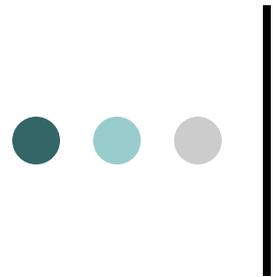


Demographic and Noncompliance Study of the Advance EITC (AEITC)

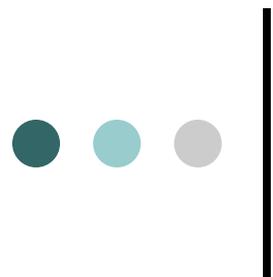
Presented at the 2008 IRS Research Conference
Wednesday, June 11, 2008

Joanna Stamatiades and James Cook,
Government Accountability Office
Eric Larson, Wage & Investment Division,
Internal Revenue Service



Introduction

- Background
- Prior Methods For Calculating AEITC Use
- Alternative Method: Use of the Form W-2
- Challenges in Analyzing the Form W-2 Data File
- Overcoming the Challenges: The Use of Subpopulations
- New Findings From Using Forms W-2
- Results, Conclusions, Finale



Background: Congressional Interest in the AEITC

- GAO conducted this research at the request of the Joint Committee on Taxation
- Little has been known about the individuals who receive the AEITC, the employers who pay it and compliance with its requirements. Neither the IRS or employers are required to confirm the eligibility of those who elect the AEITC before they receive it.
- Limited research has been conducted on the AEITC since GAO last examined it in the early 1990s.



Background: GAO's AEITC Researchable Questions

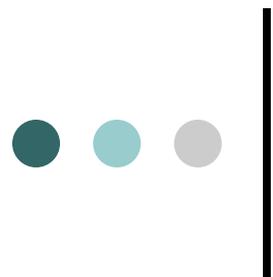
- How many individuals received the AEITC compared with the EITC and how much did they receive in tax years 2002 through 2004? What actions, if any, have been taken to increase use since 1992 and what is the potential for significant increases in the future?
- What is the extent of noncompliance, if any, associated with the AEITC?
- How well do IRS's procedures address any areas of noncompliance?



Background: AEITC

AEITC

- Allows taxpayers who expect to qualify for the EITC and have at least one qualifying child to receive part of the credit in each paycheck during the year.
- Capped at 60 percent of EITC for 1 qualifying child
- Significant requirements
 - Have only one Form W-5 in effect at a time
 - Inform employer if spouse also has a Form W-5 in effect
 - File a tax return reporting the AEITC payment amount as reported on the Form W-2, box 9



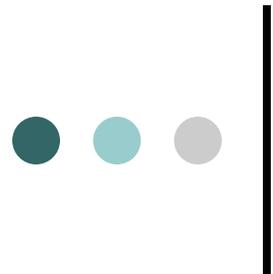
Prior Methods For Calculating AEITC Use

GAO's 1992 report (GAO/GGD-92-26)

- Method: Number of individuals who received the EITC in 1989 and also the AEITC.
- Result: Less than 0.5% of individuals who received the EITC elected the AEITC.

IRS's historical approach

- Method: Number of EITC returns reporting AEITC (using EITC claimed population)
- Result: Less than 1% of returns reported AEITC



Prior Methods For Calculating AEITC Use

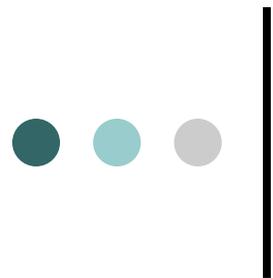
IRS's initial calculation for GAO's 2007 report

- Method: Number of taxpayers receiving AEITC
 - Taxpayers receiving and reporting AEITC + individuals receiving and not reporting
- Result: Less than 1% of returns that claimed the EITC also received the AEITC in tax year 2000-2002.



Alternative Method: Use of the Form W-2

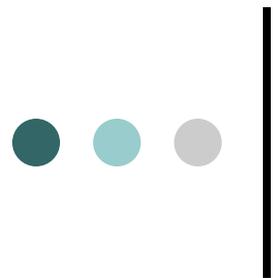
- Step 1: IRS developed a data file of all Forms W-2 for tax years 1999-2004 indicating an AEITC payment as shown by an amount greater than \$0 in box 9 of the Form W-2.
- Step 2: IRS and GAO calculated the number of individuals who received AEITC based on the number of Forms W-2 reporting AEITC per unique SSN.
- Step 3: All data pertaining to filed tax returns came either from returns that reported receipt of the AEITC or from a “constructed tax return.”



Alternative Method: Use of the Form W-2

Two caveats to this alternative method

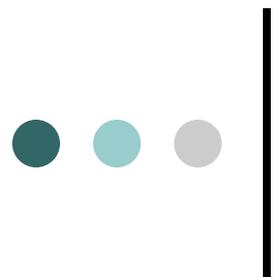
- The AEITC amount on the Form W-2 is not necessarily evidence that the employee actually received that amount.
- There could be instances when a tax return was filed but not detected using our methodology. For example, a taxpayer's SSN on the Form W-2 might have been incorrect and the taxpayer reported the correct SSN on the tax return.



Alternative Method: Use of the Form W-2

Two primary benefits of using the Form W-2

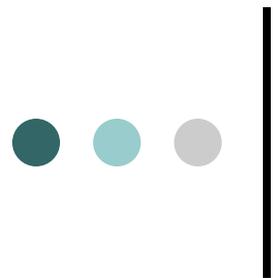
- It is the only document that contains the AEITC recipient's name, address, SSN, amount of AEITC paid and employer's name/address.
- It is the most comprehensive method used to date and accounts for instances when (1) individuals receive the AEITC, but do not file a return (2) file a return, but do not report receiving AEITC and (3) both spouses receive the AEITC and file jointly on one return.



Challenges in Analyzing the Form W-2 Data File

Challenge #1: In the majority of the years we examined, most Forms W-2 reported AEITC within the yearly limit, but extreme numbers skewed the results.

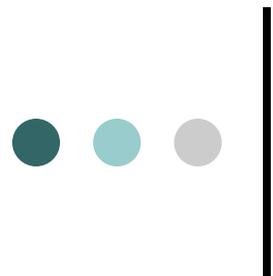
- Example: In TY 2004, 616,838 Forms W-2 received AEITC
 - 99.6% of these were within the yearly AEITC limit and accounted for about \$50 million in AEITC.
 - 11 Forms W-2 each reported \$100,000 or more in AEITC and accounted for a total of about \$6 million in AEITC.



Challenges in Analyzing the Form W-2 Data File

Challenge #2: Invalid SSNs

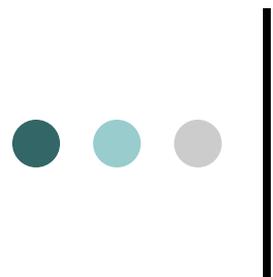
- Using the entire Form W-2 file, 5% of the SSNs with AEITC had an invalid SSN
 - Example: There were 935 instances of 000-00-0000 receiving AEITC.
- We then checked whether the Form W-2 SSN and name matched what was reported in IRS's National Account Profile. This analysis increased the invalid Form W-2 file population by another 15%, to a total of 20% invalid SSNs.



Overcoming the Challenges: The Use of Subpopulations

Used three criteria to create four subpopulations to capture all AEITC recipients. The three criteria were whether the:

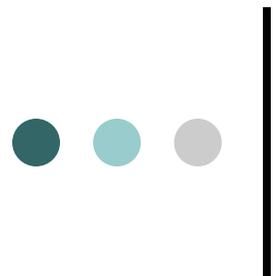
- SSN on the Form W-2 was valid (source: DM-1)
- SSN and recipient's name matched (source: DM-1)
- AEITC amount exceeded the yearly limit (source: Form W-2)



Overcoming the Challenges: The Use of Subpopulations

Four subpopulations were created to account for all Forms W-2

- **Valid subpopulation:** Individuals with (1) a valid SSN, per SSA (2) name and SSN match (3) AEITC within yearly max. More than 75 percent of the Forms W-2 on average were in this subpopulation.
- **Invalid name subpopulation:** Individuals with (1) a valid SSN (2) SSN didn't match individual's name (3) AEITC within yearly max. About 17 percent of the Forms W-2 fell in this subpopulation.



Overcoming the Challenges: The Use of Subpopulations

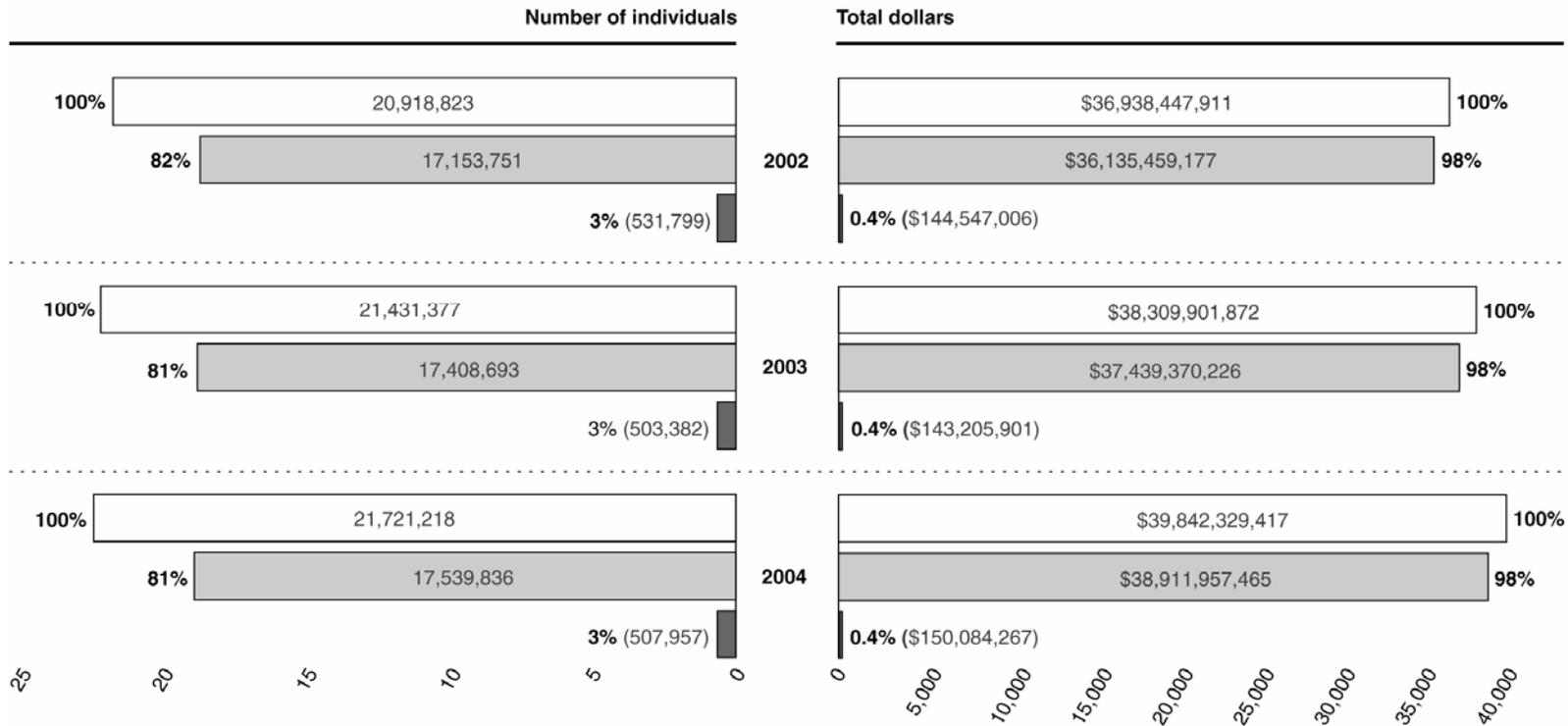
Four subpopulations were created to account for all Forms W-2

- **Invalid number subpopulation:** (1) All Forms W-2 with an invalid SSN (2) AEITC within yearly max. This subpopulation comprised about 7% of the Forms W-2.
- **Dollar limit subpopulation:** W-2 AEITC amount was above the yearly limit regardless whether the SSN was valid or the individual's name matched the SSN. This represented less than 1 percent on average of all Forms W-2.



New Findings From Using Forms W-2—Use Data

Number of EITC Recipients, EITC Recipients Potentially Eligible for the AEITC, AEITC Recipients, and Total Dollars They Received, Tax Years 2002 through 2004



This figure includes the valid, invalid name and invalid number subpopulations.

- EITC recipients (Percentage is total EITC recipients)
- EITC recipients potentially eligible for AEITC (Percentage is out of EITC recipients)
- AEITC recipients (Percentage is out of EITC recipients potentially eligible for AEITC)

Sources: GAO analysis of IRS data.



New Findings From Using Forms W-2—Dollars Received

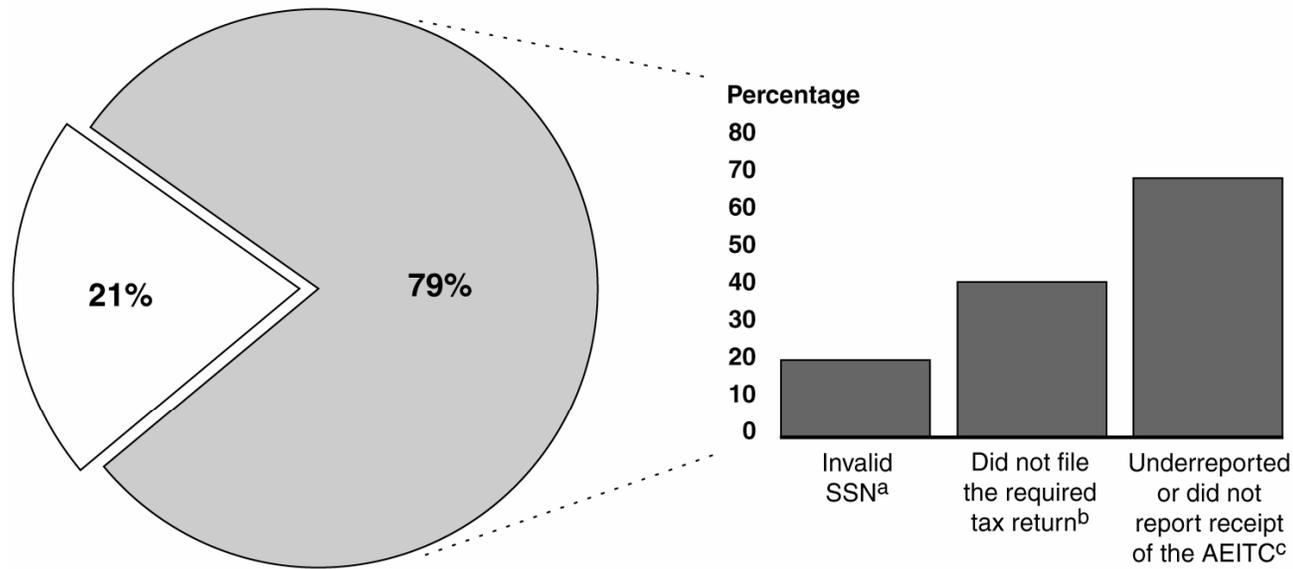
**Percentage of AEITC Recipients Receiving an Amount of AEITC,
Tax Years 2002-2004**

Amount of AEITC received	Percentage of AEITC recipients		
	2002	2003	2004
\$1-\$100	50	50	48
\$101-\$250	17	17	17
\$251-\$500	13	13	13
\$501-\$750	7	7	8
\$751-\$1,000	5	5	5
\$1,000—yearly maximum	7	8	8

This table includes the valid, invalid name and invalid number subpopulations.

New Findings From Using Forms W-2—Noncompliance

Percentage of AEITC Recipients Compliant and Noncompliant with at Least One AEITC Requirement, Tax Years 2002-2004



-  Complied with AEITC requirements reviewed
-  Did not comply with at least one AEITC requirement reviewed
-  Primary areas of noncompliance or errors

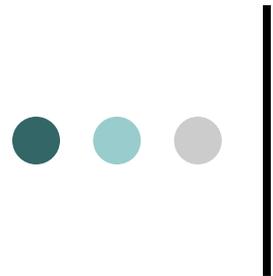
Source: GAO analysis of IRS data.

Note: The pie chart includes the valid, invalid name, and invalid number subpopulations.

^a This includes the invalid name and invalid number subpopulations.

^b This includes the valid, invalid name and invalid number subpopulations.

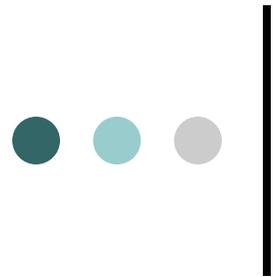
^c This is of individuals who filed a federal tax return in the valid, invalid name, and invalid number subpopulations.



Results from GAO's Findings

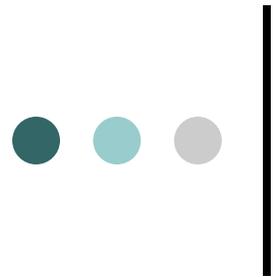
In making a recommendation to the Acting IRS Commissioner, GAO said IRS should consider whether any of three different options could cost effectively and significantly reduce AEITC noncompliance.

If IRS determines none of the options would be successful and if IRS believes no other remedies are viable, GAO recommended that the Treasury Secretary inform Congress of this and provide Treasury's opinion about whether the AEITC should be retained.



Conclusions

- Researchers should consider alternative sources of data, such as Forms W-2, as they can yield new data. However, they should understand the associated challenges that may exist, such as extreme values and invalid SSNs, and the additional amount of time that will likely be needed to work with and interpret the new data.
- Developing criteria to manage data can be an effective method to account for a wide variety of differing scenarios.
- Fostering strong interpersonal relationships can lead to quality analysis.



Finale

- Additional information about GAO's AEITC report can be found at gao.gov (report # GAO-07-1110)
- Questions or comments?