



General Government Division

B-271108

June 26, 1996

The Honorable Bill Archer
Chairman, Committee on
Ways and Means
House of Representatives

Dear Mr. Chairman:

This letter responds to your January 5, 1996, request that we review the processing and issuance of income tax refund payments in 1996 and compare this year's pattern to prior years' patterns for the timing of income tax refund payments. Your request was prompted by a concern that the timing of income tax refund payments might be manipulated to avoid reaching the debt limit.

In response to your request, we (1) analyzed IRS data on the number of returns received and the number and dollar amount of refunds issued for each week of 1994, 1995, and 1996 (through April 26, 1996); (2) monitored the results of IRS' annual test of refund timeliness; and (3) tracked a sample of paper returns with refund claims that were processed by IRS' Kansas City Service Center (KCSC). We conducted our work from January through May 1996 in accordance with generally accepted government auditing standards.

RESULTS IN BRIEF

Our work indicated that (1) the number and dollar amount of refunds issued as of the end of April 1996 either exceeded or closely approximated the end-of-April figures for 1994 and 1995 and (2) the average number of days for issuing refunds in 1996 was the same as in past years. Also, our tracking of returns processed by KCSC showed nothing unusual. Thus, there is no evidence that any special steps were taken in 1996 to delay refunds.¹ That conclusion is supported by the absence of any evidence of public outcry over delayed refunds. By comparison, there was

¹This does not mean that no refunds were delayed in 1996. As in 1995, but to a much lesser degree, IRS delayed some refunds in 1996 to verify Social Security numbers and Earned Income Credit claims.

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much adverse reaction in 1995 when IRS delayed millions of refunds for several weeks to verify Social Security numbers and Earned Income Credit claims.

COMPARISON OF 1996 DATA WITH
DATA FOR 1995 AND 1994

IRS maintains cumulative data, which it updates weekly, on the number of returns received and the number and amount of refunds issued. We obtained those data for 1994, 1995, and the first 4 months of 1996, to see whether there was any indication of a significant difference in patterns this year compared with the past 2 years. We saw none.

Table 1 shows comparable statistics as of the end of April for each of the 3 years.

Table 1: Data on the Number of Returns Received and the Number and Amount of Refunds Issued as of the End of April 1994, 1995, and 1996

	1994	1995	1996
Returns received (in thousands)	106,762	107,291	103,400
Number of refunds issued (in thousands)	60,216	57,401	59,783
Percentage of returns receiving refunds	56.4%	53.5%	57.8%
Amount refunded (in millions)	\$61,877	\$64,031	\$73,313
Average refund amount	\$ 1,028	\$ 1,116	\$ 1,226

Source: IRS' Management Information System for Top Level Executives.

IRS' REFUND TIMELINESS TEST

To further check whether refunds were being issued in a timely manner, we obtained the results of IRS' tests of refund timeliness for 1996.

For the past several years, IRS has reviewed samples of refunds on paper returns to measure its performance in issuing refunds. IRS' goal, as documented in its customer service standards, is to issue refunds on paper returns within 40 days. To measure actual performance, each of IRS' 10 service centers takes four samples during the filing season and computes the elapsed time from the date the taxpayer signed the return to the date the taxpayer would have received the refund. IRS estimates the

latter date by allowing 2 days after refund issuance for the refund to reach the taxpayer. In 1994, we examined the methodology IRS was using to test refund timeliness by replicating the test at one service center. We concluded that the service center's test provided a valid measure of refund timeliness.²

According to IRS, there were only minor changes to its test methodology this year. One change involved the handling of refunds that are paid by direct deposit. Because this was the first year that filers of paper returns could ask for a direct deposit, IRS decided to exclude direct deposits from the timeliness sample. To do otherwise could have distorted year-to-year comparisons, because direct deposits are faster than paper checks.

IRS' tests of refund timeliness during the 1993, 1994, and 1995 filing seasons showed that, in each of those years, refunds on paper returns were issued in an average of 36 days. As of May 29, 1996, IRS had completed three of its four samples for the 1996 filing season. Those three samples covered refunds issued during the weeks ending February 10, March 9, and April 6, 1996.³ The results of the samples, as reported by IRS, showed that refunds were issued in an average of (1) 33 days during the first test week, compared with 31 days for the first sample last year, and (2) 37 days during the second week and 36 days during the third week, which were the same averages as last year's.⁴ As noted, those results closely approximate last year's and are well within IRS' goal of 40 days. Because IRS' processing times tend to increase as the filing season progresses and return volumes grow, it is reasonable to expect the average refund issuance time to increase after the first sample.

SAMPLE OF REFUND CLAIMS PROCESSED BY KCSC

As an independent check on the timeliness of refunds, we took a sample of paper returns with refund claims that were processed by KCSC and tracked those returns

²Tax Administration: Continuing Problems Affect Otherwise Successful 1994 Filing Season (GAO/GGD-95-5, Oct. 7, 1994).

³The other sample covered refunds issued during the week ending May 4, 1996.

⁴The average refund times in 1995 were somewhat lower than in 1996, even though IRS delayed millions of refunds for several weeks in 1995. That apparent contradiction stems from IRS' decision to exclude the delayed refunds from its samples in 1995. We expressed our concern with aspects of that decision in a December 29, 1995, report entitled The 1995 Tax Filing Season: IRS Performance Indicators Provide Incomplete Information About Some Problems (GAO/GGD-96-48).

and refunds through IRS' Martinsburg Computing Center (MCC) and Treasury's Financial Management Service (FMS).

Paper tax returns are processed by IRS' 10 service centers. When a center finishes processing a batch of returns, it is to forward the return information, via computer tape, to MCC for further processing and posting to IRS' master file of taxpayer accounts. After MCC posts the returns, it is to create a data tape with information on the refunds to be issued. Refund data for each service center are kept in separate files. The tapes are to be sent to FMS, which is responsible for sending refunds to taxpayers.

MCC also processes information on the refund data tapes, such as the total number and amount of the refunds, and creates a report known as Schedule 1166. MCC sends the 1166 to the respective service centers where the returns and refunds were processed, as well as to FMS so that it can compare the data on the tapes with that on the 1166 to ensure that all refunds are being issued.

After FMS processes the data tape, prints the refund checks, and mails them to taxpayers, it is to create an "Agency Confirmation Report Refund List" for each service center. The confirmation report, which certifies that the checks were issued, contains the range of check serial numbers and the total amount of checks issued. The service center is to match the data in the confirmation report to the data in the 1166 to ensure that all checks for the service center were issued.

On February 23, 1996, we judgmentally selected 100 refund returns to get a cross section of the various types of individual income tax returns. We selected 25 each from returns filed on paper forms 1040, 1040A, 1040EZ, and 1040PC. The returns were selected from work that had been completed by the service center during that week. The data from these returns were ready to be forwarded to MCC for processing to the taxpayers' accounts. We recorded each taxpayer's identification number, the document locator number from each return, the date the taxpayer signed the return, and the amount of each refund claimed.

After waiting 4 weeks for processing to be completed at MCC and the refund data tapes to be forwarded to FMS, we requested printouts of each taxpayer's account from IRS to see how closely the date the return was posted to the taxpayer's account matched the date the refund was authorized to be issued.

Refunds in our sample were processed at MCC during the weeks ending March 2 and March 9. We verified that the refunds processed during those 2 weeks were actually issued by tracking back to FMS' confirmation report. The confirmation report showed that the refunds for those 2 weeks were issued on March 8 and March 15, respectively.

We compared the amount from the confirmation report with the amount on the Schedules 1166 to ensure that all refunds KCSC processed for the week that ended on February 24, 1996, were processed to the master file and forwarded to FMS for issuance.

Results of Our Test

For 2 of the 100 cases in our sample, the above process was interrupted and issuance of the refund, was delayed.

- The first refund was delayed due to a Social Security number mismatch—caused by a taxpayer error—that prevented MCC from posting the return to the taxpayer's account. The mismatch was resolved, and the refund was authorized 3 weeks after the first attempt to post the return.
- The second refund was delayed due to a service center processing error involving overlooked withholdings claimed on the taxpayer's return. That error led IRS to believe that the taxpayer was not entitled to the claimed refund. When IRS discovered it, the error was corrected, and the refund was authorized about 3 weeks later than it would have been if there had been no error.

Of the 100 cases in our sample, 2 involved bifurcated refunds—i.e., a portion of the refund was issued while the rest was delayed until a question about the return could be resolved. In both cases, IRS' records indicated that the unquestioned portion of the refund was issued within the same week that processing of the return was completed, along with a notice explaining why the rest of the refund was being delayed.

AGENCY COMMENTS

We requested comments on a draft of this letter from the Commissioner of Internal Revenue or her designated representative. On June 12, 1996, we were advised by the Chief, Taxpayer Service, who has functional responsibility for the matters discussed in the letter, that IRS agreed with our basic findings.

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We are sending copies of this letter to the Committee's Ranking Minority Member, the Secretary of the Treasury, the Commissioner of Internal Revenue, and other interested

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parties. We will also make copies available to others on request. If you or your staff have any questions about the information in this letter, please contact me at (202) 512-9110 or David Attianese of my staff at (202) 512-9029.

Sincerely yours,



Lynda D. Willis
Director, Tax Policy and
Administration Issues

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