Office of the Inspector General

SOCIAL SECURITY ADMINISTRATION

Audit Report

Follow-up Review of Self-employment Earnings Removed from the Master Earnings File

A-06-21-51020 September 2023

MEMORANDUM

Date: September 26, 2023 **Refer to:** A-06-21-51020

To: Kilolo Kijakazi
Acting Commissioner

From: Gail S. Ennis
Inspector General

Subject: Follow-up Review of Self-employment Earnings Removed from the Master Earnings File

The attached final report presents the results of the Office of Audit's review. The objectives were to (1) determine whether the Social Security Administration had taken corrective action in response to the recommendation in our 2015 review of *Self-employment Earnings Removed from the Master Earnings File* and (2) review instances where SSA removed self-employment earnings from the Master Earnings File since our 2015 review.

Please provide within 60 days a corrective action plan that addresses each recommendation. If you wish to discuss the final report, please call me or have your staff contact Michelle L. Anderson, Assistant Inspector General for Audit.

Attachment

Follow-up Review of Self-employment Earnings Removed from the Master Earnings File
A-06-21-51020

September 2023 **Office of Audit Report Summary**

Objectives

To (1) determine whether the Social Security Administration (SSA) had taken corrective action in response to the recommendation in our 2015 review of *Self-employment Earnings Removed from the Master Earnings File* and (2) review instances where SSA removed self-employment earnings from the Master Earnings File (MEF) since our 2015 review.

Background

In January 2015, we reported SSA removed from its MEF about $742 million in self-employment income (SEI) originally reported on approximately 50,000 numberholders' Federal income tax returns for Tax Years (TY) 2008 through 2011. During the period reviewed, SSA deleted $343 million in SEI and notified the Internal Revenue Service (IRS) when it deleted the earnings. However, during the same period, SSA transferred $399 million in SEI to the Earnings Suspense File (ESF), SSA's repository of all reported earnings it cannot match to individual workers' earnings records, instead of deleting it. SSA did not report these transactions to the IRS. We recommended that SSA notify the IRS in all cases where it removes SEI from a numberholder's earnings record. SSA agreed with the recommendation. For our current review, we identified approximately 61,000 numberholders for whom SSA removed about $1.2 billion in TY 2012 through 2019 SEI from the MEF.

Results

In response to the recommendation in our 2015 review, in July 2019, SSA and the IRS signed a Memorandum of Understanding under which SSA electronically transmits SEI Determination Posting Record reports to the IRS. Since that time, SSA has provided the IRS weekly data identifying SEI adjustments, including when SSA removes numberholders' SEI from the MEF and transfers the earnings to the ESF. Providing the IRS information on all instances where SSA removes SEI from individuals' earnings records allows the IRS to identify erroneous refundable tax credit payments.

However, SSA employees did not follow Agency policy when they removed SEI from the MEF in 119 (79 percent) of 150 randomly selected cases we reviewed. Further, most, if not all, of the $551 million in disclaimed SEI that SSA employees removed from 27,834 numberholders' earnings records during our audit period and transferred to the ESF did not meet Agency requirements for transfer and, instead, should have been deleted. Transferring earnings to the ESF, instead of deleting them, prevented the earnings from being considered as net corrections and prevented the return to the Department of the Treasury approximately $67 million in *Self-Employment Contributions Act* tax SSA collected on the earnings.

SSA employees not following policy in such a high percentage of disclaimed SEI transactions, which occur infrequently compared with other transactions routinely processed in SSA field offices, suggests the employees processing them were not familiar with the policies or the policies were not clear.

Recommendations

We recommended SSA (1) amend policies to clearly instruct employees to delete SEI when the numberholder under whose personal information the earnings were reported disclaims the earnings; (2) take appropriate action to ensure employees process earnings adjustments in accordance with policy, and (3) delete all disclaimed SEI for TYs 2012 through 2019 that remain in the ESF unless the earnings were reported with a name that clearly differs from that on the earnings record to which they were originally posted. SSA agreed with Recommendation 2 but disagreed with Recommendations 1 and 3.

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ABBREVIATIONS

EITC	Earned Income Tax Credit
ESF	Earnings Suspense File
IRS	Internal Revenue Service
MEF	Master Earnings File
OIG	Office of the Inspector General
POMS	Program Operations Manual System
SEI	Self-Employment Income
SSA	Social Security Administration
SSI	Supplemental Security Income
SSN	Social Security Number
TY	Tax Year
U.S.C.	United States Code

OBJECTIVES

To (1) determine whether the Social Security Administration (SSA) had taken corrective action in response to the recommendation in our 2015 review of *Self-employment Earnings Removed from the Master Earnings File* and (2) review instances where SSA removed self-employment earnings from the Master Earnings File (MEF)[1] since our 2015 review.

BACKGROUND

Individuals initially report self-employment income (SEI)[2] to the Internal Revenue Service (IRS). In turn, the IRS reports the SEI to SSA to be posted to the individual's earnings record. SSA uses earnings information for various purposes, including determining the accuracy of past Social Security benefits or Supplemental Security Income (SSI) payments and evaluating continuing eligibility for payments. A recipient who reports SEI on a Federal tax return can prevent a reduction in SSI payments or re-evaluation of a disability claim by contacting an SSA field office and renouncing or disclaiming the earnings because they claim, or SSA finds, they did not earn them. SSA generally accepts an individual's signed statement disclaiming the earnings[3] and removes the earnings from the individual's earnings record by deleting the earnings or transferring them to the Earnings Suspense File (ESF)[4] using its Item Correction System.

SSA employees are to be aware when it may be to an individual's advantage to disclaim earnings. Policy states that, if it appears to be to the individual's advantage to have earnings removed, do not accept the statement or remove the earnings without complete investigation of the situation involved.[5] Specifically, SSA employees who believe there is reason to question the reported SEI should obtain and review at least one IRS Form 1040, Schedule C, *Profit or Loss from Business (Sole Proprietorship)*, Schedule F, *Profit or Loss from Farming*, or Schedule SE (Self-Employment Tax).[6] When SEI must be developed, SSA requires that the individual provide pertinent portions of their income tax return(s) (that is, Schedules C, F, and SE).[7]

We initiated our 2015 review after a Dallas Regional Commissioner informed us that field offices had reported several cases where SSI recipients admitted they falsified SEI on tax returns to fraudulently obtain the Earned Income Tax Credit (EITC),[8] which requires among other things, that the individual has earned income and meets certain adjusted gross income and credit limits for the current, previous, and upcoming tax years. The recipients subsequently visited SSA field

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[1] The MEF is a repository of earnings information maintained by SSA.

[2] SSA refers to earnings from self-employment as both "self-employment earnings" and "self-employment income." Throughout the report we use "SEI" to refer to earnings from self-employment.

[3] SSA, *POMS,* RM 03870.060 B.1 (effective January 29, 2015).

[4] The ESF is a repository for reported earnings items with names/Social Security numbers (SSN) that do not match SSA's records or have other questionable characteristics, such as earnings reported under a deceased individual's SSN.

[5] SSA, *POMS,* RM 03870.060 B.2 (effective January 29, 2015).

[6] SSA, *POMS,* RS 01804.044 B (effective August 19, 2010).

[7] SSA, *POMS,* RS 01804.050 (effective August 19, 2010).

[8] See [Who Qualifies for the Earned Income Tax Credit (EITC), Internal Revenue Service (irs.gov)](irs.gov).

offices and disclaimed the SEI to prevent SSA from reducing the SSI payments. We reported SSA removed from its MEF about $742 million in SEI originally reported on approximately 50,000 numberholders' Federal income tax returns for Tax Years (TY) 2008 through 2011. SSA deleted $343 million in SEI and notified the IRS of these transactions. However, during the same period, instead of deleting $399 million in SEI, SSA transferred it to the ESF. SSA did not report these transactions to the IRS. At our request, the Treasury Inspector General for Tax Administration reviewed tax returns associated with SEI that SSA transferred to the ESF from randomly selected numberholders' earnings records. Based on its review, the Treasury Inspector General for Tax Administration determined tax filers had used the SEI to claim the EITC on 77.3 percent of the tax returns reviewed. The average EITC amount paid per tax return was $4,053. We recommended SSA notify the IRS in all cases where it removes SEI from a numberholder's earnings record. SSA agreed with the recommendation.

For this review, we obtained data from the MEF that identified all instances where SSA used the Item Correction System to remove SEI reported for TYs 2012 through 2019. As of April 2021, SSA had processed 102,476 transactions and removed approximately $1.2 billion in SEI from 61,214 numberholders' earnings records. See Appendix A for additional background and Appendix B for information on our scope and methodology.

RESULTS OF REVIEW

SSA took corrective action in response to the recommendation in our 2015 review. Specifically, in July 2019, SSA and the IRS signed a Memorandum of Understanding under which SSA electronically transmits SEI Determination Posting Record reports to IRS. Since that time, SSA has provided the IRS with weekly data that identify SEI adjustments, including instances when SSA removed numberholders' SEI from the MEF and transferred the earnings to the ESF.[9] Providing the IRS with information on all instances where SSA removes SEI from individuals' earnings records gives the IRS an opportunity to identify erroneous refundable tax credit payments, including EITCs.

We reviewed SSA's justification for removing SEI from the earnings records of 150 randomly selected numberholders and found that 90 (60 percent) transactions involved instances where individuals admitted they falsified SEI or alleged identity thieves misused their personally identifiable information to fraudulently obtain tax benefits. We also found SSA did not follow Agency policy when it removed SEI from the MEF in 119 (79 percent) cases. Further, most of the $551 million in disclaimed SEI that SSA employees removed from 27,834 numberholders' earnings records during our audit period and transferred to the ESF did not meet Agency requirements for transfer, and instead, should have been deleted.

[9] SSA informed us it did not retain copies of data provided to IRS under this Memorandum of Understanding. The IRS provided us with the data files it received from SSA and informed us SSA did not provide data during two different weeks of our review period. SSA officials disagreed and provided copies of transmittal logs indicating that SSA had transmitted data to the IRS during the 2 weeks in question. We provided the IRS with the 1,596 earnings adjustment records SSA processed during the 2 weeks and consider this matter resolved.

Transferring earnings to the ESF, instead of deleting them, prevented the earnings from being considered as net corrections[10] and prevented the return to the Department of the Treasury approximately $67 million[11] in *Self-Employment Contributions Act* tax SSA collected on the earnings.

Justification for Removing Self-employment Earnings from the Master Earnings File

For TYs 2012 through 2019, SSA removed approximately $1.2 billion in SEI from about 61,000 individuals' earnings records. SSA staff deleted approximately $668 million in SEI and transferred $551 million in SEI to the ESF. We reviewed SEI determination rationale that SSA employees recorded in the Item Correction System and other documents available in SSA systems for randomly selected transactions. We summarize the information below.

Acknowledged False Reporting of Self-employment Earnings to Fraudulently Obtain the Earned Income Tax Credit

In 45 cases, SSA removed SEI from the MEF after numberholders acknowledged falsifying SEI on their tax returns to fraudulently obtain the EITC. Each of these cases involved improper Federal payments. Not only did these individuals admit to fraudulently obtaining the EITC, but by disclaiming the earnings, they also avoided any negative affect the earnings would have had on their SSA claims or payments. For example, a disability recipient defrauded the EITC program on her 2013 through 2018 tax returns and received $27,719 in tax refunds to which she was not entitled. This beneficiary signed a statement alleging an accountant filed her taxes for those TYs. However, tax returns the beneficiary provided for TYs 2013 through 2017 were self-prepared. SSA deleted the earnings and continued paying her disability benefits.

Alleged Identity Theft

In 45 cases, SSA removed the SEI from the MEF after numberholders (1) alleged identity thieves used their SSNs to file fraudulent tax returns or (2) denied earning or reporting SEI on a tax return. For example, SSA reviewed a disability recipient's record after the IRS notified SSA the recipient reported $55,000 in SEI for TYs 2013 through 2017. The recipient alleged she had not worked since she became disabled in 2008. She stated someone used her SSN to work and file tax returns. However, SSA records included an SSA-820, *Work Activity Report,* the numberholder completed in 2015 acknowledging SEI in TYs 2013 and 2014. SSA deleted the earnings without proper development.

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[10] SSA provides the Department of the Treasury information each quarter that certifies changes in earnings (both wages and SEI) since the previous quarter to adjust previously transferred tax liabilities made on an estimated basis, and to reflect the latest available earnings data. All past years' earnings are subject to correction. SSA includes deleted SEI in the earnings corrections reported to the IRS but does not include SEI it transfers to the ESF.

[11] This amount was computed based on $550,893,489 in TY 2012 through 2019 SEI that SSA transferred to the ESF, minus $9,463,962 in TY 2012 through 2019 SEI that SSA reinstated to other wage earners' records, times 12.4 percent *Self-Employment Contributions Act* tax collected on the earnings and transferred to SSA Trust Funds.

Earnings Not Bona Fide

In 35 cases, SSA personnel deleted SEI from the MEF after they determined the SEI claimed on the numberholders' tax returns was not bona fide. In most cases, the numberholder claimed SEI for babysitting, cooking, or cleaning for family members. For example, a 65-year-old man filed for retirement benefits in 2012. SSA denied the claim because he had only 12 of the 40 quarterly work credits required to be eligible for benefits. In 2019, he re-applied for retirement benefits. While the claim was being processed, SSA personnel observed he reported between $5,818 and $6,649 in SEI on his 2016 through 2018 tax returns, providing him the exact amount of work credits needed for retirement benefit eligibility. (We note the numberholder similarly reported SEI during TYs 2012 through 2015; however, SSA did not conduct any development of those earnings to evaluate if they were bona fide.) The man claimed he earned SEI working in construction. However, the profession listed on his tax return was not consistent with his statement. He could not substantiate any of the earnings. SSA deleted the earnings and denied the retirement claim. Based on provision of new earnings information, the man reapplied and was approved for retirement benefits in 2021.

Other Justification Provided

In the remaining 25 cases, SSA's justification for removing the earnings indicated individuals allegedly misreported SEI on Federal tax returns. In 13 cases, SSA removed earnings from the MEF after the numberholders alleged they mistakenly reported other types of income as SEI. For example, SSA reviewed an SSI claim after it received IRS notification a recipient reported SEI for TY 2012. The beneficiary told SSA she mistakenly reported $3,361 in janitorial wages on her tax return as both wages and as SEI. The recipient's tax return showed the overstated income resulted in a $3,120 EITC. SSA deleted the earnings and continued paying SSI.

In four cases, SSA removed earnings from the MEF after numberholders alleged they had submitted amended tax returns to correct income reporting errors. For example, SSA reviewed a disability claim after it received IRS notification indicating the beneficiary reported $16,749 in SEI for TY 2012. The beneficiary told SSA he filed an amended tax return that changed the income to $13,984. SSA deleted the $16,749 earnings and continued paying benefits. Several months later, the IRS reported the $13,984 in revised SEI and SSA added the earnings to the numberholder's earnings record.

In the remaining eight cases, SSA removed earnings from the MEF after numberholders alleged a family member's earnings were mistakenly reported under their own SSN. For example, SSA reviewed a disability claim after it received IRS notification indicating the beneficiary reported $27,908 in SEI for TY 2015. The beneficiary told SSA he mistakenly reported his wife's SEI to the IRS under his name and SSN. SSA transferred the earnings to the ESF and continued paying benefits.

Individuals Disclaimed Self-employment Earnings in Multiple Tax Years

The current process allows beneficiaries to falsify earnings to the IRS but disclaim the earnings to SSA. SSA policy instructs field office staff to remove disclaimed SEI from an individual's earnings record and send notification to the IRS. However, SSA policy provides for no punitive action against beneficiaries who repeatedly take advantage of this process. As illustrated in Table 1, during our review period, 22,486 individuals disclaimed SEI for multiple TYs.

Table 1: Numberholders Who Requested SSA Remove More than 1 Year of SEI from Their Earnings Records for TYs 2012 Through 2019

TYs with Disclaimed SEI	Number of Individuals
2	12,376
3	5,625
4	2,384
5	1,154
6	597
7	288
8	62
TOTAL	**22,486**

These 22,486 individuals include 62 individuals who disclaimed SEI reported to SSA in all 8 TYs from 2012 through 2019. For example, every TY from 2012 through 2019, a disabled adult child receiving disability benefits on her parent's payment record reported SEI to the IRS to fraudulently obtain the EITC. Each year when SSA informed her the earnings negatively affected her entitlement to disability benefits, she requested SSA remove the earnings from her record. An SSA employee who processed at least one of the SEI removal transactions input a note in SSA systems stating the beneficiary ". . . is committing fraud and has been for many years. We have removed SEI from her SSN every year since 2005 but she continues to abuse the IRS. She is not self-employed and has never been self-employed."

Employees Who Removed Earnings Did Not Follow Policy

SSA staff who removed SEI from the MEF did not consistently comply with established earnings development policies in 119 (79 percent) of 150 randomly selected cases reviewed.[12]

- In 82 cases, SSA did not obtain copies of tax returns from numberholders requesting removal of SEI from their earnings record. In these cases, it was advantageous for the individual to disclaim the earnings because they were receiving benefits or had filed a benefit application.[13]

[12] In 96 of the 119 cases, employees did not comply with multiple agency policies when removing SEI from the MEF.

[13] SSA, *POMS*, RM 03870.055 B (September 22, 2022), RS 01804.050 (August 19, 2010), and RS 01804.044 B (August 19, 2010).

- In 62 cases, SSA staff transferred the disclaimed earnings to the ESF when the earnings should have been deleted because they were reported to the IRS under the identities of the numberholders who disclaimed the earnings.[14]
- In 42 cases, SSA employees did not require the numberholders to sign written statements disclaiming the earnings.[15]
- In 52 cases, SSA accepted the numberholder's statement disclaiming earnings in instances where it was to the numberholder's advantage to remove the earnings without requiring the numberholder to submit additional supporting documentation.[16]
- In 20 cases, SSA did not include system remarks to notify the IRS that numberholders had acknowledged reporting fictitious earnings to fraudulently obtain the EITC.
- In 14 cases, SSA staff did not provide the numberholder with a written notice containing full appeal rights.[17]

Disclaimed SEI transactions occur relatively infrequently compared with other transactions routinely processed in SSA field offices, such as enumeration and disability or retirement claims processing. Employees not following policy in such a high percentage of cases reviewed suggests either SSA employees processing the transactions were not familiar with the policies or the policies were not clear.

Failure to follow policy when removing earnings from SSA records can inadvertently facilitate tax or SSA benefit fraud by allowing individuals to falsify earnings to the IRS to obtain the EITC, then allow the individuals to avoid corresponding payment reductions, reconsideration, or denial of SSA benefits simply by requesting SSA remove the earnings from their record. Now that SSA is reporting to the IRS both deleted SEI and SEI it transfers to the ESF, the IRS has a better opportunity to identify erroneous or fraudulent refundable tax credit payments.

Disclaimed Earnings Erroneously Transferred to the Earnings Suspense File

SSA removed from the MEF $551 million in SEI reported for TYs 2012 through 2019 that it originally posted to 27,834 individuals' earnings records and transferred the earnings to the ESF. Before posting earnings to the MEF, SSA systems verify that the name and SSN on the earnings report received from the IRS match information in its Numerical Identification file. SSA employees can remove SEI posted to the MEF and transfer the earnings to the ESF only when (1) the earnings are reported in a name which clearly differs from that on the earnings record to which they are posted and (2) the numberholder alleges the earnings do not belong to him/her.[18]

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[14] SSA, *POMS*, RM 03870.057 A (May 7, 2008).

[15] SSA, *POMS,* RM 03870.060 A (January 29, 2015). We considered all statements provided by the individuals; for these 42 cases, no statements were documented in SSA systems.

[16] SSA, *POMS,* RM 03870.060 B (January 29, 2015).

[17] SSA, *POMS,* RS 01405.003 B.1 (February 22, 2007).

[18] SSA, POMS RM 03870.057 (effective May 07, 2008).

Because SSA system controls are designed to verify that SEI posted to an individual's earnings record is reported in the individual's name, most, if not all, the $551 million in disclaimed SEI that SSA employees removed from numberholders' earnings records and transferred to the ESF did not meet Agency requirements for transfer, and instead, should have been deleted.[19] Transferring earnings to the ESF, instead of deleting them, prevented the earnings from being considered as net corrections and prevented the return to the Department of the Treasury approximately $67 million in *Self-Employment Contributions Act* tax SSA collected on the earnings.

RECOMMENDATIONS

We recommend SSA:

1. Amend policies to clearly instruct employees to delete SEI, rather than transfer it to the ESF, when the numberholder under whose personal information the earnings were reported disclaims the earnings.

2. Take appropriate action (for example, conduct additional training, update policy and user guides, send emergency messages) to ensure employees process earnings adjustments in accordance with policy.

3. Delete all disclaimed SEI for TYs 2012 through 2019 that remain in the ESF unless the earnings were reported with a name that clearly differs from that on the earnings record to which they were originally posted.

AGENCY COMMENTS

SSA agreed with Recommendation 2 to take appropriate action to ensure employees process earnings adjustments in accordance with policy. However, SSA disagreed with Recommendation 1 and stated it cannot delete SEI without an IRS action, such as granting a taxpayer request for correction. SSA also disagreed with Recommendation 3 and stated there is no basis to presume that disclaimed SEI should be deleted from the ESF until the IRS tells the Agency that SEI reported on a tax return is fraudulent or otherwise requires correction. See the full text of the Agency's comments in Appendix C.

OFFICE OF THE INSPECTOR GENERAL RESPONSE

Regarding SSA's response to Recommendation 1, without justification or reference to legal authority, SSA officials stated the Agency's new position is that it cannot delete SEI without an IRS action, such as granting a taxpayer request for correction (meaning the taxpayer must file an amended tax return). However, the Agency's assertion is contrary to (1) Federal statute, which grants SSA the authority to correct earnings prior to expiration of the time limitation or delete earnings after expiration of the time limitation;[20] (2) existing Agency policy, which explains

[19] Our review of 150 randomly selected cases included 62 cases where SSA removed SEI from the MEF and transferred it to the ESF. In all 62 cases, the SEI was reported to SSA under the name and SSN of the individual who disclaimed the earnings and did not meet Agency requirements for transfer to the ESF.

[20] 42 U.S.C. §§ 405(c)(1)(B), 405(c)(4), 405(c)(5)(C). The time limitation is 3 years, 3 months, and 15 days.

conditions required to transfer earnings to the ESF and provides examples of disclaimed SEI that SSA should delete;[21] and (3) past practice, as demonstrated by the $668 million in SEI that SSA deleted during our audit period with little or no IRS action. Based on SSA's response, it appears the Agency intends to begin transferring nearly all disclaimed SEI to the ESF including when (1) taxpayers acknowledge falsifying the earnings to obtain the EITC, (2) identity thieves falsify the earnings on fraudulently filed tax returns, and (3) SSA formally determines the earnings are not bona fide.

SSA created the ESF as a holding place for wage and SEI items *it cannot match* to a worker's earnings record. However, SSA *matched* all of the $551 million in SEI it transferred to ESF during our audit period to workers' earnings records. In most cases, when individuals disclaimed the SEI, they effectively invalidated the earnings and removed any expectation that SSA would or should credit the earnings to another wage earner's record. Therefore, SSA should have realized when it transferred the disclaimed earnings they were likely to remain in the ESF indefinitely.

SSA removes SEI posted to a numberholder's record at the numberholder's request without any assurance the numberholder will report the same changes to the IRS. Individuals face minimal consequences for disclaiming SEI to SSA and often benefit financially from doing so (for example, by asking SSA to remove SEI from their earnings records, SSI recipients can avoid overpayments SSA assessed after receiving and posting the earnings information to the recipients' earnings records). However, most individuals face negative consequences if they report the same changes to the IRS (for example, they could be required to repay fraudulently obtained EITC or other fraudulently obtained tax refunds/credits, face criminal charges, etc.). As a result, it is unlikely that individuals who disclaim SEI to SSA voluntarily report the changes to the IRS or request corrections to their tax returns. Therefore, the IRS will not have related actions/corrections to report back to SSA. SSA's new position that it cannot delete SEI without an IRS action seems to be intended to minimize deletion of disclaimed SEI and maximize its transfer to the ESF. This, in turn, will allow SSA to retain *Self-Employment Contribution Act* taxes collected on these illegitimate earnings.

[21] See Footnote 14.

Regarding SSA's response to Recommendation 3, we disagree with the assertion that SSA has no basis to presume that disclaimed SEI should be deleted from the ESF. The individuals under whose personally identifiable information the earnings were initially reported provided the basis to presume the earnings should be deleted when they disclaimed the earnings and acknowledged the earnings were fraudulent or illegitimate. SSA should not have transferred the earnings to the ESF and should delete them.

Michelle L. Anderson

Michelle L. Anderson
Assistant Inspector General for Audit

APPENDICES

Appendix A – BACKGROUND

The Social Security Administration (SSA) provides benefits under Titles II and XVI of the *Social Security Act*.[1] Under Title II, an individual (or certain qualifying family members such as a spouse, widow[er], or child[ren]) may become entitled to benefits under the Old-Age, Survivors and Disability Insurance programs based on the individual's taxable earnings during his/her lifetime. In addition, to qualify for Disability Insurance benefits, a worker must have a physical or mental impairment that prevents him/her from performing substantial gainful activity with earnings above a certain monthly amount. Disability Insurance beneficiaries are required to report work activity.[2] Under Title XVI, eligibility for Supplemental Security Income (SSI) is based on income and resources. Additionally, SSI recipients must be age 65 or older or meet disability requirements. Income is counted each month and, generally, the more income a recipient has, the lower his/her SSI payment will be. An individual who has too much income in a particular month is not eligible for an SSI payment in that month.[3] Income includes wages and net earnings from self-employment.[4] SSI recipients must report any information that may affect their eligibility or payment amount.

Individuals with $400 or more in net earnings from self-employment are required to report the earnings to the Internal Revenue Service (IRS) on their Federal tax return using IRS Form 1040, Schedule C, *Profit or Loss From Business*.[5] Individuals must also use the income or loss calculated on Schedule C to determine the amount of Social Security and Medicare taxes owed on their self-employment income (SEI) and report these amounts on IRS Form 1040, Schedule SE, *Self-Employment Tax*. The IRS, in turn, forwards the SEI information to SSA. The Department of the Treasury transfers any Social Security taxes payable on the income to the Social Security Trust Fund.[6] SSA is responsible for recording each worker's earnings history for benefit purposes and processing earnings and tax information to transmit to the IRS.

Low- to moderate-income workers may be eligible to claim the Earned Income Tax Credit (EITC), which may lower their taxes or result in a tax refund. For Tax Year 2021, the maximum EITC available to earners with three or more qualifying children was $6,728. To claim the EITC, individuals must have earned income within certain limits. The amount of EITC decreases as earned income increases up to specified levels. Earnings above specified levels ($57,414 in Tax Year 2021 for joint filers with 3 or more children) reduce the EITC to $0.

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[1] *Social Security Act*, 42 U.S.C. §§ 401-402, 1381-1382.

[2] 20 C.F.R. § 404.1588.

[3] *SSA, POMS,* SI 00810.001 (September 26, 2011).

[4] *SSA, POMS, SI* 00810.015 (September 26, 2011).

[5] Taxpayers may use Form 1040, Schedule C-EZ, *Net Profit from Business*, instead of Schedule C in limited circumstances.

[6] Workers earn their Social Security benefits by contributing through deductions from their paychecks. The Social Security trust funds include the Old-Age and Survivors Insurance fund, which pays benefits to retired workers and their families and to the families of deceased workers; and the Disability Insurance fund, which pays benefits to disabled workers and their families.

The EITC is subject to fraud and abuse. According to the Treasury Inspector General for Tax Administration, the IRS estimated that 28 percent of all EITC payments should not have been issued for Fiscal Year 2021 and were therefore improper. The IRS also estimated that, during this period, it issued $19 billion in improper EITC payments.[7]

SSA uses earnings information for various purposes, including determining the amount of Social Security benefits and/or SSI payments and evaluating continuing eligibility for payments. Once SSA becomes aware of earnings, SSA can retroactively correct the benefit or payment amount as necessary. One way a recipient can prevent a reduction in SSI payments or re-evaluation of a disability claim prompted by SEI reported on their Federal tax return is to contact an SSA field office and renounce or disclaim the earnings.

Supplemental Security Income Recipients with Self-employment Income

The SSI program provides income to persons with little or no resources or countable income who are aged 65 or older, blind or disabled adults, and blind or disabled children. The Federal payment is based on the individual's countable income. The first $20 in monthly earned or unearned income is not counted. SSA also excludes $65 of monthly earnings plus one-half of any earnings above $65. SSA treats net earnings from self-employment as earned income. This SEI is determined on a taxable year basis. The SSA divides the earnings equally among the months in the taxable year to get the earnings for each month.

SSI recipients are required to report all earnings to SSA. If the IRS notifies SSA that an SSI recipient reported SEI on his/her tax return, and the recipient has not already disclosed this income to SSA, SSA determines whether it overpaid the recipient. If so, SSA informs the recipient of the cause of the overpayment and requests a refund of the full amount of the overpayment.

Disability Insurance Beneficiaries with Self-employment Income

Disabled beneficiaries must report all earnings to SSA for timely evaluation of substantial gainful activity. If the IRS notifies SSA that a disability beneficiary reported SEI on his/her tax return, SSA determines whether the work constitutes substantial gainful activity. SEI earned by disabled beneficiaries may indicate they are able to do work that constitutes substantial gainful activity, and therefore, are not eligible for payments. Additionally, SEI earned by individuals applying for disability benefits may indicate they are able to do work that constitutes substantial gainful activity, and therefore, are not eligible for benefits.

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[7] Treasury Inspector General for Tax Administration, *Programs Susceptible to Improper Payments Are Not Adequately Assessed and Reported*, May 2022.

Appendix B – Scope and Methodology

To accomplish our objectives, we:

- Reviewed applicable Federal laws and regulations; Social Security Administration (SSA) policies and procedures; and prior Office of the Inspector General reports.
- Contacted SSA officials to gain an understanding of the Item Correction adjustment process.
- Evaluated the criteria in the Memorandum of Understanding for SSA's weekly self-employment income (SEI) Determination Posting Record data to the Internal Revenue Service (IRS).
- Reviewed IRS publications on the Earned-income Tax Credit.
- Met with IRS officials to obtain weekly SEI report data they received from SSA.
- Obtained data identifying all instances where SSA used the Item Correction System to remove from the Master Earnings File (MEF) SEI reported for Tax Years (TY) 2012 through 2019. As of April 2021, SSA had processed 102,476 transactions removing $1,218,543,093 in SEI from 61,214 numberholders' earnings records:
    - SSA processed 57,763 transactions that deleted $667,649,604 in SEI from the MEF.
    - SSA processed 44,713 transactions that transferred $550,893,489 in SEI from the MEF to the Earnings Suspense File (ESF).
- We separated the audit population into 3 groups:
    1. 35,236 transactions related to 20,592 numberholders who received Supplemental Security Income payments in the TY for which SSA removed SEI;
    2. 19,385 transactions related to 13,428 numberholders who received Old-Age, Survivors and Disability Insurance benefit payments in the TY for which SSA removed SEI; and
    3. 47,855 transactions related to 27,194 numberholders who did not receive SSA payments in the TY for which SSA removed SEI.
- Reviewed a random sample of 150 SEI transactions (50 from each group) removed from the MEF to:
    - identify justification provided for removing SEI,
    - determine whether SEI was deleted or suspended, and
    - determine whether SSA staff accurately followed policies when removing SEI from the MEF.
- For each sampled transaction, we reviewed available transaction documentation including Item Correction System, Online Retrieval System, Evidence Portal, Master Beneficiary Record, and Supplemental Security Record.

- Matched the Social Security numbers of the 61,214 numberholders against SSA's ESF Self-employment Reinstate File and identified 198 transactions reinstating $9,463,962 in TYs 2012 through 2019 SEI onto another numberholder's earnings record.

- Obtained 114 weekly Determination Posting Record reports SSA transmitted to the IRS from July 29, 2019 through January 31, 2022 directly from the IRS. We matched the 77 weekly Determination Posting Record reports SSA transmitted to the IRS from July 29, 2019 through April 5, 2021 to our population to determine whether SSA sent the records to the IRS.

We conducted our review between September 2021 and February 2023. We assessed the reliability of the MEF, ESF, SEI Reinstate File, and Determination Posting Record reports by conducting tests to determine the completeness and accuracy of the data primarily by tracing information in the data to SSA payment and Numident records. We determined the data used in this report were sufficiently reliable given our audit objectives and intended use of the data. The principal entities audited were the Offices of Operations and Systems under the Offices of the Deputy Commissioners for Operations and Systems.

We assessed the significance of internal controls necessary to satisfy the audit objective. This included an assessment of the five internal control components, including control environment, risk assessment, control activities, information and communication, and monitoring. In addition, we reviewed the principles of internal controls associated with the audit objective. We identified the following component and principles as significant to the audit objective:

- Component 3: Control Activities
  - Principle 10 – Design control activities
  - Principle 12 – Implement control activities

We conducted this performance audit 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.

Appendix C – AGENCY COMMENTS

SOCIAL SECURITY

MEMORANDUM

Date: September 5, 2023 Refer To: TQA-1

To: Gail S. Ennis
Inspector General

From: Scott Frey
Chief of Staff

Subject: Office of the Inspector General Draft Report "Follow-up Review of Self-employment Earnings Removed from the Master Earnings File" (**A-06-21-51020**) — INFORMATION

Thank you for the opportunity to review the draft report. Please see our detailed comments in the attached document.

Please let me know if I can be of further assistance. You may direct staff inquiries to Trae Sommer at (410) 965-9102.

Attachment

SSA COMMENTS ON THE OFFICE OF INSPECTOR GENERAL DRAFT REPORT

"FOLLOW-UP REVIEW OF SELF-EMPLOYMENT EARNINGS REMOVED FROM THE MASTER EARNINGS FILE" (A-06-21-51020)

Recommendation 1

Amend policies to clearly instruct employees to delete self-employment income (SEI), rather than transfer it to the earnings suspense file (ESF), when the numberholder under whose personal information the earnings were reported disclaims the earnings.

Response

We disagree. We cannot delete SEI without an Internal Revenue Service (IRS) action, such as granting a taxpayer request for correction. We plan to update our instructions to clarify when it is appropriate to send SEI to the ESF, when it is appropriate to delete earnings, and when technicians should contact IRS.

Recommendation 2

Take appropriate action (for example, conduct additional training, update policy and user guides, send emergency messages) to ensure employees process earnings adjustments in accordance with policy.

Response

We agree.

Recommendation 3

Delete all disclaimed SEI for tax years 2012 through 2019 that remain in the ESF unless the earnings were reported with a name that clearly differs from that on the earnings record to which they were originally posted.

Response

We disagree. There is no basis to presume that disclaimed SEI should be deleted from the ESF until IRS tells us that SEI reported on a tax return is fraudulent or otherwise requires correction. SEI is reported to IRS on tax form 1040, and Self-Employment Contribution Act tax is paid with those returns. IRS has the sole responsibility to determine whether SEI reported on a tax return is incorrect.

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