United States General Accounting Office 136591

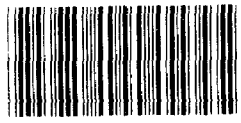
GAO Testimony

For Release
On Delivery
Expected At
2:00 p.m. EDT
Tuesday
August 9, 1988

Resolving Differences In Wage Amounts Reported By Employers to the Internal Revenue Service and Social Security Administration

Statement Of
Joseph F. Delfico
Senior Associate Director

Before the
Subcommittee on Social Security and the
Subcommittee on Oversight
Committee on Ways and Means
House of Representatives



SUMMARY

Consistent with recommendations in a September 1987 GAO report, on July 12, 1988, the Internal Revenue Service (IRS) and Social Security Administration (SSA) signed a new agreement detailing agency responsibilities under the Combined Annual Wage Reporting System. GAO believes the agreement is an improvement over the prior arrangement and should result in more employees' social security covered earnings being properly reported to and recorded by SSA.

The new agreement better recognizes the agencies responsibilities and enforcement authorities for wage reporting, more clearly delineates responsibilities and performance periods, establishes accountability for nonperformance, and works towards reducing future workloads.

Current efforts to address the backlog of unreconciled cases have met with limited success. Most employers SSA contacted either have not responded, are no longer in business, or no longer have the necessary records. It is unclear what additional actions the agencies can or should take for the 1978-86 unreconciled reports when employers do not respond to two mailings by SSA.

Future reconciliation efforts should be more successful because employer contacts will be made soon after wages are reported to SSA and IRS, thereby increasing the chances that employers are still in business and that they have necessary records. Also, SSA's new initiative to provide an earnings and benefit statement to all workers over 25, starting in 1991, should help individuals to identify discrepancies between earnings paid and SSA's records and seek correction of any problems.

Mr. Chairman and Members of the Subcommittees:

I am pleased to be here today to discuss the interagency agreement for the Combined Annual Wage Reporting System which was signed by the Internal Revenue Service (IRS) and the Social Security Administration (SSA) on July 12, 1988. The IRS and SSA revised their interagency agreement after we reported in September 1987[1] that they had failed to reconcile differences in employer reported wages.

Under the current system employers report aggregate wage amounts quarterly to IRS and each employee's wages annually to SSA. These totals are computer matched to determine if differences exist. These differences generally occur when employers fail to report to one of the agencies or they report different amounts to each agency. Sometimes the agencies themselves err in processing reports but these processing errors occur infrequently when compared to employer reporting errors. Omission of earnings from individuals' earnings records may eventually result in benefits which are too low.

We believe the revised agreement can be an effective vehicle for addressing and reducing future occurrences of employer reporting differences. The agreement provides for the

---

[1] Social Security: More Must Be Done To Credit Earnings to Individual's Accounts (GAO/HRD-87-52, September 18, 1987)

reconciliation actions we believe are necessary and establishes what we consider to be reasonable timeframes. The agencies also are designating resources for reconciling the backlog and for handling future workloads. However, though the agreement goes a long way toward reconciling future errors, early reconciliation results for past backlogs are not encouraging. I will elaborate briefly on each of these points.

THE AGREEMENT PROVIDES FOR NEEDED RECONCILIATION ACTIONS

Several events contributed to the former agreement's ineffectiveness. First, each agency held the other responsible for corresponding with employers to resolve SSA-related reporting differences. These were differences where the earnings reported to IRS were greater than those reported to SSA and, hence, appeared to have no tax potential. IRS limited its involvement to tax-related cases, and SSA argued that IRS should handle all cases because, unlike SSA, IRS had enforcement authority to penalize employers for errors in reporting. Consequently, a backlog of unreconciled reports accumulated because of the agencies' disagreement. Secondly, the agencies did not act to address causes of employer reporting differences.

For several reasons, we believe the new agreement improves the reconciliation process. First, the agreement requires actions by the appropriate parties. For 1987 and future tax years, SSA and IRS will share information that identifies

employers with reporting problems. SSA will then correspond with these employers requesting information needed to correct reporting differences. Copies of wage reports will be requested to substantiate any needed corrections to SSA records. Should employers fail to respond to this request, SSA will forward pertinent information on these employers to IRS for a second contact. IRS will then correspond with the employers and ask them to provide the requested information. It will also advise them that penalties may be assessed for failing to cooperate.

Second, the agreement addresses the backlog problem and causes of reporting differences. This agreement assigns SSA exclusive responsibility for working the 1978-86 backlog, thereby resolving the longstanding dispute between IRS and SSA.

In 1987 the agencies undertook a joint study to look more closely at the reasons for reporting differences. As a result of the study, the agreement was fashioned to address identified causes of reporting problems. For example, employers sometimes file quarterly reports to IRS under multiple identification numbers but file an annual report to SSA under one identification number. This makes it appear that SSA has not received an employer's report when it actually has. The new agreement requires IRS to improve the cross-referencing of employers' identification numbers furnished to SSA.

Finally, the agreement strengthens the periodic review process and holds the agencies accountable for nonperformance of designated responsibilities. The new agreement requires an IRS/SSA work group to evaluate the effectiveness of operations under the agreement, annually review data exchanges between the agencies, and provide a joint report with recommendations to the Commissioners of SSA and IRS. It requires that if either agency is unable to perform for any reason, the Commissioner of that agency must give the other Commissioner written notice and proposed remedial actions.

For the above reasons, we believe that under the revised agreement the agencies can more effectively reconcile reporting differences.

TIMEFRAMES APPEAR REASONABLE

Our September 1987 report disclosed that IRS and SSA had been slow to resolve their differences in reconciling reports. IRS initially had responsibility for reconciling all wage reports, but as early as 1980, informed SSA that it would not work SSA-related cases. For 1978 and later tax years, SSA accepted information from IRS identifying these cases but did not begin working them until 1986. As a result, SSA did not contact some employers to request them to explain their reporting differences until as long as 7 years after the reports were originally due.

The new agreement spells out timeframes for IRS and SSA to exchange data needed to identify employers with reporting problems who must be contacted. The first contact with employers will be about one year after the reports are due.

For example, SSA will complete the processing of tax year 1987 wage reports around the Fall of 1988. SSA will then provide IRS with information on the employers' reports it processed. IRS will use this information to compare employers reporting to SSA with its own records. The agreement requires IRS to give SSA, by March 1, 1989, information on the employer reports which show that more wages were reported to IRS. SSA will use this information to contact employers and request that they explain their reporting differences. By November 1, 1989, the agreement requires SSA to forward information on non-responding employers to IRS. By early 1990, IRS should mail follow-up correspondence to employers requesting explanations of reporting differences and advising them of the penalties for non-compliance.

Regarding the 1978-86 cases to be worked solely by SSA, to date, SSA has mailed a first and when necessary, a second correspondence to employers for most 1978-83 cases. SSA expects to mail the first correspondence to employers for the 1984-86 backlog early next year. While the agreement does not specify

when SSA should complete work on these cases, SSA said it will have contacted all employers involved by the end of 1989.

The timeframes relating to the exchange of reconciliation data and SSA's plans for completing work on the backlog appear reasonable. The required performance period for exchanging reconciliation data allows SSA sufficient time to correspond with and receive responses from employers before IRS follows-up with nonresponders. Additionally, IRS will have sufficient time to follow-up within the 4 year record retention period required by the tax code and request that employers provide wage data.

With regard to the 1984-86 backlog, SSA's experience in working 6 years of the backlog (1978-83) in about 3 years indicates that SSA should be able to work the remaining 3 years of the backlog within the next year.

ADEQUACY OF RESOURCES: DIFFICULT TO JUDGE

From 1978 to 1986 each agency devoted minimal resources to reconciling differences in employer reports. In 1980, IRS informed SSA that it lacked resources to reconcile cases where employers reported more wages to it than to SSA. SSA received information from IRS on the unworked cases, but it did not attempt to resolve the differences.

Both SSA and IRS have budgeted staff levels for handling the workload but judging the adequacy of the staff levels is difficult because of uncertainties over workloads and procedures. Several factors make future workloads difficult to predict. On the one hand the anticipated workload of employer reporting differences should be reduced due to agencies' actions to address known causes of reporting differences. On the other hand, SSA has taken actions that will increase the number of cases it will work by reducing the tolerance[2] it applies in deciding whether to reconcile discrepant reports. Additionally, because future reconciliation efforts will involve more current reports, it is likely employer responses will be higher and SSA will have more reports to process. It is also unclear how many cases will be referred to IRS for follow-up.

SSA will basically follow the same reconciliation procedures for tax year 1987 and future years as it did for working backlogged cases. However, SSA is also planning telephone contacts with employers having large discrepancies who do not respond to correspondence. It estimates that about 13,000 such calls might be made each year. IRS has not developed procedures yet for handling referred SSA cases. IRS told us that its procedures could include more than one correspondence with

---

[2]The new tolerance is equal to the dollar amount needed to earn a quarter of coverage.

employers, face-to-face contact with employers, and assessing and collecting penalties.

Given these uncertainties it is difficult to judge the adequacy of resource plans. SSA's fiscal year 1987 and 1988 budgets included 290 and 355 work years respectively, for reconciling the 1978-83 backlog. The agency's fiscal year 1989 budget includes 355 work years for reconciling the 1984-86 backlog as well as tax year 1987 reports. On the surface, these numbers appear reasonable.

IRS' proposed fiscal year 1990 budget includes 93 staff years for handling SSA referrals. IRS estimates it can handle 175,000 SSA referred cases at this staff level. Without knowledge of IRS' future workload and procedures, we can not adequately assess IRS' resource plans.

EFFECTIVENESS OF RECONCILIATION

We find it is difficult to predict the completeness of reconciliation under the new agreement. The effectiveness of reconciliation depends on factors such as being able to locate employers, contacting them before the 4 year record retention requirement expires, and having them cooperate with the information request.

We reviewed the results of SSA's working the 3.5 million reports included in the 1978-83 backlog to get an idea on the extent to which these factors influence the outcome. Our review showed that as of June 10, 1988, most of the differences in employer reports to the two agencies have not been resolved and likely will not be.

As of June 10, 1988, about 17 percent of the reports had been reconciled. This category includes cases where employers either submitted wage data for SSA to process or provided information that enabled SSA to determine that earnings had been reported to SSA but under a different identification number.

About 29 percent of the cases are still pending. This category includes cases for which SSA (1) has received employer responses but not completed work to close cases (2 percent) or (2) had previously excluded from its workload because the reporting difference was below an applied tolerance (27 percent). Due to lowering the tolerance, SSA will now contact about one half of the employers whose cases were previously excluded.

For over half the cases in the 1978-83 backlog, SSA has been unsuccessful to date in reconciling differences. SSA could not reconcile about 25 percent of the reports because the employers could not be contacted for reasons such as business closing or relocations or they responded that they no longer had wage data

available. This situation highlights the need for timely contacts to reconcile differences.

Finally, for the remaining cases (about 29 percent), it is uncertain to what extent they will be reconciled. This category includes employers who have not responded to SSA's first and second correspondence effort. SSA attempts to contact employers up to two times. If no response is received, SSA generally will make no further reconciliation contacts. It will, however, accept and process wage data should these employers later submit reports. There are no plans to forward these cases to IRS for possible enforcement action. IRS pointed out that questions exist as to whether IRS could assess penalties based solely on SSA's certification that employers failed to report. This is a problem because until recently, SSA did not record the receipt of wage reports.

Despite SSA's limited success in working the backlog, the results of future work under the new agreement should be better. Because reconciliation will begin the year after employers' reports were due, it is less likely that the businesses will have terminated or relocated. As a result, more employers will be contacted and should have wage data available, and IRS will use its enforcement authority to encourage employer cooperation.

Lastly, one SSA project unrelated to the interagency agreement but related to the issue of the reporting of earnings, is SSA's newly developed earnings and benefit statement. Starting this month SSA plans to make available, upon request, an estimate of social security benefits and a statement of all earnings posted to an individual's account. Starting in 1991 SSA plans to begin sending these statements to all workers over age 25 on a periodic basis. This will provide a way for them to check the accuracy of earnings posted to their account. We support this effort and think it will help individuals to identify and resolve problems associated with unreconciled earnings.

This concludes my statement. I will be happy to answer questions.