpayers in amending their returns if they did not claim the full amount of the Credit to which they were entitled.

Coding Tax Accounts to Distinguish Between Credits

We also determined that most of the approximately 48,500 taxpayers described above, who appeared to have not claimed or received the full amount of the Credit, did not have their IRS accounts properly coded to indicate that their homes were acquired in calendar year 2009. Proper coding is significant because it is the indicator that the IRS will use to distinguish between taxpayers who must repay the First-Time Homebuyer Credit over 15 years (in accordance with HERA) and taxpayers who will not be required to do so unless they sell their homes within 36 months (in accordance with the Recovery Act). Unless the IRS properly codes the accounts, these taxpayers may eventually be subject to IRS collection procedures.

We reported this issue as part of our audit of the IRS 2009 Filing Season and recommended that the IRS take steps to accurately code these taxpayers' accounts to properly indicate whether the taxpayers are required to repay their Credits.

Conclusion

The First-Time Homebuyer Credit continues to play a significant role for millions of American taxpayers. Most recently, on October 8, 2009, the U.S. House of Representatives voted 416 to 0 to pass H.R. 3590, the Service Members Home Ownership Tax Act of 2009. This legislation would provide certain American service members, Foreign Service personnel, and some members of the intelligence community an additional 12 months past the current November 30, 2009, deadline in order to claim the First-Time Homebuyer Credit.

Based on the administration of the Credit to date, I am concerned about the IRS's ability to effectively administer the Credits claimed within the original deadline, let alone within an extended deadline for certain taxpayers. Although the IRS developed Form 5405 for eligible taxpayers to calculate and claim the Credit and implemented some controls to ensure the accuracy of claims for the Credit, several key controls were not designed or implemented. We are pleased that the IRS agreed to improve its controls in response to our findings. However, given the control shortcomings noted by TIGTA auditors, we will continue to provide oversight of the IRS's efforts to effectively administer the Credit and any extensions or changes to it. We plan to issue our next report assessing the administration of the Credit in spring 2010.

Mr. Chairman and Members of the Committee, thank you for the opportunity to provide TIGTA's assessment of the IRS's administration of the First-Time Homebuyer Credit. In closing, I would like to emphasize that TIGTA will continue to closely monitor the IRS's administration of the Credit and will promptly alert the IRS of any problems or emerging issues. I would be pleased to answer any questions you may have at the appropriate time.

Form **5405** (Rev. February 2009) Department of the Treasury Internal Revenue Service

First-Time Homebuyer Credit

► Attach to Form 1040

OMB No. 1545-0074
2008
Attachment Sequence No. 163

Name(s) shown on return | Your social security number

Part I **General Information**

A Address of home qualifying for the credit (if different from the address shown on return)

B Date acquired (see instructions)

C If you are choosing to claim the credit on your 2008 return for a main home bought after December 31, 2008, and before December 1, 2009, check here (see instructions) . . . . ► ☐

Part II **Credit**

1 Enter the **smaller** of:
- $7,500 ($8,000 if you purchased your home in 2009), but only half of that amount if married filing separately, **or**
- 10% of the purchase price of the home.

If someone other than a spouse also held an interest in the home, enter only your share of this amount (see instructions) **1**

2 Enter your modified adjusted gross income (see instructions) . . **2**

3 Is line 2 more than $75,000 ($150,000 if married filing jointly)?
No. Skip lines 3 through 5 and enter the amount from line 1 on line 6.
Yes. Subtract $75,000 ($150,000 if married filing jointly) from the amount on line 2 and enter the result **3**

4 Divide line 3 by $20,000 and enter the result as a decimal (rounded to at least three places). **Do not** enter more than 1.000 . . . . **4** X .

5 Multiply line 1 by line 4 . . . . **5**

6 Subtract line 5 from line 1. This is your **credit.** Enter here and on Form 1040, line 69 . . . . **6**

General Instructions

Section references are to the Internal Revenue Code.

Purpose of Form

Use Form 5405 to claim the first-time homebuyer credit. The credit may give you a refund even if you do not owe any tax.

For homes purchased in 2008, the credit operates much like an interest-free loan. You generally must repay it over a 15-year period. For homes purchased in 2009, you must repay the credit only if the home ceases to be your main home within the 36-month period beginning on the purchase date. See *Repayment of Credit* on page 2.

Who Can Claim the Credit

In general, you can claim the credit if you are a first-time homebuyer. You are considered a first-time homebuyer if:

- You purchased your main home located in the United States after April 8, 2008, and before December 1, 2009.
- You (and your spouse if married) did not own any other main home during the 3-year period ending on the date of purchase.

If you constructed your main home, you are treated as having purchased it on the date you first occupied it.

Main home. Your main home is the one you live in most of the time. It can be a house, houseboat, housetrailer, cooperative apartment, condominium, or other type of residence.

Who Cannot Claim the Credit

You cannot claim the credit if any of the following apply.

1. Your modified adjusted gross income is $95,000 or more ($170,000 or more if married filing jointly). See the instructions for line 2.

2. You are, or were, eligible to claim the District of Columbia first-time homebuyer credit for any tax year. This rule does not apply for a home purchased in 2009.

3. Your home financing comes from tax-exempt mortgage revenue bonds. This rule does not apply for a home purchased in 2009.

4. You are a nonresident alien.

5. Your home is located outside the United States.

6. You sell the home, or it ceases to be your main home, before the end of 2008.

7. You acquired your home by gift or inheritance.

8. You acquired your home from a related person.

A related person includes:

a. Your spouse, ancestors (parents, grandparents, etc.), or lineal descendants (children, grandchildren, etc.).

b. A corporation in which you directly or indirectly own more than 50% in value of the outstanding stock of the corporation.

c. A partnership in which you directly or indirectly own more than 50% of the capital interest or profits interest.

For Paperwork Reduction Act Notice, see page 3. Cat. No. 11880I Form **5405** (2008) (Rev. 2-2009)

For more information about related persons, see *Nondeductible Loss* in Chapter 2 of Pub. 544, *Sales and Other Dispositions of Assets.* When determining whether you acquired your main home from a related person, family members in that discussion (except item 7) include only the people mentioned in 8a above.

Amount of the Credit

Generally, the credit is the smaller of:

- $7,500 ($8,000 if you purchased your home in 2009), but only half of that amount if married filing separately, **or**
- 10% of the purchase price of the home.

You are allowed the full amount of the credit if your modified adjusted gross income (MAGI) is $75,000 or less ($150,000 or less if married filing jointly). The phase-out of the credit begins when your MAGI exceeds $75,000 ($150,000 if married filing jointly). The credit is eliminated completely when your MAGI reaches $95,000 ($170,000 if married filing jointly).

Repayment of Credit

Homes purchased in 2008. You generally must repay the credit over a 15-year period in 15 equal installments. The repayment period begins in 2010 and you must include the first installment as additional tax on your 2010 tax return.

If your home ceases to be your main home before the 15-year period is up, you must include all remaining annual installments as additional tax on the return for the tax year that happens. This includes situations where you sell the home, you convert it to business or rental property, or the home is destroyed, condemned, or disposed of under threat of condemnation.

If you and your spouse claim the credit on a joint return, each spouse is treated as having been allowed half of the credit for purposes of repaying the credit.

Example 1. You claimed a $7,500 credit on your 2008 tax return. You must include $500 ($7,500 ÷ 15) as additional tax on your 2010 tax return and on each tax return for the next 14 years.

Example 2. You claimed a $7,500 credit on your 2008 tax return. In 2009, you sold the home to your son. You must include $7,500 as additional tax on your 2009 tax return.

Exceptions. The following are exceptions to the repayment rule.

- If you sell the home to someone who is **not** related to you, the repayment in the year of sale is limited to the amount of gain on the sale. (See item 8 under *Who Cannot Claim the Credit* for the definition of a related person.) When figuring the gain, reduce the adjusted basis of the home by the amount of the credit you did not repay.
- If the home is destroyed, condemned, or disposed of under threat of condemnation, and you acquire a new main home within 2 years of the event, you continue to pay the installments over the remainder of the 15-year repayment period.
- If, as part of a divorce settlement, the home is transferred to a spouse or former spouse, the spouse who receives the home is responsible for making all subsequent installment payments.
- If you die, any remaining annual installments are not due. If you filed a joint return and then you die, your surviving spouse would be required to repay his or her half of the remaining repayment amount.

Homes purchased in 2009. You must repay the credit only if the home ceases to be your main home within the 36-month period beginning on the purchase date. This includes situations where you sell the home, you convert it to business or rental property, or the home is destroyed, condemned, or disposed of under threat of condemnation. You repay the credit by including it as additional tax on the return for the year the home ceases to be your main home. If the home continues to be your main home for at least 36 months beginning on the purchase date, you do not have to repay any of the credit.

If you and your spouse claim the credit on a joint return, each spouse is treated as having been allowed half of the credit for purposes of repaying the credit.

Exceptions. The following are exceptions to the repayment rule.

- If you sell the home to someone who is **not** related to you, the repayment in the year of sale is limited to the amount of gain on the sale. (See item 8 under *Who Cannot Claim the Credit* for the definition of a related person.) When figuring the gain, reduce the adjusted basis of the home by the amount of the credit.
- If the home is destroyed, condemned, or disposed of under threat of condemnation, and you acquire a new main home within 2 years of the event, you do not have to repay the credit.
- If, as part of a divorce settlement, the home is transferred to a spouse or former spouse, the spouse who receives the home is responsible for repaying the credit.
- If you die, repayment of the credit is not required. If you filed a joint return and then you die, your surviving spouse would be required to repay his or her half of the credit.

Specific Instructions

Part I General Information

Line B. Enter the date you acquired the home. This is the date you purchased it (or the date you first occupied it if you constructed your main home).

Line C. You can choose to claim the credit on your 2008 Form 1040 for a main home purchased after December 31, 2008, and before December 1, 2009. If you make this choice, check the box.

Part II Credit

Line 1. If two or more unmarried individuals buy a main home, they can allocate the credit among the individual owners using any reasonable method. The total amount allocated cannot exceed the smaller of $7,500 ($8,000 if you purchased your home in 2009) or 10% of the purchase price. See *Purchase price* on page 3.

Note. A reasonable method is any method that does not allocate all or a part of the credit to a co-owner who is not eligible to claim that part of the credit.

Purchase price. The purchase price is the adjusted basis of your home on the date you purchased it. This includes certain settlement or closing costs (such as legal fees and recording fees) and your down payment and debt (such as a first or second mortgage or notes you gave the seller in payment for the home). If you build, or contract to build, a new home, your purchase price can include costs of construction. For more information about adjusted basis, see Pub. 551, Basis of Assets.

Line 2. Your modified adjusted gross income is the amount from Form 1040, line 38, increased by the total of any:

- Exclusion of income from Puerto Rico, and
- Amount from Form 2555, lines 45 and 50; Form 2555-EZ, line 18; and Form 4563, line 15.

Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws and to allow us to figure and collect the right amount of tax.

You are not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. Generally, tax returns and return information are confidential, as required by section 6103.

The average time and expenses required to complete and file this form will vary depending on individual circumstances. For the estimated averages, see the instructions for your income tax return.

If you have suggestions for making this form simpler, we would be happy to hear from you. See the instructions for your income tax return.

Appendix II

A. **Settlement Statement**

U.S. Department of Housing and Urban Development

OMB Approval No. 2502-0265

B. Type of Loan			
1. ☐ FHA 2. ☐ FmHA 3. ☐ Conv. Unins. 4. ☐ VA 5. ☐ Conv. Ins.	6. File Number:	7. Loan Number:	8. Mortgage Insurance Case Number:

C. Note: This form is furnished to give you a statement of actual settlement costs. Amounts paid to and by the settlement agent are shown. Items marked "(p.o.c.)" were paid outside the closing; they are shown here for informational purposes and are not included in the totals.

D. Name & Address of Borrower:	E. Name & Address of Seller:	F. Name & Address of Lender:

G. Property Location:	H. Settlement Agent:	
	Place of Settlement:	I. Settlement Date:

J. Summary of Borrower's Transaction		K. Summary of Seller's Transaction	
100. Gross Amount Due From Borrower		**400. Gross Amount Due To Seller**	
101. Contract sales price		401. Contract sales price	
102. Personal property		402. Personal property	
103. Settlement charges to borrower (line 1400)		403.	
104.		404.	
105.		405.	
Adjustments for items paid by seller in advance		**Adjustments for items paid by seller in advance**	
106. City/town taxes to		406. City/town taxes to	
107. County taxes to		407. County taxes to	
108. Assessments to		408. Assessments to	
109.		409.	
110.		410.	
111.		411.	
112.		412.	
120. Gross Amount Due From Borrower		**420. Gross Amount Due To Seller**	
200. Amounts Paid By Or In Behalf Of Borrower		**500. Reductions In Amount Due To Seller**	
201. Deposit or earnest money		501. Excess deposit (see instructions)	
202. Principal amount of new loan(s)		502. Settlement charges to seller (line 1400)	
203. Existing loan(s) taken subject to		503. Existing loan(s) taken subject to	
204.		504. Payoff of first mortgage loan	
205.		505. Payoff of second mortgage loan	
206.		506.	
207.		507.	
208.		508.	
209.		509.	
Adjustments for items unpaid by seller		**Adjustments for items unpaid by seller**	
210. City/town taxes to		510. City/town taxes to	
211. County taxes to		511. County taxes to	
212. Assessments to		512. Assessments to	
213.		513.	
214.		514.	
215.		515.	
216.		516.	
217.		517.	
218.		518.	
219.		519.	
220. Total Paid By/For Borrower		**520. Total Reduction Amount Due Seller**	
300. Cash At Settlement From/To Borrower		**600. Cash At Settlement To/From Seller**	
301. Gross Amount due from borrower (line 120)		601. Gross amount due to seller (line 420)	
302. Less amounts paid by/for borrower (line 220)	( )	602. Less reductions in amt. due seller (line 520)	( )
303. Cash ☐ From ☐ To Borrower		**603. Cash ☐ To ☐ From Seller**	

Section 5 of the Real Estate Settlement Procedures Act (RESPA) requires the following: • HUD must develop a Special Information Booklet to help persons borrowing money to finance the purchase of residential real estate to better understand the nature and costs of real estate settlement services; • Each lender must provide the booklet to all applicants from whom it receives or for whom it prepares a written application to borrow money to finance the purchase of residential real estate; • Lenders must prepare and distribute with the Booklet a Good Faith Estimate of the settlement costs that the borrower is likely to incur in connection with the settlement. These disclosures are manadatory.

Section 4(a) of RESPA mandates that HUD develop and prescribe this standard form to be used at the time of loan settlement to provide full disclosure of all charges imposed upon the borrower and seller. These are third party disclosures that are designed to provide the borrower with pertinent information during the settlement process in order to be a better shopper.

The Public Reporting Burden for this collection of information is estimated to average one hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.

This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number.

The information requested does not lend itself to confidentiality.

Previous editions are obsolete

Page 1 of 2

form **HUD-1** (3/86)
ref Handbook 4305.2

L. Settlement Charges

	Paid From Borrowers Funds at Settlement	Paid From Seller's Funds at Settlement
700. Total Sales/Broker's Commission based on price $ @ % =		
Division of Commission (line 700) as follows:		
701. $ to		
702. $ to		
703. Commission paid at Settlement		
704.		
800. Items Payable In Connection With Loan		
801. Loan Origination Fee %		
802. Loan Discount %		
803. Appraisal Fee to		
804. Credit Report to		
805. Lender's Inspection Fee		
806. Mortgage Insurance Application Fee to		
807. Assumption Fee		
808.		
809.		
810.		
811.		
900. Items Required By Lender To Be Paid In Advance		
901. Interest from to @$ /day		
902. Mortgage Insurance Premium for months to		
903. Hazard Insurance Premium for years to		
904. years to		
905.		
1000. Reserves Deposited With Lender		
1001. Hazard insurance months@$ per month		
1002. Mortgage insurance months@$ per month		
1003. City property taxes months@$ per month		
1004. County property taxes months@$ per month		
1005. Annual assessments months@$ per month		
1006. months@$ per month		
1007. months@$ per month		
1008. months@$ per month		
1100. Title Charges		
1101. Settlement or closing fee to		
1102. Abstract or title search to		
1103. Title examination to		
1104. Title insurance binder to		
1105. Document preparation to		
1106. Notary fees to		
1107. Attorney's fees to		
(includes above items numbers:)		
1108. Title insurance to		
(includes above items numbers:)		
1109. Lender's coverage $		
1110. Owner's coverage $		
1111.		
1112.		
1113.		
1200. Government Recording and Transfer Charges		
1201. Recording fees: Deed $; Mortgage $; Releases $		
1202. City/county tax/stamps: Deed $; Mortgage $		
1203. State tax/stamps: Deed $; Mortgage $		
1204.		
1205.		
1300. Additional Settlement Charges		
1301. Survey to		
1302. Pest inspection to		
1303.		
1304.		
1305.		
1400. Total Settlement Charges (enter on lines 103, Section J and 502, Section K)		