ADMINISTRATION OF THE FIRST–TIME HOMEBUYER TAX CREDIT

HEARING

BEFORE THE

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

ONE HUNDRED ELEVENTH CONGRESS

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THURSDAY, OCTOBER 22, 2009

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON OVERSIGHT,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:03 a.m. in 1100 Longworth House Office Building, the Honorable John Lewis (Chairman of the Subcommittee) presiding.

[The advisory of the hearing follows:]

HEARING ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

Lewis Announces Hearing on Administration of the First-Time Homebuyer Tax Credit

October 22, 2009

House Ways and Means Oversight Subcommittee Chairman John Lewis (D–GA) today announced that the Subcommittee on Oversight will hold a hearing on administration of the first-time homebuyer tax credit. **The hearing will take place on Thursday, October 22, 2009, at 10:00 a.m., in the main Committee hearing room, 1100 Longworth House Office Building**.

In view of the limited time available to hear witnesses, oral testimony at this hearing will be from invited witnesses only. Any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Subcommittee and for inclusion in the printed record of the hearing.

BACKGROUND:

In 2008, the "Housing and Economic Recovery Act of 2008" (Public Law 110–289) established a first-time homebuyer tax credit for low- and moderate-income taxpayers of up to $7,500. The tax credit applies to homes purchased after April 8, 2008, and before July 1, 2009. The credit must be repaid over a 15-year period, and repayment is accelerated if the home is sold within such period.

In 2009, the "American Recovery and Reinvestment Act of 2009" (Public Law 111–5) extended and expanded the 2008 first-time homebuyer tax credit for homes purchased between January 1, 2009, and December 1, 2009. The Act increased the maximum tax credit to $8,000. It also waived the repayment requirement unless the home ceases to be the taxpayer's principal residence within a 36-month period following purchase.

The first-time homebuyer credit is fully refundable, which means that the credit will be paid out to eligible taxpayers even if they have no tax liability or the credit exceeds the amount of tax due. For homes purchased in 2008, the credit may be claimed on the 2008 income tax return. For homes purchased in 2009, the credit may be claimed on the 2008 income tax return (original or amended) or the 2009 income tax return.

On July 29, 2009, the Internal Revenue Service (IRS) announced its first successful prosecution related to fraud involving the first-time homebuyer credit and warned taxpayers to beware of schemes. As of September 30, 2009, the IRS has identified 167 criminal schemes involving the credit and opened nearly 107,000 civil examinations involving the credit.

In announcing the hearing, Chairman Lewis said, **"I am pleased that more than one million taxpayers claimed the first-time homebuyer credit. However, I am concerned about recent reports that there have been fraudulent schemes involving the credit. This hearing will allow the Subcommittee to hear what, if any, additional steps should be taken to allow the IRS to strike a balance between issuing timely refunds of the homebuyer tax credit and protecting federal revenue."**

FOCUS OF THE HEARING:

The focus of the hearing is to review the IRS's administration of the first-time homebuyer tax credit. The Subcommittee will examine recent allegations of fraud involving the tax credit and consider opportunities to enhance administration during the 2010 filing season.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Please Note: Any person(s) and/or organization(s) wishing to submit for the hearing record must follow the appropriate link on the hearing page of the Committee website and complete the informational forms. From the Committee homepage, http://democrats.waysandmeans.house.gov, select *"Committee Hearings."* Select the hearing for which you would like to submit, and click on the link entitled, *"Click here to provide a submission for the record."* Once you have followed the online instructions, complete all informational forms and click "submit" on the final page. ***ATTACH*** your submission as a Word or WordPerfect document, in compliance with the formatting requirements listed below, by close of business **November 5, 2009.** Finally, please note that due to the change in House mail policy, the U.S. Capitol Police will refuse sealed-package deliveries to all House Office Buildings. For questions, or if you encounter technical problems, please call (202) 225–1721.

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The Committee relies on electronic submissions for printing the official hearing record. As always, submissions will be included in the record according to the discretion of the Committee. The Committee will not alter the content of your submission, but we reserve the right to format it according to our guidelines. Any submission provided to the Committee by a witness, any supplementary materials submitted for the printed record, and any written comments in response to a request for written comments must conform to the guidelines listed below. Any submission or supplementary item not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All submissions and supplementary materials must be provided in Word or WordPerfect format and MUST NOT exceed a total of 10 pages, including attachments. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. All submissions must include a list of all clients, persons, and/or organizations on whose behalf the witness appears. A supplemental sheet must accompany each submission listing the name, company, address, telephone, and fax numbers of each witness.Q04

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Chairman LEWIS. Good morning. The hearing is now called to order. Today's hearing is on the first-time homebuyer credit.

Today the Subcommittee will examine the first-time homebuyer credit. We need to answer two basic questions. Are people claiming the credit who should not and what can be done to stop the abuse.

The tax credit was created to stimulate the economy and home sales. It was estimated that at least 2.2 million households would claim about $18 billion of tax credits. To date, about 1.4 million households have claimed nearly $10 billion. The majority of these households, 60 percent of them, have income below $50,000.

To ensure the credit achieved its goals, the Internal Revenue Service developed a program to timely process returns and issue refunds for those claiming the credit. I salute this effort.

I am mindful, however, that this quick response came at a cost. The Service processed over one million returns claiming the credit before new fraud filters were in place. The result so far is that more than 100,000 exams have been opened involving the credit.

We will hear today that taxpayers claiming the credit include those who already owned a home, who had not yet bought a home, and who are children, some as young as four years old.

There are possibly hundreds of millions of dollars that have been paid to taxpayers who are not entitled to the credit. We want to and we need to stop this fraud and abuse. I look forward to the recommendations of our witnesses.

At this time, I would like to take a moment to thank the Deputy Commissioner, Linda Stiff, previously Acting Commissioner, for her outstanding and great service as a public official.

I understand that you plan to retire in December after 30 great years with the Service, and this is your last appearance before the Subcommittee.

We have enjoyed working with you over the years and your retirement will be a great loss, not just to the Committee, the Subcommittee, the Full Committee, to the Congress and to the nation. It goes without saying that you will be deeply missed. We wish you the very, very best in whatever you decide to do in the days, weeks, months and years to come.

Thank you for your service.

I am pleased to recognize the distinguished Ranking Member, Dr. Boustany, for his opening statement.

Mr. BOUSTANY. Thank you, Mr. Chairman. Thank you for yielding time. I want to thank you for holding this very important hearing.

When the Ways and Means Committee and the Tax Code are used for purposes beyond raising the revenues necessary to fund the Federal Government, for instance, to pursue social and economic policy goals, the members of this Subcommittee have a very important responsibility to conduct oversight of those tax provisions just as the Appropriations Committee in the House conducts oversight programs it funds to ensure that precious resources are being used effectively and honestly.

We are holding this hearing today to review the administration of the first-time homebuyer tax credit, examine allegations of fraud in claiming this refundable credit, and consider possible legislative changes to the credit.

The credit expires at the end of next month and a debate is heating up here in Congress over whether we should extend it, for how long, and with what modifications.

Determining whether or not we should extend the credit is not the purpose of this hearing today. Every time Congress creates a new refundable credit, meaning that individuals get a check from the Government, whether or not they have actual tax liability, the incentive for fraud is magnified, as we have seen for example with a high percentage of erroneous claims for the earned income tax credit and with recent videos showing ACORN officials advising people on how to fraudulently claim refundable child credits.

Therefore, this Subcommittee has a responsibility to figure out how we can minimize the opportunities for fraud and to be good stewards of the taxpayers' money.

If Congress decides to extend the home buyer tax credit, both Chairman Lewis and I believe Congress should consider reasonable proposals to reduce fraud and improve the IRS' ability to administer this credit.

In addition, given the worsening fiscal crisis our Government faces, I believe any extension of the home buyer tax credit should be paid for by reducing wasteful spending elsewhere in the budget, such as perhaps canceling ineffective stimulus fundings that have not yet been spent.

Finally, I want to share the same sentiments expressed by Chairman Lewis earlier regarding your service to our country, Ms. Stiff. Thank you very much. Thirty years of dedicated service to the American people is something that is quite remarkable, and we are thankful for that service.

Congratulations on your well deserved retirement. Best of luck in your future endeavors. I look forward to hearing your final thoughts here today as well as the thoughts of our other witnesses.

With that, Mr. Chairman, I yield back.

Chairman LEWIS. Thank you very much, Dr. Boustany, for your statement.

Now we will hear from our witnesses. I ask that you limit your testimony to five minutes. Without objection, your entire statement will be included in the record. I thank each of you for being here today.

It is my pleasure to introduce the Inspector General for Tax Administration, the Honorable Russell George. This is your first appearance before the Subcommittee and we welcome you.

STATEMENT OF J. RUSSELL GEORGE, TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Mr. GEORGE. Thank you, Mr. Chairman. Chairman Lewis, Dr. Boustany, Members of the Subcommittee, thank you for the opportunity to appear before you today to discuss the subject of the Internal Revenue Service's administration of the first-time homebuyer credit.

Based on the administration of the credit to date, I am very concerned about the IRS' ability to effectively administer the credits that are claimed before the December 1 deadline, let alone any credits that may be claimed within future extended deadlines.

The original credit was enacted in July of 2008, and my office provided our first memorandum to the IRS with recommendations on administering the credit on November 25, 2008, which was before the start of the 2009 filing season.

Despite that effort, several key controls to ensure the accuracy of claims for the credit have still not been designed or implemented.

The President has called on Federal agencies to ensure that Recovery Act funds are used for authorized purposes and that every step is taken to prevent instances of fraud, waste, error and abuse.

I am very concerned by the findings of our audit, given the stakes that are involved.

The law requires that to claim a credit, a home must first be purchased. However, we identified more than 19,300 electronically filed 2008 tax returns on which taxpayers claimed the home buyer credit for a home which had not yet been purchased, but alleged would be in the future.

We alerted the IRS of the need to validate claims for the credit in the November 2008 memorandum. However, the IRS disagreed with our recommendations.

Had the IRS timely implemented our suggestions to both capture and use the purchase date information from the forms taxpayers submit in order to claim the credit, these claims would not have been paid.

The amount of the credits inappropriately claimed in this instance totaled more than $139 million. We have yet to determine the number of paper returns with similar claims.

To its credit, the IRS has now implemented filters to reject claims with future purchase dates.

IRS management, however, indicated that they had not decided whether to go back and review or correct the more than 19,300 electronically filed returns that were processed before the filters were put in place or to identify how many paper filed returns with future purchase dates were similarly processed.

We found that the taxpayers who had indications of prior home ownership within the preceding three years were claiming the credit. These indicators included deduction 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. The deduction should not automatically disqualify the taxpayers from receiving the credit. However, we believe these claims were not scrutinized by the IRS.

The IRS reported that as of May 17, 2009, it had initiated the use of filters to identify such taxpayers for examination. Unfortunately, more than 70,000 questionable claims totaling almost half a billion dollars were processed by the IRS prior to the initiation of its examination filters.

We reviewed a random sample of these taxpayers. None of the accounts had received scrutiny from the IRS relative to their claims for the credit.

In addition, we identified more than 580 taxpayers younger than 18 who claimed almost $4 million in first-time homebuyer credits, the youngest of which were taxpayers who were four years of age.

Contract law generally exempts children under the age of 18 from being bound by the terms of a contract. It is highly unlikely that these taxpayers would have entered into arm's length transactions for the purchase of a home.

We identified more than 3,200 taxpayers claiming the credit totaling over $20.8 million on tax returns filed with individual taxpayer identification numbers of ITINs. An ITIN does not indicate that an individual is authorized to live or work in the United States.

The Recovery Act specifically denies home buyer credit to individuals who are non-resident aliens.

We also determined that most of the approximately 48,500 taxpayers who purchased a home in 2009 but claimed a credit of $7,500 even though they may be entitled to a credit of $8,000, 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 an indicator that the IRS will use to distinguish between taxpayers who must repay the credit over 15 years and taxpayers who will not be required to do so unless they sell their homes within 36 months.

Unless the IRS properly codes these accounts, these taxpayers may eventually be subject to IRS collection procedures.

Finally, Mr. Chairman, it is also very troubling that my auditors discovered that among those who apparently wrongly claimed the credit are a number of Internal Revenue Service employees. These cases have been referred to my Office of Investigations for review.

Mr. Chairman, Members of the Subcommittee, this concludes my oral statement. I would be pleased to answer any questions at the appropriate time.

[The prepared statement of J. Russell George follows:]

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
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

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

[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

[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.tigta.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.

Appendix I

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. 11880 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 [illegible] | 7. Loan Number [illegible] | 8. Mortgage Insurance Case Number [illegible]

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 [illegible] | E. Name & Address of Seller [illegible] | F. Name & Address of Lender [illegible]

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 mandatory.

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 Borrower's 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)		

Chairman LEWIS. Thank you very much, Mr. Inspector General.

It is my pleasure to call on the Deputy Commissioner, Linda Stiff.

STATEMENT OF LINDA STIFF, DEPUTY COMMISSIONER FOR SERVICES AND ENFORCEMENT, INTERNAL REVENUE SERVICE

Ms. STIFF. Chairman Lewis, Ranking Member Boustany, and Members of the Subcommittee on Oversight, thank you for this opportunity to testify on the IRS' efforts to effectively administer the American Recovery and Reinvestment Act's expanded first-time homebuyer credit.

The Service moved aggressively to implement this important program as soon as it was enacted by Congress and signed by the President.

There has been a strong response, as previously noted, to the program. Between January 2009 and September 2009, we have processed claims for more than 1.5 million individuals or families who have purchased homes.

In administering this program, the IRS has undertaken significant outreach to ensure that taxpayers are aware of the benefit. We developed new forms and instructions to allow taxpayers to file the claim, and we instituted significant compliance programs to ensure the validity of the claims filed.

As with any tax credit, the IRS must run a balanced program aimed at delivering the benefits that the legislation intended, while assuring that appropriate controls are in place to minimize errors and fraud.

The genesis of the credit was the Housing and Economic Recovery Act of 2008. Under that Act, taxpayers who purchased a principal residence after April 2008 and before July 2009 were allowed to claim the credit equal to ten percent of the purchase price not to exceed $7,500.

It also was required that taxpayers claiming that credit paid it back over a 15 year period beginning two years after the credit was claimed.

With the February passage of the ARRA credit, the amount was increased to $8,000 and extended to purchases completed on or after January 2009 and before this December.

Unlike the credit provided for in the 2008 Act, there is no repayment requirement if they retain the residence for three years.

Taxpayers seeking to claim the ARRA credit may do so on either their 2008 or 2009 tax returns.

The IRS was therefore faced with the administrative challenges of implementing two first-time homebuyer credit provisions during 2009. In response, we developed robust outreach and compliance strategies.

Through a series of expansive outreach efforts, the IRS worked to make sure that taxpayers were aware of the expanded credit. These efforts included numerous media interviews, press events, pod casts, public service announcements, nationwide tax forums, a national marketing campaign, expanded use of our web site and working with business stakeholders and our partners in the tax community.

Additionally, the IRS conducted extensive education and outreach activities with the return preparer and practitioner community. We sought to ensure that these individuals understood the eligibility requirements and endeavored to minimize inaccurate claims.

The IRS recognizes that there is the potential for both fraud and errors whenever a new refundable tax credit like the first-time homebuyer credit is enacted. As we began implementing this credit in the days after the Recovery Act legislation was passed, we identified different types of potential errors or fraudulent claims and matched our compliance program to those abuses.

We are and we will continue to vigorously pursue those who file fraudulent claims for the credit. It is important to put the administration of this credit in overall context of the tax filing process. The expanded credit was made available to taxpayers beginning in February, right in the middle of the filing season, at which time the IRS is processing approximately 140 million individual tax returns.

In addition to developing a form to collect the information pertinent, the IRS took steps to ensure the accuracy of claims. This included compliance checks to identify and select for audit the high risk claims and criminal investigations of possible fraudulent activities.

As with any other compliance program, the IRS is continuously refining the steps it takes to detect ineligible filers. The IRS has already identified more than 160 potential schemes resulting in scores of ongoing criminal investigations. We have selected more than 100,000 returns for audit.

The first-time homebuyer credit has helped more than a million American families purchase homes. We cannot let fraudulent activity undermine a program that has benefitted so many.

Mr. Chairman, the IRS administered the statute as written in a responsible way to meet the legislative intent of stimulating the economy quickly and providing first-time homebuyer's with the credit promptly.

We appreciate and we welcome the independent feedback that we have received from a number of our stakeholders, including my colleagues from TIGTA and GAO.

Thank you for the opportunity to testify. I will be happy to respond to any questions, and thank you for your acknowledgement and kind words as I approach retirement.

[The prepared statement of Linda Stiff follows:]

Statement of Linda E. Stiff,
Deputy Commissioner for Services and Enforcement, Internal Revenue Service

On the Administration of the First-Time Homebuyer Tax Credit

Before the Subcommittee on Oversight of the
House Committee on Ways and Means

October 22, 2009

Chairman Lewis, Ranking Member Boustany and Members of the Subcommittee on Oversight, thank you for this opportunity to testify on the IRS' efforts to effectively administer the American Recovery and Reinvestment Act's expanded first-time homebuyer credit (FTHBC or credit).

The IRS moved aggressively to implement this important program as soon as it was enacted by Congress and signed by the President. There has been a strong response to the program. Indeed, between January 2009 and September 2009, I am proud that we have processed claims from more than 1.5 million individuals or families who have purchased homes.

In administering the FTHBC program, the IRS has undertaken significant outreach to ensure that taxpayers are aware of the benefit, developed new forms and instructions to allow taxpayers to file the claim, and instituted significant compliance programs to ensure that those claims are valid. As with any tax credit, the IRS must run a balanced program aimed at delivering the benefits that the legislation provides, while ensuring that appropriate controls are in place to minimize errors and fraud.

BACKGROUND

The genesis of the FTHBC is the Housing and Economic Recovery Act of 2008 (HERA), which was signed into law in July 2008. Under the 2008 Act, taxpayers who purchased a principal residence after April 8, 2008, and before July 1, 2009, are allowed to claim a credit equal to 10 percent of the purchase price of the home, limited to $7,500. This credit served as an interest-free loan to taxpayers that must be paid back over a 15-year period beginning two years after the credit is claimed.

With the February passage of the American Recovery and Reinvestment Act of 2009 (ARRA), the maximum credit was increased to $8,000 and extended to include purchases completed on or after January 1, 2009, and before December 1, 2009. For homebuyers qualifying under the ARRA provision for 2009 purchases, unlike the credit provided for by the 2008 Act, there is no repayment requirement for qualifying purchases if they retain the residence for three years. Taxpayers seeking to claim this credit may do so on either their tax year 2008 or 2009 individual income tax returns.

The IRS was, therefore, faced with the administrative challenges of implementing two FTHBC provisions during 2009. In response, the IRS developed robust outreach and compliance strategies.

IRS' OUTREACH EFFORTS

Through a series of expansive outreach efforts, the IRS worked to make sure that taxpayers were aware of the expanded FTHBC.

Our efforts included numerous media interviews, press events, podcasts, public service announcements, IRS Nationwide Tax Forums, a national marketing campaign, expanded use of our website and working with business stakeholders and our partners in the tax community, to name but a few. These efforts led to virtually countless news articles in English and Spanish detailing the FTHBC. As part of this effort, the IRS worked to publicize the program's details through a special section on IRS.gov and created YouTube videos in English, Spanish and American Sign Language. Through these efforts we not only reached individuals who claimed the credit, but we also talked with return preparers who assisted individuals claiming the credit. Moreover, we intend to send notices to taxpayers who claimed the $7,500 FTHBC but who may be entitled to the expanded $8,000 ARRA credit to encourage them to file an amended return to claim the additional benefit.

We also worked with stakeholders to develop and implement a collaborative plan. For example, the IRS entered into a partnership with the Department of Housing and Urban

Development's Department of Single Family Housing Planning and Development to educate homebuilders, mortgage lenders, banks and other industry organizations as well as advocacy groups, on the FTHBC requirements for their clients. The IRS has plans to participate with HUD on a number of phone forums the agency coordinates to share information with the housing industry.

The IRS conducted extensive education and outreach activities with the return preparer and practitioner community as well. The IRS sought to ensure that preparers and practitioners understood the FTHBC eligibility requirements and endeavored to minimize inaccurate FTHBC claims. For example, we distributed written materials through our e-news for Tax Professionals e-mail service.

IRS' COMPLIANCE EFFORTS

The IRS recognizes that there is potential for both fraud and errors whenever a new refundable tax credit like the FTHBC is enacted. As we began implementing this credit in the days after the Recovery Act legislation was passed, we also identified different types of potential erroneous or fraudulent claims, and matched our compliance program to those abuses. We will vigorously pursue those who filed fraudulent claims for the credit, and have already opened up scores of criminal investigations. We have selected thousands of returns for those claiming the credit for civil examination.

Administering the FTHBC poses challenges similar to those the IRS confronts with other refundable credits -- namely, it has a number of eligibility rules and the Federal government lacks third-party data sources which can be used to verify taxpayers' eligibility for the credit.

It is important to put the administration of the FTHBC in context of the overall tax filing process. The expanded credit available under the ARRA came in February – a time when the IRS processes tens of millions of tax returns filed during a peak month. In fact, during February 2009 alone, we received almost 44 million returns for processing. And the majority of the 1.5 million returns claiming the FTHBC, just over 1.1 million, were filed between January and May 2009. It was important that the IRS implement and administer the FTHBC in a way that did not disrupt the annual tax return filing process.

In response to HERA, the IRS developed Form 5405, First-Time Homebuyer Credit, for taxpayers to complete when calculating and claiming the first-time homebuyer credit. Taxpayers are required to: (1) provide the address of the home qualifying for the credit; (2) the date the qualifying home was purchased; and (3) the amount of the credit they are claiming. The IRS updated this form just after the ARRA was passed in February 2009. Taxpayers are required to attach this form to their individual income tax returns. The IRS considered requiring taxpayers to attach additional documentation, such as the HUD-1 Settlement Statement, to their tax returns. It is important to note that the statute did not grant the IRS the authority to disallow claims solely based on insufficient documentation

– an audit is required to disallow the claim. Additionally, requiring paper documentation up-front with the tax return would have caused all taxpayers claiming the credit to wait longer, in part because claims would need to be filed on paper. Therefore, within the mandate of the statute, the IRS took steps to implement a compliance plan through screening filters that would identify returns with potentially inappropriate claims.

In addition to developing a form which collects information pertinent to determining eligibility for the credit, the IRS took additional steps to ensure accuracy of the claims. Some of those steps include: (1) compliance checks to identify and select for audit the highest-risk FTHBC claims before refunding money; (2) post-refund audits of less problematic returns; and (3) criminal investigations of possibly fraudulent activities. As with any other compliance program, the IRS continuously refines the steps it takes to detect ineligible filers.

Soon after implementation, the IRS took steps to revise its return filters to identify egregious claims. It is important to note that these steps were being taken at the height of the IRS filing season, which is mid- to late February. As returns are being reviewed and additional issues identified, the IRS continues to revise its systems to allow it to identify erroneous claims. In early May, the IRS put in place additional filters that would continue to identify improper claims, such as indications of prior home ownership. Returns that were processed early in the filing season that were not subject to these additional filters have been run against the new filters and those returns will be reviewed for potential future examinations. Additionally, the IRS used a limited statutory authority (known as "math error" authority) to prevent simple mistakes in three situations: claims in excess of the maximum allowable credit; claims in excess of the allowable amounts for those taxpayers with adjusted gross income exceeding income limitations; and claims without the required Form 5405 attached.

Through these efforts, the IRS has been able to identify and investigate many potentially fraudulent schemes and erroneous claims. For example, we have seen a number of taxpayers claiming the FTHBC indicating a future purchase date for the home on returns filed with the IRS. We are reviewing these claims and contacting taxpayers in order to correct their accounts. As another example, our return filters have identified a number of situations in which taxpayers claiming the FTHBC had indications of prior home ownership within the previous three years. It is important to note that just because these claims are being flagged as potentially erroneous, these taxpayers may actually be entitled to the FTHBC. Until the IRS follows up with the taxpayer, it is not possible to make a conclusive determination. We will vigorously pursue those who filed fraudulent claims for this credit, but we also will seek to respect the rights of taxpayers who claim a credit to which they are lawfully entitled.

The IRS has already identified over 160 potential schemes resulting in scores of criminal investigations. We have also selected more than 100,000 returns claiming the FTHBC for examination. We anticipate reviewing the audit results to refine our filters even further. The FTHBC has helped over a million American families purchase homes, and we cannot let fraudulent activity undermine a program that has benefited so many.

CONCLUSION

Mr. Chairman, the IRS administered the statute as written in a responsible way to meet the legislative intent of stimulating the economy quickly and providing first-time homebuyers with the credit promptly.

We appreciate and welcome the independent feedback that we have received from a number of our stakeholders, including the GAO and TIGTA. It has helped us to focus on continuing to improve the administration of this credit.

Mr. Chairman, thank you again for this opportunity to testify on the IRS' efforts to effectively administer the first-time homebuyer credit and help in the economic recovery efforts. I will be happy to respond to any questions.

Chairman LEWIS. Madam Deputy Commissioner, thank you very much for your statement and thank you for being here. As I said and the Ranking Member said, this is your last appearance before this Committee. Again, we appreciate your work.

Now it is my pleasure to introduce Mr. Jim White, Director, Tax Issues, at the GAO. Thank you for being here, Mr. White.

STATEMENT OF JAMES R. WHITE, DIRECTOR, TAX ISSUES, GOVERNMENT ACCOUNTABILITY OFFICE

Mr. WHITE. Mr. Chairman and Members of the Subcommittee, I am pleased to be here to discuss how taxpayers have used the first-time homebuyer tax credit as well as the major implementation and compliance challenges faced by the IRS.

As you know, there are two versions of the credit. The 2008 credit was for $7,500 and must be repaid over 15 years in increments of $500. The 2009 credit is for $8,000 with no repayment. It was enacted in mid-February of this year and made retroactive to January 1.

We summarized taxpayers' use of the credit in my statement. Table one on page three shows that over 1.4 million taxpayers claimed either the 2008 or 2009 credit so far and that the amount claimed is almost $10 billion.

Table one also shows the number of claims for each year, but those numbers should be viewed with caution. One reason is that some of the 2008 claims will be re-coded as 2009 claims either because the 2009 credit was made retroactive or because of IRS coding errors.

Further, 2009 is not over and many taxpayers are not expected to claim the 2009 credit until they file their tax returns in 2010. We expect the 2009 numbers to change significantly.

Table two on page four shows the income level of people who claimed the credit. Based on claims to date, a clear majority, 59 percent of credit claimants had adjusted gross incomes of less than $50,000. Compared to all taxpayers, credit claimants were disproportionately in the income range from $25,000 to $100,000.

Because purchasing a home is such a major financial commitment, it is not surprising that people with incomes of less than $25,000 are under represented, those with incomes above $100,000 are under represented for a variety of reasons, including income caps on eligibility.

Appendix three on page 11 shows credit claims by state. There is considerable variation in state claim rates measured as claims per capita. For example, Nevada's claim rate, the highest, is three times higher than New York's.

Now I want to discuss implementation and enforcement. IRS had to balance quick implementation of the credit with enforcement. Despite having to implement many stimulus related tax law changes during the filing season, IRS quickly issued the new form for claiming the Credit Form 5405, communicated with taxpayers through a wide variety of media, and made necessary computer programming changes.

IRS does face significant challenges ensuring compliance with the credit's complex rules. To determine eligibility, IRS must among other things determine that taxpayers have not owned a house in the previous three years and verify the closing date of the purchase.

IRS must also enforce the 15-year payback provision for the 2008 credit, which is important because the amount to be repaid is on the order of $7 billion, and IRS must also enforce the recapture provisions of the 2009 credit.

One reason compliance is a challenge is that IRS did not require substantiation through supplemental documentation provided by taxpayers or third parties to validate the information on the 5405.

IRS officials said they do not have the ability to accept supplemental documentation from taxpayers electronically, so requiring such documentation could cause more paper filing.

Further, providing supplemental documentation would be burdensome. IRS has procedures to stop some credit fraud and detect some taxpayer mistakes so they can be corrected before refunds are issued. As a result of the pre-refund checks, IRS froze 110,000 refunds pending audits, identified 167 criminal schemes, and began 115 criminal investigations.

IRS is also conducting post-refund audits but they are done after refunds are issued, making it more difficult to recoup the money.

To reduce reliance on costly and burdensome audits, we suggested in a recent report that Congress consider providing IRS with additional legislative authority called Math Error authority, that allows IRS to correct obvious errors on tax returns without an audit.

IRS has such authority for some tax provisions but we identified two more related to the homebuyer credit where the authority could reduce the need for audits.

One is the 2008 payback provision which could be verified using tax return information. The other is the prohibition on claiming both the 2008 and 2009 credit, which could also be verified using tax return information.

It is too early to tell whether IRS' enforcement actions and the proposed new math error authorities will be sufficient. Because of the complexity of the credit and the multi-year compliance issues, continued oversight of IRS' enforcement effort is warranted.

Mr. Chairman, this concludes my statement. I would be happy to answer questions.

[The prepared statement of James R. White follows:]

United States Government Accountability Office

GAO

Testimony

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

For Release on Delivery
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FIRST-TIME HOMEBUYER TAX CREDIT

Taxpayers' Use of the Credit and Implementation and Compliance Challenges

Statement of James R. White, Director
Strategic Issues

GAO
Accountability • Integrity • Reliability

GAO-10-166T

Mr. Chairman and Members of the Subcommittee:

I appreciate this opportunity to comment on taxpayers' use of the First-time Homebuyer Credit (FTHBC) and the Internal Revenue Service's (IRS) implementation and compliance challenges.

As an important part of the recent economic stimulus efforts, Congress enacted the FTHBC to assist the struggling real estate market and encourage taxpayers to purchase their first home. The credit initially was enacted by the Housing and Economic Recovery Act of 2008 (Housing Act) and revised by the American Recovery and Reinvestment Act of 2009 (Recovery Act).[1] The 2008 FTHBC provided taxpayers a credit of up to $7,500 that must be paid back over 15 years. The Recovery Act increased the maximum credit for the 2009 FTHBC to $8,000, with no payback required unless the home ceases to be the taxpayer's principal residence within 3 years. This $8,000 credit is a refundable tax credit that is paid out even if there is no tax liability or the credit exceeds the amount of any tax due.

The 2009 FTHBC was enacted into law on February 17, 2009, but eligibility was made retroactive for homes purchased beginning January 1, 2009. See appendix I for a comparison of the 2008 and 2009 FTHBC.

My testimony today, based on on-going work, describes two issues:

- the extent to which taxpayers are using the FTHBC, including breakouts by state and income; and
- IRS's implementation and compliance challenges associated with both the 2008 and 2009 credits.

To describe the extent to which taxpayers are using the FTHBC, we obtained and analyzed data from IRS about the use of the FTHBC and reviewed IRS documents. We ensured these data were reliable by reviewing IRS's computer programs for capturing the data and discussing the computer programming and verification processes with IRS officials. While combined 2008 and 2009 data appear reliable, the data for each of the years do not. This is because some claims were filed by taxpayers for

[1] Pub. L. No. 110-289, 122 Stat. 2654 (2008) and Pub. L. No. 111-5, 123 Stat. 115 (2009). The 2008 FTHBC applies to purchases made between April 9, 2008 and June 30, 2009. The 2008 FTHBC was amended by the 2009 credit, which applies to purchases made between January 1, 2009 and November 30, 2009.

the 2008 credit who actually could have claimed the 2009 credit, and IRS did not flag the problem. In following up on 47,276 electronically filed returns that appeared not to have claimed the whole FTHBC, the Treasury Inspector General for Tax Administration (TIGTA) found that 93 percent, or 43,967, were not coded as a 2009 FTHBC even though the purchase had occurred in 2009. It is likely that the errors are a result of (1) taxpayers who purchased a house in 2009 prior to the passage of the Recovery Act and claimed the 2008 credit, when, in fact, they are eligible for the expanded benefits of the 2009 credit; and (2) IRS's not properly coding the purchase date as a 2009 FTHBC on some returns. IRS has plans to monitor instances where taxpayers claimed the 2008 instead of the 2009 credit. When those taxpayers do not file an amended return, IRS has plans to notify them as to their eligibility for the expanded benefits of the 2009 credit. According to IRS officials, IRS plans to correct the other errors when it begins enforcing the 2008 FTHBC payback provisions. At that time, IRS plans to verify the date of purchase and make any adjustments.

To describe IRS's implementation and compliance challenges, we reviewed IRS documents and interviewed IRS officials to identify the guidance, outreach, and programming changes instituted to implement the credit. For this objective, we used several approaches to identify compliance challenges. Primarily, we reviewed IRS documents—including a risk assessment questionnaire, mitigation plan, and program decision document—to determine the risks associated with the credit and IRS's plans for mitigating them, and we reviewed previous GAO reports. We also consulted ongoing TIGTA audits on the credit. In addition, we interviewed officials from the Department of the Treasury and IRS's Wage and Investment division.

We have been conducting performance audits on the 2009 filing season and on the tax provisions in the Recovery Act since January 2009, and June 2009, respectively, in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Over 1.4 Million Taxpayers Have Claimed about $10 Billion in FTHBC

According to preliminary data from IRS, as of August 22, 2009, over 1.4 million taxpayers have claimed the FTHBC for homes purchased in 2008 and 2009, as shown in table 1. This represents total foregone tax revenue of about $10 billion through August 22.

While the combined 2008 and 2009 data appear reliable, as we noted the data for each year may be subject to revision because some claims made by taxpayers for the 2008 credit could have been made for the 2009 credit. In addition, the figures for 2009 are incomplete for several reasons. First, the figures do not include some returns that have been received by IRS but not processed. Second, some taxpayers have already purchased a home but have not yet filed for the credit. Taxpayers can claim the 2009 FTHBC on their 2008 or 2009 tax return. Last, the 2009 FTHBC does not expire until December 1, 2009, so taxpayers still have time to purchase homes and qualify for the credit. The Joint Committee on Taxation estimates that a majority of claims will occur in 2010 when taxpayers file their 2009 tax returns.

With these caveats in mind, table 1 shows the 2008 and 2009 FTHBC claims. The 2008 credit numbers, while subject to revision as noted above, are likely to be of the correct order of magnitude. The 2009 numbers should be interpreted as interim and are likely to change substantially.

Table 1: Taxpayers Claiming the FTHBC in 2008 and 2009

	Taxpayers claiming homes purchased in 2008	Taxpayers claiming homes purchased in 2009	Total
Number of taxpayers claiming the FTHBC	1,041,361	385,193	**1,426,554**
Dollar amount of credit claimed (in billions)	$7.108	$2.89	**$9.998**

Source: IRS data.

Note: Data as of August 22, 2009.

Taxpayer Use of the FTHBC Varied by Income and State

Based on claims made to IRS as of August 22, 2009, 59 percent of taxpayers who claimed the FTHBC had an adjusted gross income (AGI) of less than $50,000, as shown in table 2. The FTHBC was disproportionately claimed by taxpayers in the $25,000 to $100,000 AGI range. About 74 percent of credit claimants were in this AGI range, as compared to 46 percent of all taxpayers who filed a tax return in 2007. The low percentage of taxpayers claiming the credit with over $100,000 AGI reflects, in part, the income cap, for the FTHBC. For example, for joint filers the credit phases out between $150,000 and $170,000 (see app. I).

Table 2: AGI of Taxpayers Who Claimed the FTHBC (2008 and 2009 Combined) Compared to the AGI of All Taxpayers Who Filed a Tax Return in 2007

	AGI Ranges						
	Zero or less[a]	$1 to $25,000	$25,001 to $50,000	$50,001 to $75,000	$75,001 to $100,000	Greater than $100,000	Total
Total number of FTHBC claims[b]	25,200	265,263	543,996	362,474	152,054	87,547	1,436,534
Percentage of total FTHBC claims	2	18	38	25	11	6	100
Percentage of total taxpayers filing a tax return in 2007[c]	1	40	24	14	8	13	100

Source: GAO analysis of IRS data.

Note: Percentages may not add due to rounding.

[a]Taxpayers in the zero or less AGI range may be purchasing a home using savings or have income that varies across years.

[b]Data as of August 22, 2009.

[c]The 2007 data were the most current available for comparison purposes.

Looking at credit claims for each year separately must be done with caution because of the data issues described earlier. Comparing the preliminary 2009 data to the 2008 data shows an increase in the use of the credit by taxpayers with an AGI under $50,000 and especially by taxpayers with AGI under $25,000. For example, 18 percent of taxpayers who claimed the 2008 credit had an AGI of less than $25,000 compared to 27 percent of taxpayers claiming the 2009 credit. See appendix II for more detail. It is not possible to know whether these patterns will change as more complete and accurate 2009 data become available.

There are also differences in FTHBC claim rates among the states, as shown in appendix III. The highest number of FTHBC claims per capita is in Nevada, which has about three times the number of claims per capita than New York and Hawaii. Appendix III also shows the aggregate dollars claimed in each state and per capita dollars claimed. There is a strong correlation between state ranking of claims per capita and dollars per capita.

IRS Faces Significant Implementation and Compliance Challenges Related to the FTHBC

IRS had to balance quick implementation of the FTHBC with enforcement of the laws' requirements. Although IRS routinely implements tax legislation, the 2008 and 2009 FTHBC pose significant implementation challenges because they occurred during the filing season and in conjunction with other multifaceted tax law changes. IRS quickly implemented the complex FTHBC legislation, allowing taxpayers to claim about $10 billion as of August 2009. For example, IRS

- issued a new form, the Form 5405—"First-Time Homebuyer Credit"—and new instructions for the Form 5405, and revised other related forms and instructions;
- communicated with taxpayers and tax return preparers through a variety of avenues, such as news releases, postings on irs.gov, podcasts, and YouTube videos; and
- made computer programming changes to enable processing for paper and electronically filed returns. For example, the 2009 credit required programming changes to accommodate the differences in the eligibility rules for the 2008 and 2009 credits.[7]

IRS faces significant challenges in determining if taxpayers are complying with the numerous conditions for the credit. For example, to determine eligibility, IRS must verify that taxpayers have not owned a house in the previous 3 years and verify the closing date on home purchases. Other challenges include enforcing the $500 per year payback provision in the 2008 credit. According to recent IRS data, up to $7 billion could be repaid to the federal treasury over the 15-year period of this provision.

One reason assuring compliance is a challenge is that IRS did not require substantiation, either by the taxpayer or from a third-party source, to validate the information on the Form 5405. For example, IRS decided that requiring taxpayers to attach supplemental documentation about a home sale to a tax return would be burdensome. Further, according to IRS officials, IRS does not have the ability to accept such documentation

[7]IRS made minimal computer programming changes directly pertaining to the 2009 FTHBC. Officials said changes were implemented as part of Recovery Act programming changes, which resulted in IRS having to shut down its computers one weekend during the middle of the filing season—a first for IRS in several officials' memories.

electronically, which could impede taxpayers' ability to file tax returns electronically.[3]

Initially, IRS put procedures in place to stop some FTHBC fraud and detect common mistakes so that returns could be sent back to taxpayers for amendment. The results of IRS's review of early FTHBC filings prompted IRS to implement new computer filters to further determine eligibility up front, prior to refund issuance. As a result of up-front pre-refund checks as of September 30, 2009, IRS had (1) frozen more than 110,000 refunds pending civil or criminal examinations, (2) identified 167 criminal schemes, and (3) begun 115 criminal investigations.

IRS is also conducting post-refund FTHBC audits, but such audits are labor intensive for IRS, burdensome for taxpayers, and conducted after refunds are issued, making it more difficult for IRS to recoup the money. These audits address not only eligibility issues, but also recapture and payback issues for the 2009 and 2008 credits, respectively.[4] Because of the complicated provisions governing the credits, IRS is still determining the extent to which enforcement will have to be done through post-refund audits versus pre-refund compliance checks.

To reduce IRS's reliance on costly and burdensome audits, in a recent report we suggested the Congress consider providing IRS with additional legislative authority known as math error authority (MEA).[5] MEA, which IRS has for some tax provisions, must be granted by statute for specified purposes. Using MEA, IRS identifies calculation errors and checks for obvious noncompliance, such as claims above income and credit limits. IRS corrects these errors during tax return processing, which avoids the need for audits. Specifically, we suggested that Congress consider giving IRS MEA to use tax return information to automatically verify taxpayers'

[3]One potential example of supplemental documentation would be a copy of the Housing and Urban Development (HUD) form, HUD-1, Settlement Statement, required to be provided by settlement agents to the borrower at the time of closing. The form provides the date and sale price, which could help determine eligibility for the credit. However, it does not include a Social Security number, which makes matching to tax returns a challenge and it would be burdensome for closing agents to provide to IRS.

[4]The 2009 tax credit has a recapture provision. If a house is resold within 3 years, the credit must be repaid, under certain conditions.

[5]GAO, *Tax Administration: Opportunities Exist for IRS to Enhance Taxpayer Service and Enforcement for the 2010 Filing Season*, GAO-09-1026 (Washington, D.C.: Sept. 23, 2009).

compliance with the 2008 FTHBC payback provision and ensure that taxpayers do not improperly claim the credit in multiple years.

It is too early to tell whether IRS's enforcement actions and the proposed new legal authorities will be enough to protect federal revenue. Because of the complexities and multi-year compliance issues associated with the credit, along with the potential for significant burden on taxpayers, continued oversight of IRS's enforcement efforts will be necessary.

Agency Comments

In commenting on a draft of this testimony, IRS stated that the statement is very fair, presents a balanced picture, and gives a good perspective of where the agency is in the overall compliance cycle. IRS also provided technical comments which we incorporated where appropriate.

Mr. Chairman, this concludes my prepared statement. I would be happy to respond to questions that you or other Members of the Subcommittee may have at this time.

Contacts and Acknowledgments

For further information regarding this testimony, please contact James R. White, Director, Strategic Issues, on (202) 512-9110 or whitej@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Individuals making key contributions to this testimony include Libby Mixon, Assistant Director; Joanna M. Stamatiades, Assistant Director; Sherwin D. Chapman; Andrea S. Clark; John P. Dell'Osso; Rachel Dunsmoor; Kirsten B. Lauber; Lawrence M. Korb; Natalie L. Maddox; Karen V. O'Conor; Neil A. Pinney; and Sabrina C. Streagle.

Appendix I: Requirements for the 2008 and 2009 First-time Homebuyer Credit (FTHBC)

The 2008 and 2009 FTHBC have complex requirements. Regarding the amount of the credit, taxpayers generally can claim the smaller of

- $7,500 for the 2008 credit and $8,000 for the 2009 credit, or
- 10 percent of the purchase price of the home.

Virtually all eligibility requirements for the 2008 and 2009 FTHBC are identical, as noted in table 3. However, there are three key differences, the primary one being the purchase date.

Table 3: Eligibility Requirements for the FTHBC

Eligibility requirements	2008 FTHBC	2009 FTHBC
Date of purchase must be between April 9, 2008 and June 30, 2009	x	
Date of purchase must be between January 1, 2009 and November 30, 2009		x
Home must be principal residence[a]	x	x
Taxpayer must have no prior homeownership within the past 3 years	x	x
Home cannot be a gift or inheritance	x	x
Home cannot be acquired from a relative	x	x
Home must be located in the United States	x	x
Single filers: Modified adjusted gross income (MAGI) must be less than $95,000[b] Between $75,000 and $95,000 the credit phases out.	x	x
Married filing jointly filers: MAGI must be less than $170,000 Between $150,000 and $170,000 the credit phases out.	x	x
Cannot claim the FTHBC in both 2008 and 2009	x	x
Taxpayer cannot be a non-resident alien	x	x
Taxpayer must not be or must not have been eligible to claim the District of Columbia homebuyer credit for any tax year	x	
Home financing cannot come from tax-exempt mortgage revenue bonds	x	

Source: GAO analysis of FTHBC information.

Note: The "x" indicates if the related eligibility requirement applies to FTHBC for homes purchased in 2008 or 2009.

[a]A principal residence is the main home a taxpayer lives in most of the time. It can be a house, houseboat, housetrailer, cooperative apartment, condominium, or other type of residence.

[b]MAGI is modified adjusted gross income (AGI), as figured on an income tax return, plus various amounts excluded from the income tax return, such as some types of foreign income that would have to be added to AGI to yield MAGI.

In addition to eligibility requirements, the 2008 credit has a 15-year payback provision, but the payback may be accelerated if the home is sold or is no longer the principal residence. In addition, payback is waived if certain conditions are met, such as when a taxpayer is deceased and not a joint filer.

The 2009 tax credit has a recapture provision. If a house is resold or ceases to be the primary residence of the taxpayer within 3 years, the credit must be repaid. However, the recapture provision is limited to the amount of gain on the sale, so a taxpayer could sell within 3 years and still not owe repayment. There are exceptions to the recapture provision in the case of death, divorce, and involuntary conversion. Bills are currently under consideration in the Congress that would waive the recapture provision for members of the Armed Services if they are required to move.

Appendix II: Number of 2008 and 2009 FTHBC Claims and Adjusted Gross Income (AGI) Ranges

Table 4: Number of 2008 FTHBC Claims Filed and AGI Ranges

	Zero or less	$1 to $25,000	$25,001 to $50,000	$50,001 to $75,000	$75,001 to $100,000	Greater than $100,000	Total
Number of 2008 FTHBC claims	12,021	174,026	393,039	269,676	121,844	70,755	1,041,361
Percentage of claims	1	17	38	26	12	7	100

Source: GAO analysis of IRS data.

Note: Percentages may not add due to rounding; data as of August 22, 2009.

Table 5: Number of 2009 FTHBC Claims Filed and AGI Ranges

	Zero or less	$1 to $25,000	$25,001 to $50,000	$50,001 to $75,000	$75,001 to $100,000	Greater than $100,000	Total
Number of 2009 FTHBC claims	13,179	91,257	150,957	82,796	30,210	16,792	385,190
Percentage of claims	3	24	39	21	8	4	100

Source: GAO analysis of IRS data.

Note: Percentages may not add due to rounding; data as of August 22, 2009.

Appendix III: State-level Data on FTHBC Claims

Table 6: State-level Claims for the FTHBC for 2008 and 2009 Compared with Census Population Data as of July 1, 2008, Sorted by Claims per Capita

Rank	State	Number of filers claiming FTHBC	Population	Claims per capita	Total dollars claimed	Dollars per capita
1	Nevada	20,177	2,600,167	0.00776	$146,370,293	$56
2	Utah	17,569	2,736,424	0.00642	$129,697,371	$47
3	Arizona	39,130	6,500,180	0.00597	$275,499,450	$42
4	Florida	105,865	18,328,340	0.00578	$770,496,882	$42
5	Tennessee	35,836	6,214,888	0.00577	$256,184,764	$41
6	Georgia	55,840	9,685,744	0.00577	$398,493,119	$41
7	Nebraska	10,149	1,783,432	0.00569	$70,893,504	$40
8	Idaho	8,525	1,523,816	0.00559	$61,971,426	$41
9	Minnesota	28,760	5,220,393	0.00551	$200,222,141	$38
10	Michigan	55,116	10,003,422	0.00551	$362,430,212	$36
11	Iowa	16,532	3,002,555	0.00551	$111,307,663	$37
12	Colorado	27,121	4,939,456	0.00549	$193,220,686	$39
13	Alabama	25,303	4,661,900	0.00543	$177,395,844	$38
14	Texas	131,472	24,326,974	0.00540	$932,461,606	$38
15	Oklahoma	19,554	3,642,361	0.00537	$133,377,012	$37
16	Wyoming	2,812	532,668	0.00528	$19,719,986	$37
17	Virginia	40,597	7,769,089	0.00523	$287,769,731	$37
18	Mississippi	15,142	2,938,618	0.00515	$104,257,573	$35
19	Arkansas	14,670	2,855,390	0.00514	$99,872,964	$35
20	Missouri	30,120	5,911,605	0.00510	$207,974,834	$35
21	Louisiana	21,781	4,410,796	0.00494	$150,314,446	$34
22	Kansas	13,836	2,802,134	0.00494	$94,205,713	$34
23	South Carolina	21,876	4,479,800	0.00488	$153,971,018	$34
24	North Carolina	44,785	9,222,414	0.00486	$320,122,059	$35
25	Indiana	30,834	6,376,792	0.00484	$209,073,724	$33
26	Alaska	3,153	686,293	0.00459	$21,767,374	$32
27	Kentucky	19,230	4,269,245	0.00450	$132,955,896	$31
28	Delaware	3,886	873,092	0.00445	$27,412,020	$31
29	Montana	4,272	967,440	0.00442	$29,631,226	$31
30	Wisconsin	24,695	5,627,967	0.00439	$171,136,305	$30
31	California	160,795	36,756,666	0.00437	$1,151,605,634	$31
32	Pennsylvania	53,521	12,448,279	0.00430	$366,475,016	$29
33	Ohio	48,776	11,485,910	0.00425	$326,460,385	$28
34	Maryland	23,831	5,633,597	0.00423	$166,204,408	$30

Rank	State	Number of filers claiming FTHBC	Population	Claims per capita	Total dollars claimed	Dollars per capita
35	North Dakota	2,699	641,481	0.00421	$18,139,186	$28
36	South Dakota	3,343	804,194	0.00416	$22,630,645	$28
37	Washington	26,604	6,549,224	0.00406	$189,408,939	$29
38	Illinois	51,794	12,901,563	0.00401	$357,438,259	$28
39	Rhode Island	4,190	1,050,788	0.00399	$29,762,911	$28
40	New Hampshire	5,145	1,315,809	0.00391	$35,402,421	$27
41	Massachusetts	25,090	6,497,967	0.00386	$172,308,588	$27
42	Maine	5,080	1,316,456	0.00386	$34,907,560	$27
43	Oregon	14,248	3,790,060	0.00376	$101,012,536	$27
44	New Mexico	7,262	1,984,356	0.00366	$51,382,080	$26
45	New Jersey	30,471	8,682,661	0.00351	$209,133,493	$24
46	Connecticut	12,223	3,501,252	0.00349	$84,964,985	$24
47	Vermont	2,100	621,270	0.00338	$14,183,146	$23
48	West Virginia	5,536	1,814,468	0.00305	$36,203,272	$20
49	New York	50,673	19,490,297	0.00260	$341,384,040	$18
50	Hawaii	3,207	1,288,198	0.00249	$22,391,318	$17
51	District of Columbia	1,383	591,833	0.00234	$9,480,535	$16

Source: GAO analysis of IRS and Census data.

Note: FTHBC data are for 2008 and 2009 claims as of August 22, 2009.

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Chairman LEWIS. Thank you very much, Mr. White, for your statement.

At this time, we will open the hearing for questions. I ask that each member follow the five minute rule. If the witnesses will respond with short answers, all members should have the opportunity to ask questions.

Mr. George, you mentioned that 600 children received a credit. Do you think it would help the administration of the credit if there was an age limit?

Mr. GEORGE. Yes, there is no question that would be helpful. Let me also add that there may be instances when someone under the age of 18 legitimately is purchasing a home, an emancipated youth, for example, but nonetheless, there is precedent for income levels or requirements in other refundable credit instances.

I believe the EITC has an income/age requirement for certain individuals seeking that credit.

Once again, sir, yes.

Chairman LEWIS. Mr. George, how would you deal with the case of a child four years old, maybe five, six, seven, eight, nine or ten? I do not think a child that young is going to be filing a form. Should not the guardians or the parents be held liable/responsible?

Mr. GEORGE. Again, without having completed our review, and obviously the IRS has not completed theirs yet, I cannot speak definitively, but there is no question that most indications are that the parent is attempting to bypass the income limitations for seeking the credit by attributing the home purchase to a minor.

Some form of action would seem appropriate in terms of the adult who actually signs on behalf of the child.

Chairman LEWIS. Mr. White, what is the most important tool we can give the IRS now to help with the credit?

Mr. WHITE. One thing that would help ensure compliance is the additional math error authority that I discussed. The advantage of this is it shifts at least some of the compliance efforts from post-refund auditing to pre-refund compliance checks. It is also less burdensome for the taxpayer.

Some errors can be identified as clear cut unambiguous errors and IRS can correct those without the need for back and forth correspondence with the taxpayer. IRS would correct the error and notify the taxpayer that the error has been corrected.

There are two cases we found where such math error authority, we think, would be useful to IRS, where they don't have the math error authority right now that are in my statement.

Chairman LEWIS. Thank you. Commissioner Stiff, I intend to introduce a bill to help with administration of this credit. Will any of the following help the IRS? Mr. White just mentioned math error authority. Would that help?

Ms. STIFF. Yes, sir. We specifically would like to have math error authority based on indications of prior year home ownership. Secondly, we would like a requirement that the HUD–1 document be attached with the filing of the return and that additionally, a failure to do so or an inaccurate or incomplete, that we would have math error authority to disallow it as we process the return.

Chairman LEWIS. What about adding an age limit?

Ms. STIFF. Absolutely.

Chairman LEWIS. What about requiring people to prove they purchased the home?

Ms. STIFF. Yes, sir. That goes back to what I was suggesting by asking them to include the HUD–1 or another legal settlement document that would allow us to math error it and catch it up front.

Chairman LEWIS. What about increasing the number of electronic returns?

Ms. STIFF. Yes, sir. That certainly facilitates our compliance efforts.

Chairman LEWIS. Thank you very much. Now I will turn to the Ranking Member, Mr. Boustany, for his questions.

Mr. BOUSTANY. Thank you, Mr. Chairman. Commissioner Stiff, your testimony concedes there is potential for both fraud and errors whenever a new refundable tax credit like the homebuyer tax credit is enacted.

I believe this is an acknowledgement that refundable tax credits pose a higher risk for fraud than other types of tax credits. Is that your understanding?

Ms. STIFF. Yes, sir. Based on experience with refundable credits, any time there is an opportunity to receive cash back, it tends to attract people that might have an intent to defraud the Government. Then you have another segment which is perhaps the largest where there is just simply inadvertent errors due to the complexity that Mr. White outlined in his testimony.

Mr. BOUSTANY. Thank you. The Chairman started mentioning some remedies and additional tools that you may need. I just want to get a clarification. Initially, IRS did not feel that the HUD–1 form was necessary or it was going to impose an additional paperwork burden?

Ms. STIFF. Let me clarify. We could have required the HUD–1 document, but it would not impact our compliance efforts because we did not have math error authority.

If there was something in question on that document, we would still have to go through the audit process that we are going through today. We created a form, the 5405, that asks taxpayers to provide some of that as the formal part of processing the tax return, and a failure to do that did allow us to math error on that basis.

Granted, that was not as robust, but we felt like it was a reasonable alternative to get some of that stopped before it ever went out the door.

Mr. BOUSTANY. You need additional statutory authority now for the math error authority?

Ms. STIFF. Right. If you get the form, we need the ability to disallow on that basis because without it, we find ourselves where we are today.

Mr. BOUSTANY. Finally, IRS is generally much more successful at identifying errors and fraud and so forth when there is third party reporting. I think the statistics are pretty clear on this.

Given that the homebuyer credit has imposed serious auditing difficulties, I want to explore some of the options with third party verification. I would invite the entire panel to comment on this.

How would you see this playing out? What types of statutory authority should we consider to help you with that tool of third party verification?

Ms. STIFF. I think my best recommendation is the one we just discussed, requiring the attachment of the HUD–1 document or an alternative legal settlement document, and then math error authority.

Mr. WHITE. We talked about math error authority but in terms of third parties, one alternative that at least is an option, I am not recommending this, but it is an option, is instead of having the HUD–1 submitted by the taxpayer, who in cases of fraud might be able to submit a phony HUD–1, to have it submitted by the settlement agent.

There is a tradeoff there because that would impose burden on settlement agents who would have to submit that form and IRS would have to develop a procedure for processing those.

Mr. BOUSTANY. Thank you. Mr. George.

Mr. GEORGE. I would simply note that we have discovered that third party reporting in the context of wages results in almost a 98-percent compliance rate. We strongly advocate that.

In this instance, whether or not you actually have a third party reporting the information, as long as you require the taxpayer to have the information, we believe it would serve as a deterrent on whether or not again they are ultimately required to submit it to the IRS, somewhat akin to charitable contributions when taxpayers are required to receive something in writing from the charities they donate to.

Mr. BOUSTANY. Is it the consensus of the panel that there should be some third party verification mechanism, just for clarification?

Mr. GEORGE. Let me answer only by saying the Secretary of the Treasury has given the tax policy authority within the Department to the Office of Tax Policy, but with that said, I think it would be helpful.

Mr. BOUSTANY. Thank you.

Mr. WHITE. I guess I would just repeat, we have not done an analysis of the tradeoffs there. There are some tradeoffs. It would be a burden imposed on closing agents. This would be something entirely new for them to have to submit a form to IRS.

Mr. BOUSTANY. Commissioner Stiff, do you want to add anything to that?

Ms. STIFF. Just to restate what I said before. I would neither promote involving the people closing the mortgages to do it so much as I would ask that taxpayers be required to provide the documentation with us because I believe that will get us a long way to where we all want to end up.

Mr. BOUSTANY. Thank you. I will yield back.

Chairman LEWIS. Now we turn to Mr. Pascrell for his questions.

Mr. PASCRELL. Thank you, Mr. Chairman. Thank you all for being here and your service to this nation.

We tried in February to deal with a growing problem, which seems to have subsided somewhat. Very concerned, and this is not what we are talking about today, but the foreclosures in this country are devastating. That, to me, would be a priority.

If I have to make priorities in a limited budget, it would seem to me that we want to keep people in their homes and then secondly, we would want to encourage people to buy new homes because of that ripple effect in the economy.

If I have to make a judgment, if I have to establish priorities, and that is what the Congress is all about—I was hoping we would talk about foreclosures today but this is the subject at hand.

I wanted to ask you a question, Ms. Stiff. Are you saying you could not do more to review these applications for credit mainly because of a manpower situation? You mentioned it started right in the tax season, I think you said February or March.

Or is it a statutory factor that is preventing you from going a step further? These are very disturbing things to all of us when we read about taxpayers' money, particularly in this atmosphere, going out the window and unretrievable to some degree.

What is the main problem? Manpower?

Ms. STIFF. Let me say it is a combination of things. It was that we were in the middle of the filing season. The credit was passed on February 17. Taxpayers were filing their tax returns. The next day, they could start filing the claims.

Secondly, it was the need to get appropriate compliance filters in place that would enable us in that real time window to begin to detect questionable returns.

Mr. PASCRELL. Did the Treasury, did the Administration alert you to the fact that this legislation, which was part of the February legislation, was going to be implemented?

What kind of discussions did you have with the Administration before this even happened?

Ms. STIFF. Let me say this. We generally do not enact or implement or reprogram our systems until we have legislation that is enacted because you are in the middle of a filing season, and our programming was designed for the credit that was passed the prior July.

It required two different programmings in place. We tried to make those decisions in a responsible way so that we are not poised for one thing and then it does not happen on this day and taxpayers are held up in the system.

The second thing is it would have required us to take—you had 1.1 million taxpayers that filed for this credit from February to May. You would have had to take every one of those out of the processing stream and make a contact with each and every one of those if you wanted to do that before they got their credit.

Mr. PASCRELL. What added measures are in place or about to be put in place to protect the taxpayers' money?

Ms. STIFF. Every one of the 1.5 million claims that have been filed are being reviewed through a set of filters and the high risk ones are being pursued as a part of the audit process.

For next year, we have that robust process in place as we go in for the taxpayers who are actually going to file the claim on their 2009 return as opposed to the 2008 return, and I think we are poised to administer that in a way that will enable us to catch more of it as it is going through in real time.

I think with the legislative tools that we have talked about earlier that will only enhance in strong measure our ability to do just that.

Mr. PASCRELL. Thank you. Mr. White, what grade would you give IRS in reference to this particular program? How would you grade them?

Mr. WHITE. I do not have a specific grade. As I said, IRS quickly implemented the credit and it was a challenging credit to implement. There were two versions of the credit, and they are both very complicated credits.

There are a lot of rules and a lot of exceptions to the rules. It wa a challenge to implement.

I think the strategy of trying to shift as much of the compliance checks to the pre-refund stage and doing that in an automated way is a good strategy because audits are labor intensive to do and they are burdensome on taxpayers.

Mr. PASCRELL. Do you consider—does the GAO look at the effectiveness of this program?

Mr. WHITE. We have not assessed the effectiveness of IRS' compliance efforts.

Mr. PASCRELL. Would you do that?

Mr. WHITE. We can do that; yes.

Mr. PASCRELL. I think it would be significant because we would like to know if we are spending our money in the right ways. We want to encourage first-time homebuyers. There is no question about it. We can do that successfully or we can do it unsuccessfully.

The IRS has to be tipped off by the Administration as to where we are going so they can establish this. We are flying by the seat of our pants. That is exactly what we are doing. That is why a lot of folks are taking advantage illegally of this program. That is why. It is not the IRS' problem. It is the Administration's problem.

Mr. Chairman, I would hope you will look into that.

Chairman LEWIS. Thank you very much. We all will look into it, not just the Chair. Thank you very much for your question.

We turn to Mr. Reichert for his questions.

Mr. REICHERT. Thank you, Mr. Chairman. First, I would like to go to Mr. George. You mentioned in your statement that you recommended a set of filters to the IRS which they refused to implement.

Could you just give me a short list of some of the filters?

Mr. GEORGE. One was an age filter. Even with that in place, would they have caught all of the examples that I cited in my testimony, the answer is no.

In addition to the age filter, we would have recommended that they look at—bear with me one second.

[Pause.]

Mr. GEORGE. Let me supply that, a list of the filters for the record, if I may, sir.

Mr. REICHERT. Great. Thank you.

[The information follows:]

Testimony By Georgia Aldridge, Ed.S., NCSP, Letter

Georgia Aldridge, Ed.S., NCSP, Letter

Dear Chairman Lewis,

As a 20-year resident of the ethnically diverse area of Southern Queens, New York, a School Psychologist by profession, a wife and mother, who until now could not afford to purchase a home due to the unreasonable cost of houses in this area (prices increased by the $50,000 per year at regular intervals in the past few years until the average cost of 2–3 bedroom capes was $350–$400K), and the related costs of a down payment, closing, searching,

who did not even hear of the poorly advertised Tax Credit until completing tax forms in March of this fiscal year 2009, and then as an educator could not begin to act on the possibility of purchase until July, when school is out, and then as a potential First Time Home Buyer on a shoe string budget with no real estate or legal connections, could not begin a search until considerable time was spent learning about the process,

who with pre-approvals, excellent credit rating, and qualified real estate agent finally in hand, began in earnest a search at the beginning of September, only to find that the available price range in nearby areas was often filled with sales that were "Short Sales" subject to lengthy bank approvals or foreclosures with the seller or his agent requiring particular kinds of mortgages and monies at offer, all requiring additional time and arrangements,

who in order to garner the down payment, must request a distribution from a retirement account that will "increase" the income level for that fiscal year,

therefore, who will no longer be able to consider purchasing a home, since under the current constraints of the First Time Home Buyers Tax Credit (2009) and under the general timetable and purchasing conditions found in this geographical area, the deadline of a November 31 Closing is not reachable, and since the Tax Credit would not be available to offset the higher taxes that would ensue because of the "increased" income, purchasing a home would again become unaffordable,

who has not received any individual benefits yet from any of the Economic Recovery Acts, by virtue of exclusion from Wall Street, only living in its shadow, or from the banking industry, only being subject to its apparent usury, and from any unfortunate lower socio-economic group, only serving such at work, and church, and in neighborhood, and of being Middle America in an Urban setting (yes, we do exist),

I am requesting the relevant Committees of Congress to consider another extension and modification of ARRA of 2009 "First Time Home Buyer's Tax Credit" through December 31, 2010 to allow the momentum toward the American Dream and economic stimulation to continue.

I propose, in order to reduce temptation to make fraudulent claims and to modulate the impact on the U.S. Government's Revenues, the tax credit *not* be refundable, and for it to appear as a "Tax Credit," not a "Payment" within the Income Tax structure. I am asking for you therefore to consider a higher income eligibility structure in order for the FTHB of all tax brackets to realize some relief from taxes. I am proposing that the total possible amount of 'pre-tax credit' be raised to the amount of the down payment up to $20,000. I am not asking the U.S. government for money-as some have; I am asking you for a tax break on the earnings my family has honestly made so that I can use that money to invest in America by purchasing a home in my own community.

I sincerely thank you for this opportunity to be heard.

Regards,

Mrs. Georgia R. Aldridge

Testimony By Jon R. Sias, Statement

Statement of Jon R. Sias

Thousands of borrowers who purchased under the 2008 program guidelines remain under the onus of repayment. Certain Committee text suggests the repayment dictated under 2008 guidelines were waived when the 2009 language and changes were adopted. Americans are certainly entitled to a clear delineation of this policy.

Nothing bespeaks the value of extending the FTBTC than the strong success of the "C4C" program. In both cases financial transactions are driven down to the local level where the exchange of dollars for services ripples along the entire economic tendon. As successful as the FTBTC is, it stands in the shadow of the full-stride success it could be.

Thousands of new buyer/borrowers would purchase first time homes, removing them from the large and growing glut of available inventory . . . if a portion of the tax credit were monetized in the form of a 3.5% grant to cover FHA minimum down payment guidelines.

The infrastructure to make this happen is already in place, however much of it was designed and implemented using a neighborhood specific outcome approach. Going forward, rather than targeting specific neighborhoods, the target must be local economies and the philosophic stronghold in the value of home ownership.

Mr. REICHERT. Commissioner Stiff, what is your date of retirement?

Ms. STIFF. November 30.

Mr. REICHERT. I have been in your position as the Sheriff in Seattle testifying to our County Council, and sometimes it is uncomfortable. Since you are retiring, we can ask pretty blunt questions and hope you might feel free to be as open as you can since you will be soon leaving.

What do you think the impact has been to the extent that say homebuyers and home builders in my district, they benefitted from this, and because of the fraud, to what extent do you believe this fraudulent use of tax credits are undermining the credit's goal of stabilizing the housing market?

Ms. STIFF. I cannot, I am not an economist. I cannot assess the impact. I know 1.5 million taxpayers and their families, as noted earlier, received the benefit of the credit.

I also want to add as a matter of record that these numbers that we have been throwing around as potentially questionable are not—a determination has not been made that those taxpayers are not eligible for that credit.

We found in our early audits in many instances they actually were eligible and what they had were other errors in the way they reported or how they reflected it on their return, so the tax might have been different, but their eligibility for the credit is sometimes not in question, despite having not passed a filter.

Mr. REICHERT. As an old cop, I do not know the financial terms for what you deal with, but it seems to me prevention really should be the focus. I disagree with Mr. Pascrell just a little bit in that I think it is an IRS problem.

I think it also is an Administration problem, and I think you need more resources. It is obvious to us you have kind of skirted that issue just a little bit.

When you look at 1.5 million claims that you have to process, 167 schemes and scams that you are trying to investigate, another 115 investigations that you are involved in, and you are not requiring the supplemental documentation up front to screen some of these things so you do not have to conduct investigations and uncover scams and schemes, to assign more personnel, it seems to me you need more resources, more personnel, or you need to develop a program that is able to allow these supplemental documents to be reviewed.

Ms. STIFF. I think your point goes to exactly what Chairman Lewis was proposing, that with the additional authorities, we will be able to front-end load a lot of our compliance and enforcement efforts, and additionally, I cannot resist the opportunity to pitch for the passage of the 2010 budget which will allow us to continue our efforts.

Mr. REICHERT. How many agents or investigators do you have assigned to 160 scams and schemes?

Ms. STIFF. I would have to get back to you with that number.

Mr. REICHERT. Can you estimate it for me? Mr. George, do you know the number?

Mr. GEORGE. I do not have that number. I just want to point out that to your question about filters, it is really common sense because one of the recommendations was that we simply have the IRS transcribe the information that they requested from taxpayers on the Form 5405 so that people could determine what it is that the taxpayers are reporting, and that was not being done.

Mr. REICHERT. You have experience with tax credit before, and this should be one that you should have been able to implement using some of your past practices and policies and then implement, of course, new ones to accommodate this specific issue.

How much more manpower/personnel do you need? How many more people do you need? This is an unfunded mandate, as far as I see it.

Ms. STIFF. I believe that with the legislative tools that we have requested and with the passage of the 2010 budget, I believe we are poised to execute this with that.

Mr. REICHERT. You believe the next Commissioner coming in is going to be just fine with the situation the way it exists now?

Ms. STIFF. I think with the assistance of the new tools we have requested we are going to be positioned to responsibly deal with this on the front-end. I just need to say this again, the fact that it was not stopped on the front-end does not mean we are not addressing each and every one of those——

Mr. REICHERT. I have one last question. It is very troubling to hear IRS agents actually have applied for these credits illegally. How do you intend to hold those people accountable?

Ms. STIFF. We have an employee tax compliance program that we use year in and year out, day in and day out. The fact is there has been indications——

Mr. REICHERT. If there is wrongdoing discovered, what happens?

Ms. STIFF. It will depend upon the facts and circumstances specific to each case, just as it would with any other taxpayer.

Mr. REICHERT. Do you know the numbers of your members that are involved in this?

Ms. STIFF. I do not. I think that the numbers Mr. George referred to earlier were numbers where there were questionable things on the face of the return. I do not believe there have been any numbers established that something was done incorrectly. Those are ongoing audits, the same as what we are talking about with the other 100,000.

Mr. REICHERT. Thank you, Mr. Chairman.

Chairman LEWIS. Thank you. Now we turn to Mr. Etheridge for his questions.

Mr. ETHERIDGE. Thank you, Mr. Chairman. Thank you, Chairman Lewis. Let me thank each of our panelists here this morning for testifying.

I do not need to remind you the recession has hit all sectors of our economy but really the housing industry has been hit especially hard and their troubles continue.

As a result, the first-time homebuyers tax credit really has helped to some extent lessen that sting in real estate companies, for home builders and the supply chain. We should not forget that this helps millions of people, consumers, purchase a home for the first time.

Granted, we are beginning to learn that any time you put something out there, there are more crooks than cops. We just have to work to make it happen.

As Congress considers extending or expanding this tax credit, we should make sure that this valuable economic tool is not only used wisely but that fraud and abuse are stamped out. That hurts every program and it really hurts a program that is meant to help people.

Mr. White, you suggested that there are simple tools that the IRS could use to stop errors and fraud. Would it really be as simple as checking filings against the previous years' returns?

How much delay would this add to the processing of returns, if any? How does the so-called math error authority compare to the screening Mr. George described earlier? In that, can you give us examples of how that would help?

Mr. WHITE. The math error authority that I was discussing applies to specific cases. It clearly does not prevent all fraud. There still would be a need for some post-refund check, but to the extent that the checking can be done in an automated way before a refund is issued, IRS does those checks very quickly as part of their normal processing of tax returns. They do not slow down refunds. It is all computerized done in an automated fashion.

In addition to being low cost for IRS, it is also much less burdensome for the taxpayer. The IRS does not have to correspond with taxpayers.

Mr. ETHERIDGE. It is all done in-house?

Mr. WHITE. It is done in-house. Taxpayers do not have to struggle trying to figure out what the notice means that they get from IRS.

I think in general, there is some agreement here about the advantage of these kinds of pre-refund automated checks to the extent they can be used and reduce the need for audits done. After the refund goes out the door, those audits are labor intensive and involve interaction with the taxpayer.

Mr. ETHERIDGE. If I am following you correctly, what you are suggesting is sort of like when you have health care. Do a little preventive on the front side to save a major cost on the back side. You can go through the audit process, you have a lot of manpower, you have a lot of expense that you could have prevented had you done the pre-audit before.

Mr. WHITE. Yes.

Mr. ETHERIDGE. You are saying number one, that should not slow it down?

Mr. WHITE. It does not slow it down right now. IRS has this system in place now and it is all automated and invisible to the taxpayer and happens very quickly.

Mr. ETHERIDGE. Ms. Stiff, let me ask you two questions. Is it your opinion that we could process this if we were to do it on the front side, we would then allay the fraud and abuse on the back side? I am not asking do we need people to follow up, obviously. Can we reduce the errors substantially, which is where we are right now?

Ms. STIFF. I think with the proposed legislative tools that we talked about, which includes a requirement that if you are under 18, that we will automatically preclude it coming in the door. You can come in and make a case later.

If you have to attach the HUD–1 or a legal settlement document and a failure to do so, we will preclude you in the systemic way that Mr. White described, and lastly, we screen you out and do it systemically if there is prior indications of home ownership. Again, not precluding you from making a case, but stopping it before it goes.

Mr. ETHERIDGE. That would mean you would have to come in and make a case if you are an exception.

Ms. STIFF. Right.

Mr. ETHERIDGE. Let me follow that up with another question. How successful do you think your outreach efforts were? It was estimated about 2.2 million would be used and 1.5 million so far to date.

What do you think can be done better to make sure that people who could benefit, number one, are aware, and number two, coming back to my first question, to reduce any fraud and abuse in that process?

All of us lose when we are trying to do good and there are plenty of people out there figuring out how to take advantage of the system.

Ms. STIFF. We and others around the country as a result of their own vested interests, there was expansive outreach and education for taxpayers, for consumers, regarding the credit.

I think that speaks to the fact that we have had 1.5 million, which I think actually exceeded what was originally estimated to occur this year, so I think we are going to have to continue that education campaign going into this next filing season because the Act provides eligibility on the returns that are filed next year.

I think the other thing with the passage of the new legislative tools that there will be an education and outreach campaign with preparers and taxpayers as to what is going to be required and what they are going to need to do to be able to meet the eligibility requirements.

I think as a result of our criminal investigative activities that is also going to serve both as an education and deterrent. I do not know if you saw yesterday, we had a sentencing of 30 months for a preparer that was involved in bad acts regarding the credit. I think those things start to give momentum and create awareness.

Mr. ETHERIDGE. I could not agree more. Publicity on that always helps. I can assure you some people are getting the word out. I was home this weekend. A car passed me with a great big sign on the side and one on the back, and it says “Ask me how to get $8,000.”

Mr. Chairman, it did not take me long to realize it was a real estate agent. He did a pretty good job of advertising. He or she. I am not sure which it was.

Thank you, Mr. Chairman. I yield back.

Chairman LEWIS. Thank you very much. I just want to remind members we are operating on the five minutes rule, trying to get an opportunity for all the members to have an opportunity to ask questions.

Now I turn to Mr. Davis for his questioning.

Mr. DAVIS of Illinois. Thank you very much, Mr. Chairman. Let me thank all three of the witnesses.

Inspector General George, let me go to you first and go back to the point that there were suggestions and recommendations and concerns made by your office to the IRS that went unheeded, and I guess in some instances, perhaps even disagreed with.

Do you have any indication of why there might not have been the follow up or the follow through if the advice was not taken, why it was not taken?

Mr. GEORGE. You know, while I am going to most likely yield to Linda to give a definitive response, I have to say at the outset that the IRS has been very responsive to most recommendations. I would say over 98 to 99 percent of the audit recommendations that we provided to them have been agreed with and implemented in one form or another.

In this instance, again, Linda can speak for herself, they have to do a cost/benefit analysis at times. While I understand on one level why they need to make those determinations, given the fiduciary responsibility that they have to the American people, to the American taxpayer, there are times when whether or not it might be expensive to implement a particular procedure, they have an obligation to do so, and especially when the stakes are as high as they are in this instance with billions of dollars at stake, we believe every action that could have been taken should have been taken.

Mr. DAVIS of Illinois. Let me just ask you, Commissioner Stiff, what your reaction is to that question relative to taking the advice.

Ms. STIFF. I will echo what Mr. George said here. We take very seriously any recommendation that TIGTA offers us regarding any program.

In this instance, and I will say I have to leave it to others to judge, we evaluated all the options available to us, we were in the middle of a filing season. If we had required the HUD–1 documentation, which is the point of disagreement, we would not have been able to not process the claim or not allow the claim.

We would have had to engage in an audit in each and every one of those situations the same as we are today.

Had we been loaded with more information going into that, we made a decision that since we did not have statutory math error authority to use that information to make a decision whether to process it or not, that we created a schedule and got some of that information there and were able to use the failure to comply with that as a screen for filtering returns.

Lastly, requiring the HUD–1 documentation, another factor was it would have meant the 1.5 million taxpayers who filed that would not have been able to have easily filed electronically or get their refunds, those that were entitled to it, as quickly as they did.

In looking at the full range of factors that we were considering, we made a decision that I still think is the right one at this time.

I advocate for the additional legislative authority because I think that would be the breaking point in terms of how we use it going forward.

Mr. DAVIS of Illinois. Mr. White, you acknowledged that the Internal Revenue Service moved quickly to implement the program. Do you think that perhaps had there been some additional preplanning, that might have helped, or does it really look like they may have needed additional resources to do a more effective job?

Mr. WHITE. It is clear that they did not have the legislative authority needed to do as many of the pre-refund checks that I have been talking about, as they actually could do. That would make a difference.

Mr. DAVIS of Illinois. You indicated also in your report that if they had the authority to do math error corrections, tell us how that could actually reduce these instances of fraud and abuse?

Mr. WHITE. For example, if IRS had the authority to check prior years' returns, they could easily tell from that whether taxpayers had a requirement to pay back in the $500 increments the 2008 credit.

They could also check whether taxpayers were claiming both credits. You are not allowed to claim the 2008 and the 2009 credit. You can only claim one.

IRS did not have the legal authority to use math error authority to correct situations where taxpayers were making multiple claims. They needed legal authority to do that.

Those are two cases that we found.

Mr. DAVIS of Illinois. Let me just say it has always been my experience that the Internal Revenue Service was pretty tough. It seemed to me that in this instance, a little bit of that toughness was not there. Maybe it has to revert back to the times I have appeared before them.

Thank you very much.

Chairman LEWIS. Thank you. I now turn to Mr. Higgins for his questions.

Mr. HIGGINS. Thank you, Mr. Chairman.

First of all, I just want to make it very clear that this is a good program. It should be extended. 1.4 million households have claimed nearly $10 billion in credit. Over half of those have incomes under $50,000.

While fraud is always going to be part of this, it should not be accepted. I would hope the IRS would embrace the Inspector General's report toward the goal of significantly reducing and ideally eliminating fraud altogether.

I am just curious. If there is fraudulent claims or questionable claims, as you had characterized them, I presume that is true with any of the tax credit programs.

How does this program compare in terms of the percentage of likely fraud versus that of let's say the earned income tax credit? Anybody.

Ms. STIFF. I would answer and have to be candid with you, I am not trying to be evasive, but I think it is too early to know that. We need to finish the audits we have underway and be able to see how much of that actually winds up that we do not allow versus how many is allowed. It is just too soon after the passage of the program and the time it takes to do the enforcement efforts to have an answer to know what that is going to be and then compare it to another program.

I think we are several months away from being able to give you a definitive answer there.

Mr. HIGGINS. Let me put it to you another way. What would be a program that has been longer in duration, like the earned income tax credit, what is the percentage of fraud associated with that?

Ms. STIFF. I don't know off the top of my head what the percentage of fraud is because we use fraud as that which meets a criminal standard, and then we have a number of questionable erroneous claims that are disallowed each year.

I can get you a percentage or maybe one of these gentlemen know. I do not know off the top of my head.

Mr. GEORGE. I do not know the percentage. I know that it is estimated that it is between 10 and $12 billion each year on the earned income tax credit that is inappropriately or improperly paid out.

Mr. HIGGINS. 10 or $12 billion.

Mr. GEORGE. Correct.

Mr. WHITE. Mr. Higgins, if I could add, your questions highlight, I think, a point about the cost of doing audits to ensure compliance with the first-time homebuyer credit. If IRS does more homebuyer audits, it is able to do less audits on other provisions of the Code. That highlights the importance of shifting as much of the compliance checking again to these up front automated procedures so that IRS does not have to shift resources from auditing other tax provisions into auditing this one.

Mr. HIGGINS. Got it. Just in conclusion, Mr. Chairman, I just wanted to again make very clear that I think the objective of the program has been met. Perhaps not to the exact numbers anticipated before its enactment, but it is a good program.

I want to be sure that the 70,000 questionable claims representing half a billion dollars, which is very, very significant, do not serve to undermine those 1.4 million who have benefitted from this program.

By extension, it has helped this economy at least in terms of staving off a deeper and longer recession.

Thank you, Mr. Chairman.

Chairman LEWIS. Thank you. Now we turn to Mr. Kind for your questions.

Mr. KIND. Thank you, Mr. Chairman. I want to thank our witnesses for your testimony today, and just to dove tail into what Mr. Higgins was concluding upon, as we in Congress are deliberating on possibly extending the first-time homebuyer tax credit, there is a lot of information that we are going to have to digest, including this, what you guys are involved with right now.

If there is a problem, we need to clean it up, especially if we are going to extending the program, so that we are more accountable and more responsible to the American taxpayer ultimately.

I am still trying to wrap my head around what exactly is going on here. Commissioner Stiff, let me start with you. Maybe you can help clarify some things.

Of the questionable claims that have been submitted already, do you have any indication or have you broken down what percentage of that is a clear case of criminal intent to defraud or just mistakes being made, harmless errors that you are detecting now that we need to intercept?

Ms. STIFF. A couple ways to slice that. We have had indications on 115 cases of potential schemes involving about 8,000 taxpayers and tax returns that are currently under criminal investigation. It remains to be seen whether indeed that is the case.

Mr. KIND. How many schemes did you say?

Ms. STIFF. We have identified, I think, potentially over 160 and we have 115 currently under investigation.

Mr. KIND. Of those, how many individual claims are involved?

Ms. STIFF. A little more than 8,000 on the 115. On the audits, we have the 106,000 or so under exam. We have closed so few, that to somehow extrapolate that and project it onto the whole, I think, would be doing a disservice.

Mr. KIND. I am a little more confused because somewhere I received some information that of the 167 schemes that you have detected, it could be as high as 25,000 different returns that might be involved. Does that number ring any bells?

Ms. STIFF. Actually, it does. There are 8,000 where we had clear enough indications of being a part of the fraudulent activity that we stopped the processing and did not let the money go out of the 167. The difference is in that 106,000 we are looking at and it remains to be seen. The indications were not clear enough to characterize it as fraud.

Mr. KIND. Of those that you stopped the process, that you were able to intercept, did you initiate criminal investigations or any type of criminal proceedings?

Ms. STIFF. They are part of the investigation of the scheme itself because one of the first things that we look to is were they taken advantage of as part of the scheme or were they part of the scheme. That determination has not been made yet.

Mr. KIND. How are these schemes set up? Are individual tax preparers involved with it or the real estate agents? Is it those who are purchasing the home?

Ms. STIFF. I would have to get back to you to give you a complete answer. I know the ones that I am most familiar with have involved preparers.

Mr. KIND. That would be helpful. If we knew where the problem existed, we would probably have a better idea where we need to concentrate resources and attention to.

Ms. STIFF. We are looking at that because that is what we are going to want to do this next filing season.

Mr. KIND. The audits that you have already initiated, what form are they taking? Are those written audits?

Ms. STIFF. They are. We send a letter to each of the taxpayers and we tell them there appears to be a question with what they filed and we ask them to provide the documentation needed to validate it, and the taxpayers—the ones that have it all right there, they get right back to you, and those who do not, you are in a dialogue over a period of days and weeks and months in some instances trying to get it all finalized.

Mr. KIND. Would I be safe here in assuming that the vast majority of the problem cases that lie out there that we are now detecting and trying to take action on are a result of just innocent errors, just making mistakes in filing?

Ms. STIFF. Based on what we have seen thus far, I would say the indication suggests that, but it is too early for me to weigh in and say it is more one thing than the other.

Mr. KIND. Right. What you are doing right now as far as intercepting some of the claims that have been submitted or anything else, is this going to impede or slow down the closing date process because we are bumping up against the end of November and there is a lot of concern that those purchasing a home for the first time will not be able to get in under the deadline?

Ms. STIFF. Our investigation should not slow down their ability to qualify. It may slow down their ability to receive their funds.

Mr. KIND. It should not hinder the ability of the closing date.

Ms. STIFF. If they closed and they are eligible, they can claim it. If we have a question, we will resolve that after the fact.

Mr. KIND. I want to ask a more general question. You touched upon it. I think it was with Mr. Etheridge. What is the turn around time at the IRS when we do enact a new law as far as updating the database or the filters that you have to install? Where is the state of technology and your ability to adjust on the dime what we are asking you to do?

Ms. STIFF. The state of our technology is improving, as you know. We appreciate the support we have had to continue to focus on that. We are reaching a point in some instances, we can say weeks, and in other instances, we need months lead time.

I think the reason we were able to do this as quickly as we did, admittedly not as quickly as it perhaps warranted, but it was a matter of weeks, was the fact that it was similar enough to other things that we had experience with that we were able to kind of jump start our effort to get the technology lined up.

Mr. KIND. Not to be presumptuous, but since you are looking at a pending retirement, is this a legitimate area that the Committee needs to have a little more focus on, helping the IRS be able to make the adjustments you have to make in light of new tax changes that we are doing here?

We are going to have some tax extenders, some measures that we are going to have to deal with at the end of this year because they are expiring. Usually, we sit around and wait until the 11th hour to do these things, and it puts you in a real box then.

Is this a major issue that we have to be a little more focused on?

Ms. STIFF. Yes, I think based on our experience in the last few years, I think you all have a good understanding of the challenges that late legislation proposes, and you have our commitment that we will continue to be responsive and implement in a responsible manner, regardless of whatever situation you find yourselves in with the passage of law.

Mr. KIND. If we do not see you before, we wish you a very happy retirement and we thank you for your service.

Ms. STIFF. Thank you.

Mr. KIND. Thank you.

Chairman LEWIS. Thank you. Do you have any evidence—when we think of schemes and fraud, sometimes we think of people getting together, people conspiring to do something. Do you have any evidence where there have been groups getting together to take advantage?

Mr. GEORGE. Mr. Chairman, I would note that the report that we released today is an interim report. In our next report, we are specifically looking at that issue to determine whether there are related party transactions or claims by multiple parties for the same property. That is something that we will be able to address in the subsequent report.

Chairman LEWIS. I think we would be interested in seeing that report. If we are going to extend this effort, we need to know.

We now turn to Mr. Becerra for his questions.

Mr. BECERRA. Mr. Chairman, thank you very much. Thank you for holding this hearing. Thank you to all the witnesses for their testimony.

Ms. Stiff, we wish you very well and we thank you for all your years of service to the people of this country.

Ms. STIFF. Thank you.

Mr. BECERRA. From what I understand, and I missed some of the hearing, but from what I understand, there seems to be consensus that we should have math authority extended to the IRS, math error authority, third party verification, some type of age limit.

Ms. Stiff, all that is going to require you to have a lot of very good people doing a lot of extremely diligent work to make sure this tax credit is being used by those who qualify for it.

You are also having to do quite a few audits just to take care of the normal stream of activity from people who file their taxes, 130 to 150 million in America file their taxes.

I know you sometimes have to rely on the marching orders you get from above or from down the street at the White House and OMB, the Office of Management and Budget, in terms of what you can do and say about what you need.

I do not see how you do all this work well without having the resources to actually do the checks, the audits, the follow through, so that we can come back and say it really looks like we should extend this homebuyer tax credit to more Americans because we are still in a very difficult economic time, there is still a lot of families that would like to get into their first home, but if we continue to have errors or fraud in a system like this, we cannot sell this to the American public because we are running these deficits that are very large.

I ask you this, and maybe you have a little bit more freedom as you are getting ready to exit the doors of the Service, are you able with the resources or the new authority we give you to fully examine this tax credit so that when you come back again, we will not find a situation where a four year old applied for a first-time homebuyer tax credit?

Ms. STIFF. You did miss earlier. I will restate what I said.

Mr. BECERRA. I heard what you said.

Ms. STIFF. We need the legislative authorities that we have talked about, that you outlined. We need the passage of the fiscal year 2010 budget.

Can I sit here and assure you that there will be absolutely no errors or no fraud under any circumstances? I suspect not. Experience would say I would be foolish to do that.

I stand here to tell you that I believe with the legislative authority, I believe with the passage of the 2010 budget that we stand ready to handle the work that you have put in front of us.

Mr. BECERRA. Let me ask it a different way. Let me go to door number two. Do you right now have personnel at the IRS who are sitting around twiddling their thumbs because they do not have enough to do?

Ms. STIFF. Absolutely not.

Mr. BECERRA. Do you now have personnel who are handling a workload that is greater than it was for people working at the IRS say ten years ago?

Ms. STIFF. I think the work available to the Agency has expanded.

Mr. BECERRA. Would you say the workload of the Agency is growing or diminishing?

Ms. STIFF. I would say the workload is growing based on the taxpayer base growing, but I would also say that the Agency has become much more efficient and productive in getting the work done. I do not think it requires the same level of people because we have found smarter ways to do work.

Mr. BECERRA. Productivity helps us manage an ever increasing load of work in the IRS?

Ms. STIFF. Yes, it does.

Mr. BECERRA. I know, Mr. George, you would like to jump in on this but before you do, let me ask this. Ms. Stiff, I think you actually have some phenomenal people at the IRS. I think we place such burdens on them, emotional burdens on them because of the work that they do, and it is so easy to attack an IRS worker because they are coming after our money.

At some point, I think it is unfair to us to expect the IRS to produce good results, to perform well, unless you have the ability to reward your workers for what they do. If we continue to rely on productivity increases only, I think we are going to diminish the public support for the work that we do to have a voluntary tax compliance system.

I know you are shackled. I know you cannot say much more. I think you sort of answered my question to door number two by telling me that your workers do not twiddle their thumbs and they become very productive.

We are about, I think, to give you more authority to do a better job of tracking. You have over 100,000 cases that you now have to examine that you did not have a year ago. You have some criminal prosecutions that you are going to engage in that you did not have a year ago. That is a lot of new work on top of all the extra work that is coming in because of the regular flow of activity.

I hope, Mr. Chairman, we are able to move forward to do what we need to do to give you the ability to produce so when you give us numbers, we will be happy, and then we can make decisions on a program like the first-time homebuyer tax credit that are based on its effectiveness, not on whether there was fraud in the system.

I know Mr. George wanted to say something, Mr. Chairman.

Mr. GEORGE. Ever so briefly, Mr. Chairman, with your permission. Every year my office is required to list the top ten management performance challenges confronting the IRS for the upcoming fiscal year. Repeatedly, year after year, human capital has been foremost on that list or towards the top of that list.

It is a Government-wide problem as we recognize, but given the technical nature of the subject matters being handled by the IRS, this is of utmost importance, sir.

Mr. BECERRA. Thank you. Mr. White, I do not know if you want to add anything. You have a chance to examine the IRS and its working's. You do not get paid by the Commissioner, although you still get paid by the Government.

Mr. WHITE. Yes. I would just add that the work we have done over the last 15 years clearly shows the IRS has made substantial improvements in terms of the quality of service they are providing to taxpayers and in terms of their productivity.

Things like their ability to answer telephone calls and provide correct answers to taxpayers, their ability to more quickly turn around refunds, get those checks out to taxpayers faster, they made substantial strides over time.

Mr. BECERRA. Thank you. Thank you, Mr. Chairman.

Chairman LEWIS. Thank you very much. Now we turn to Mr. Crowley for his questions.

Mr. CROWLEY. I thank the Chairman and the Committee for allowing me an opportunity to be here today, not as a member of the Subcommittee, as I once was, Mr. Chairman, and took a lot of decision making for me to not be on this Committee again. Hopefully, that is not held against me personally.

Chairman LEWIS. Mr. Crowley, thank you for sitting in. You are a member of the Full Committee and we miss you being here but we feel very lucky and very blessed to have your presence here today. You are welcome to sit in at any time.

Mr. CROWLEY. Mr. Chairman, would that compliment come out of my time or your time?

[Laughter.]

Chairman LEWIS. My time.

Mr. CROWLEY. Thank you, Mr. Chairman.

Thank you for your testimony today. I just have a couple of questions. There is a great deal of discussion as mentioned before in terms of even just piggy backing Mr. Becerra, about extending the first-time homebuyer tax credit.

How can Congress again further help simplify the administration of this or any other tax credit that we may or may not put into law in the future? Is there any advice that the IRS can give us on that?

Ms. STIFF. A couple of things. They are going to ring familiar because they are along the themes that we have discussed here today.

With any refundable credit, to the extent that we have third party reporting, to the extent that the eligibility requirements are not complex, I think it enhances the chances that credit will be administered in the way and received in the way that the Congress intends.

Mr. GEORGE. Mr. Crowley, this is going to be an extraordinarily difficult effort on the part of the IRS when you have two different classes of recipients of this credit. Again, those who received it in 2008 who will be required to repay this over the course of 15 years, and then those who received it under the Recovery Act who are not required to repay it unless they sell the home within 36 months.

Keep in mind that statutorily the IRS only has authority to go back 10 years. How they are going to figure this out and especially as we noted in our written testimony and in my oral testimony, that they are not coding some of these taxpayer accounts accordingly.

This is truly going to be a challenge.

Mr. CROWLEY. Bureaucratic nightmare.

Mr. GEORGE. It will be, sir.

Mr. CROWLEY. Thank you. Ms. Stiff, you discussed the need for the IRS to receive statutory authority for math error authority. Could you tell me about math error authority and how it would assist the IRS? Just give me a little insight into that.

Ms. STIFF. When we have math error authority, as we process, we receive your tax return, as it actually goes through our systemic processing, the system can be programmed and coded to detect those conditions or the existence of those conditions or the lack of those conditions, and stop the refund related to those conditions from being issued before it ever goes out the door.

Without that, we have to go through a full audit and assess the refund under the statutory deficiency laws.

Mr. CROWLEY. So you do not add more to the bureaucracy, so to speak, in retrieving that back.

Ms. STIFF. Right.

Mr. CROWLEY. Does anyone else want to comment on that?

[No response.]

Mr. CROWLEY. I have been given some statistics here about a break down by state per capita and their use of the first-time homebuyer tax credit. It seems to be benefitting states that are hardest hit by the real estate bubble.

Is there any documentation of the type of taxpayer that is filing for this credit or the types of homes they may be buying? For instance, do you see a tendency towards buying foreclosed properties going on in some states? Properties that are really being done for speculative purposes, albeit they may be holding on to the properties for more than 36 months, but to take advantage of the tax credit?

Just looking at my home state of New York, for instance, we are number 49, so 50,500 homes purchased in a state of 19.5 million people, in comparison to say New Jersey, 30,000 in a state of 8 million people. I can go on. It is kind of interesting. Just looking at Utah, almost 20,000 in a state of 2.5 million people.

Can anyone comment on that?

Mr. WHITE. Yes. First of all, we did not have information about the type of house that was being purchased. We did have some information about income levels. For example, about 59 percent of taxpayers had incomes under $50,000 who made use of the tax credit.

We did do a little bit of comparison with a list of states. One comparison we looked at was state foreclosure rates. We did find a pretty high correlation between states with high foreclosure rates—we did this comparison for 2008—for states that had high foreclosure rates in 2008, there was a correlation with the take up rates for the credit. Beyond that, we have not been able to do any analysis.

Mr. CROWLEY. Does anyone else have a concern—not concern. I guess we have a concern or I have a concern that maybe some of these homes that were purchased would have been purchased because they were in foreclosure. A concern that maybe some of this would have happened anyway. That is what I am trying to get at.

I think this overall is a very good program, and quite frankly, I would support the extension of the program and maybe even possibly the expansion of the program beyond first-time homebuyers. I think as Mr. Higgins has mentioned as well, I think this has helped in many ways to spur growth in our economy in many, many ways.

I do have concerns about this being taken advantage of, especially if we were to extend this beyond first-time homebuyers. Again, even with the income limits, you could still have abuse of purchasing of homes that otherwise would have been sold anyway because they had been de-valued so much.

Does anyone else have that concern or that observation?

Mr. WHITE. That is one of the fundamental questions about the effectiveness of the credit, what fraction of these homes would have been purchased anyway, what fraction of these home buyers making use of the credit would have purchased anyway as opposed to stimulating completely new purchases.

I do not have an answer to that question. That is the ultimate question about the effectiveness.

Mr. CROWLEY. Thank you all for your testimony. Thank you, Mr. Chairman.

Chairman LEWIS. Thank you very much. I believe the gentleman from California, Mr. Becerra, has one last question.

Mr. BECERRA. Thank you, Mr. Chairman. Just a quick question. Any time someone prepares a form, tax form, for the actual filer, that preparer has to identify himself or herself on the form, I believe. Is that correct?

Ms. STIFF. They should.

Mr. BECERRA. Is it possible for the IRS to tell us, and perhaps Mr. George, you already know this, if we have a breakdown of the number of filings for this tax credit that were prepared by someone other than the filer who bought the home?

Mr. GEORGE. Actually, that is a good question. I do not have that information.

Mr. BECERRA. Ms. Stiff.

Ms. STIFF. I do not have it off the top of my head, but that is certainly information we can get.

Mr. BECERRA. Can we get that for the Committee?

Ms. STIFF. Sure. I think as you know, we are working on a preparer study and hoping to have recommendations by the end of the year. I know some of what we have learned here will certainly bleed into that.

Mr. BECERRA. That is precisely the reason for asking. If you could share that with us, that would help us as we prepare to take on the issue along with the IRS on how to deal with the various tax preparers who are out there in this country.

Mr. GEORGE. If I may, Mr. Becerra, somewhat related issue. I do not know whether it is within the jurisdiction of this Committee, but if the HUD–1 form which is a document that taxpayers have completed, if it had an unique identification number or the use of a Social Security number on it, that would assist the IRS greatly in terms of matching the types of information that would determine whether or not this is a valid claim that the taxpayer is seeking.

Mr. BECERRA. That is an excellent point. Thank you for that. Thank you, Mr. Chairman.

Chairman LEWIS. Thank you very much. Let me thank the witnesses for their testimony. The Subcommittee appreciates your views. I want to thank the members for being here.

Madam Deputy Commissioner, again, we wish you well and much success in your future.

If there is any other business to come before the Subcommittee.

[No response.]

Chairman LEWIS. There being none, the hearing is now adjourned.

[Whereupon, at 11:34 a.m., the subcommittee recessed.]

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