

# TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION



## **Delays Continue to Result in Businesses Not Receiving Pandemic Relief Benefits**

August 31, 2022

Report Number: 2022-46-059

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

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## HIGHLIGHTS: Delays Continue to Result in Businesses Not Receiving Pandemic Relief Benefits

Final Audit Report issued on August 31, 2022

Report Number 2022-46-059

### Why TIGTA Did This Audit

In July 2021, TIGTA issued a report on the IRS's efforts to implement employer tax credits included in the Coronavirus Disease 2019 (COVID-19) relief legislation. This report is a continuation of our review of the IRS's business tax provisions included in the legislation passed in response to the pandemic. The overall objective of this review was to assess the IRS's processes and procedures to ensure the accuracy and validity of COVID-19 related employer tax credits on original and amended tax returns.

### Impact on Tax Administration

Employers entitled to COVID-19 related employer credits that did not claim them on their original Form 941, *Employer's QUARTERLY Federal Tax Return*, or that wanted to increase the amount originally claimed filed a Form 941-X, *Adjusted Employer's QUARTERLY Federal Tax Return or Claim for Refund*, to reduce their tax liability and receive a direct payment resulting from any refundable credit amount. The timing of the various legislative provisions increased the number of Forms 941-X the IRS received from employers that wished to amend their original Form 941. As of February 1, 2022, there were 447,435 Forms 941-X waiting to be processed.

### What TIGTA Found

Continued processing delays have prevented businesses from receiving pandemic relief benefits. The IRS did not begin processing claims for qualified Sick and Family Leave Credits and the Employee Retention Credit for 12 months and claims for Social Security Tax Deferral for 16 months after the pandemic relief legislation was enacted. This was due to a lack of updated programming and procedural guidance. A lack of training, erroneously suspended claims, and a lack of prioritization of claims contributed to additional delays processing claims.

TIGTA identified additional concerns with the IRS's processes to implement retroactive termination of the Employee Retention Credit. Specifically, the IRS does not have processes to verify a recovery startup business or effective controls to deny the Employee Retention Credit for non-recovery startup businesses. To qualify as a recovery startup business, generally, an employer had to begin operations after February 15, 2020, and have annual gross receipts that did not exceed \$1 million over a certain three-taxable-year period.

In addition, amended returns with Employee Retention Credit claims were not referred to Examination for review as required. TIGTA projected that 153 out of 209 amended returns with nonrefundable employer credit claims that met the referral criteria were not referred to Examination as required resulting in \$45 million in potentially erroneous nonrefundable employer tax credits being allowed. This occurred because the IRS's internal guidance did not include processes to refer claims with significant refundable employer credits to Examination for review. In addition, tax examiners were not always referring amended returns without a refundable tax credit as required.

### What TIGTA Recommended

TIGTA made nine recommendations to the IRS, including developing plans to prioritize processing backlogged claims, updating Examination referral criteria to include Forms 941-X with refundable credit claims, and developing a systemic process to identify Forms 941-X that meet referral criteria and alerting the employee when processing the claim of the need to refer the return to Examination for review.

The IRS agreed with eight of the nine recommendations. The IRS did not agree additional training was needed for employees related to referring Forms 941-X to Examination for review. Management stated they completed subsequent reviews of completed Form 941-X claims and determined no additional training was needed. However, the IRS's subsequent reviews do not address the concerns identified in our report. Accounts Management employees cited unclear guidance and training as to why 73 percent of claims were not referred when required.



TREASURY INSPECTOR GENERAL  
FOR TAX ADMINISTRATION

## U.S. DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20024

August 31, 2022

### MEMORANDUM FOR: COMMISSIONER OF INTERNAL REVENUE

*Heather Hill*

**FROM:** Heather M. Hill  
Deputy Inspector General for Audit

**SUBJECT:** Final Audit Report – Delays Continue to Result in Businesses Not  
Receiving Pandemic Relief Benefits (Audit # 202140623)

This report presents the results of our review to assess the Internal Revenue Service's processes and procedures to ensure the accuracy and validity of Coronavirus Disease 2019 related employer tax credits on original and amended tax returns. This review was part of our Fiscal Year 2021 Annual Audit Plan and addresses the major management and performance challenges of *Responding to the COVID-19 Pandemic* and *Implementing Tax Law Changes*.

Management's complete response to the draft report is included as Appendix III.

Copies of this report are also being sent to the Internal Revenue Service managers affected by the report recommendations. If you have any questions, please contact me or Diana M. Tengesdal, Acting Assistant Inspector General for Audit (Returns Processing and Account Services).

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## **Background**

On March 18 and March 27, 2020, respectively, the President signed into law the *Families First Coronavirus Response Act* (FFCRA)<sup>1</sup> and *Coronavirus Aid, Relief, and Economic Security (CARES) Act*.<sup>2</sup> Provisions contained in the FFCRA and CARES Act provide businesses impacted by the Coronavirus Disease 2019 (COVID-19) pandemic with three new employer tax credits – the Sick Leave Credit, the Family Leave Credit, and the Employee Retention Credit (ERC). The employer tax credits apply to employee retention wages paid between March 13, 2020, and June 30, 2021, and wages paid for periods of leave between April 1, 2020, and March 31, 2021.

In addition, the CARES Act also provided employers with the ability to defer payment of their portion of the Social Security tax. Employers and self-employed individuals deferring the employer share of the Social Security tax generally must repay half the deferral by December 31, 2021, and the other half by December 31, 2022.

### **The FFCRA**

The FFCRA provided refundable tax credits<sup>3</sup> to employers with fewer than 500 employees that reimburse them, dollar for dollar, for the cost of providing paid sick and family leave wages to their employees for leave related to COVID-19. Full-time employees may receive up to 80 hours of paid sick leave to care for their own health needs or to care for other family members. Also, the employee may receive up to 10 weeks of paid family leave to care for a child whose school or place of care is closed or whose child care provider is unavailable due to COVID-19 precautions. Certain self-employed individuals in similar circumstances are entitled to similar credits.

To qualify for the Sick and Family Leave Credits, employers must be a nongovernmental entity<sup>4</sup> and provide and pay qualified sick or family leave wages, defined in the FFCRA, for periods of leave between April 1, 2020, and March 31, 2021. Specifically, an eligible employer that pays qualified leave wages to its employees in a calendar quarter before it is required to deposit Federal employment taxes with the Internal Revenue Service (IRS) for that quarter may reduce the amount of Federal employment taxes that it deposits by the amount of the qualified leave wages paid. The eligible employer must account for the reduction in deposits on Form 941, *Employer's QUARTERLY Federal Tax Return*. However, if there are insufficient Federal employment taxes to cover the amount of the credits, an eligible employer may request an advance payment of the credits from the IRS. Figure 1 provides the requirements that need to be met to claim the Sick and Family Leave Credits.

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<sup>1</sup> Pub. L. No. 116-127, 134 Stat. 178 (codified in scattered sections of 7, 26, 29, and 41 U.S.C.), as amended by the *COVID-Related Tax Relief Act of 2020*, Pub. L. No. 116-260, div. N, 134 Stat. 1182, 1964, and the *Taxpayer Certainty and Disaster Tax Relief Act of 2020*, Pub. L. No. 116-260, div. EE, 134 Stat. 1182, 3051 (2020).

<sup>2</sup> Pub. L. No. 116-136, 134 Stat. 281 (codified as amended in scattered sections of 2, 5, 12, 15, 20, 21, 29, 42, and 45 U.S.C.), as amended by the *COVID-Related Tax Relief Act of 2020* and the *Taxpayer Certainty and Disaster Tax Relief Act of 2020* (2020).

<sup>3</sup> A refundable credit is a credit to reduce a tax liability. If the tax liability is reduced to zero and a credit remains, it is eligible to be refunded to the taxpayer.

<sup>4</sup> Certain tribal governments may also claim the credit.

**Figure 1: Requirements for the Sick and Family Leave Credits**

Sick Leave Credit	Family Leave Credit
Qualified wages are limited to 80 hours or 10 days paid to an employee at the employee's regular rate, or if higher, the Federal minimum wage or any applicable State or local minimum wages, up to \$511 per day for the individual. An employee caring for someone is eligible at two-thirds of the employee's regular rate of pay, or applicable minimum wages, up to \$200 per day.	Qualified wages are limited to two-thirds of the employee's regular rate of pay up to \$200 per day per employee for up to 10 weeks or 50 days of qualified wages paid to an employee who is unable to work.
The maximum credit allowed per employee is \$5,110 plus the amount of allocable health plan expenses and the amount of the eligible employer's share of Medicare tax imposed on the qualified sick leave wages.	The maximum credit allowed per employee is approximately \$10,000 plus the amount of allocable health plan expenses and the amount of the eligible employer's share of Medicare tax imposed on the qualified family leave wages.
Employee must be subjected to Federal, State, or local government isolation order, requested to self-quarantine, experiencing symptoms and seeking a diagnosis, caring for an individual in isolation or self-quarantine, or caring for a child if the school or place of care is closed or is unavailable due to COVID-19.	Employee must be employed for at least 30 calendar days prior to the start of the leave and unable to work/telework due to the need to care for a child because their school or place of care has been closed or is unavailable due to COVID-19.

*Source: Summary of requirements in the FFCRA.*

## The CARES Act

The CARES Act encourages eligible employers to keep employees on their payroll despite experiencing economic hardship related to COVID-19. As such, the CARES Act created the ERC, which is a refundable credit against employment taxes. The ERC is equal to 50 percent of qualified wages paid (including allocable qualified health plan expenses) between March 13, 2020, and December 31, 2020. Additional legislation passed in December 2020 and March 2021 increased the credit to 70 percent of qualified wages paid between January 1, 2021, and December 31, 2021.<sup>5</sup> Certain government entities are not eligible for this credit,<sup>6</sup> and self-employed individuals are not eligible for this credit with respect to their own self-employment earnings.

To be eligible for the credit, employers must have had a trade or business during Calendar Year 2020 or during the calendar quarter for which they are claiming the credit in Calendar Year 2021 and either fully or partially suspended operations due to orders from an appropriate governmental authority limiting commerce, travel, or group meetings due to COVID-19 or

<sup>5</sup> The *Taxpayer Certainty and Disaster Tax Relief Act of 2020* and the *American Rescue Plan Act of 2021*, Pub. L. No. 117-2 (2021).

<sup>6</sup> No government entity is eligible for this credit with respect to wages paid between March 13, 2020, and December 31, 2020.

experienced a decline in gross receipts during the calendar quarter. For Tax Year 2020, the maximum amount of qualified wages taken into account with respect to each employee for all calendar quarters is \$10,000, so the maximum credit for an eligible employer for qualified wages paid to any employee is \$5,000. For Tax Year 2021, the maximum amount of qualified wages taken into account with respect to each employee for all calendar quarters is \$10,000 per quarter, so the maximum credit for an eligible employer for qualified wages paid to any employee is \$7,000 per quarter.<sup>7</sup> An eligible employer that pays qualified wages to its employees in a calendar quarter before it is required to deposit Federal employment taxes with the IRS may reduce the amount of Federal employment taxes by the amount of the ERC it plans to claim. However, if there are insufficient Federal employment taxes to cover the amount of the credit, an eligible employer may request an advance payment of the credit from the IRS.

**The CARES Act allows employers and self-employed individuals to defer the payment of their employer share of Social Security tax over the next two years.**

Generally, half of the deferral is required to be repaid by December 31, 2021, and the other half is due by December 31, 2022. On August 8, 2020, the President issued a Presidential Memorandum<sup>8</sup> directing the Secretary of the Treasury to expand the deferral to also include the employee's portion of Social Security tax.<sup>9</sup> Pursuant to Notice 2020-65, *Relief With Respect to Employment Tax Deadlines Applicable to Employers Affected by the Ongoing Coronavirus (COVID-19) Disease 2019 Pandemic*, employers could elect to defer payment and withholding of the employee portion of Social Security tax between September 1 and December 31, 2020, for employees with biweekly pay that was less than \$4,000. Under Notice 2020-65, the due date for withholding and paying the deferred tax was extended to April 30, 2021.<sup>10</sup> Therefore, as of September 1, 2020, many employers could defer 100 percent of Social Security tax.

As of February 25, 2021, we identified 152,739 employers that deferred approximately \$97.1 billion in Social Security tax. As mentioned previously, this amount will need to be fully repaid by December 31, 2022.<sup>11</sup> We have a separate review of the Social Security tax deferral repayment process,<sup>12</sup> which will focus on the IRS's processes and procedures to ensure accurate and timely repayment of the deferred payments.

**Subsequent legislation modified provisions of the FFCRA and the CARES Act**

On December 27, 2020, the President signed into law the *Taxpayer Certainty and Disaster Tax Relief Act of 2020* and the *COVID-Related Tax Relief Act of 2020*, which made changes to the

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<sup>7</sup> The *American Rescue Plan Act of 2021* modified the ERC for the third and fourth quarters of Tax Year 2021, which will impact the maximum credit amount for some taxpayers.

<sup>8</sup> Federal Register, Vol. 85, No. 157, pp. 49587–49588, *Deferring Payroll Tax Obligations in Light of the Ongoing COVID-19 Disaster* (August 13, 2020).

<sup>9</sup> The IRS's authority was established in the issuance of Notice 2020-65, *Relief With Respect to Employment Tax Deadlines Applicable to Employers Affected by the Ongoing Coronavirus (COVID-19) Disease 2019 Pandemic* (August 2020).

<sup>10</sup> Notice 2021-11, *Additional Relief With Respect to Employment Tax Deadlines Applicable to Employers Affected by the Ongoing Coronavirus (COVID-19) Disease 2019 Pandemic* (January 2021), made changes to Notice 2020-65 to extend the payment period to December 31, 2021.

<sup>11</sup> This amount includes the employee portion of Social Security tax due by December 31, 2021.

<sup>12</sup> Treasury Inspector General for Tax Administration (TIGTA), Audit No. 202240623, *Review of Social Security Tax Deferral Repayment*.



new employer tax credits created in the FFCRA and the CARES Act passed in March 2020. Employers are eligible to continue to claim the Sick and Family Leave Credits for wages paid for leave taken through March 31, 2021, and the ERC through June 30, 2021. The new legislation also retroactively clarified language in the FFCRA and the CARES Act. For example, the legislation clarified the treatment of group health plan expenses for purposes of the ERC. Further, the legislation retroactively modified the limitation that employers who received a Paycheck Protection Program<sup>13</sup> loan could not also receive the ERC, thus allowing employers to both receive the loan and claim the credit under certain conditions, but not for the same wages. Additionally, the new legislation extended the due date for employers to repay the employee share of the Social Security tax deferral from April 30, 2021, to December 31, 2021.

On March 11, 2021, the President signed into law the *American Rescue Plan Act*,<sup>14</sup> which provided employer tax credits similar to those provided by the FFCRA and the CARES Act. Employers<sup>15</sup> are now eligible to continue to claim the Sick and Family Leave Credits for periods of leave provided through September 30, 2021, and the ERC through December 31, 2021.

On November 15, 2021, the President signed into law the *Infrastructure Investment and Jobs Act*,<sup>16</sup> which limited the availability of the ERC only to wages paid before October 1, 2021, unless the employer is a recovery startup business (RSB). Businesses that were not a RSB were no longer eligible for the credit for wages paid after September 30, 2021. Because of the retroactive termination, some businesses no longer eligible to claim the credit may have already reduced their employment tax deposits in anticipation of claiming the credit for the fourth quarter of 2021.

### **Implementation of Tax Year 2020 employer tax credits enacted in response to the COVID-19 pandemic**

In July 2021, we issued a report on the IRS's efforts to implement employer tax credits included in relief legislation.<sup>17</sup> We reported that the IRS did not have adequate time after the pandemic relief legislation was passed to make significant programming changes because the tax return filing season was already underway and Forms 941 were being processed when the legislation was enacted. As such, validations were not performed during tax return processing to identify potentially erroneous or fraudulent employer tax credits claimed on employment tax returns. In addition, we reported that ineligible entities were allowed to claim the COVID-19 employer tax credits in error. Specifically, we reported that 113 ineligible government entities received erroneous employer tax credits totaling \$2 million.

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<sup>13</sup> The CARES Act established the Paycheck Protection Program to help businesses retain their employees by offering potentially forgivable loans from Small Business Administration lenders for use to meet payroll needs and other business expenses.

<sup>14</sup> Pub. L. No. 117-2 (2021).

<sup>15</sup> Employers now include governmental employers except the Government of the United States or any agency or instrumentality thereof that is not an organization described in I.R.C. § 501(c)(1).

<sup>16</sup> Pub. L. No. 117-58 (2021).

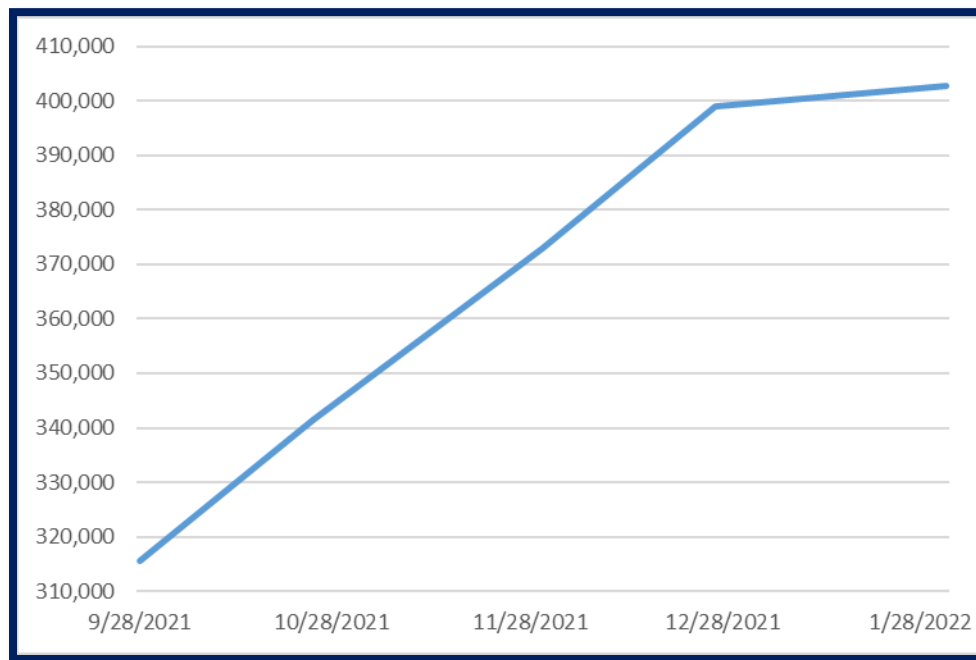
<sup>17</sup> TIGTA, Report No. 2021-46-043, *Implementation of Tax Year 2020 Employer Tax Credits Enacted in Response to the COVID-19 Pandemic* (July 2021).



## Results of Review

This report is a continuation of our review of the IRS's business tax provisions included in the legislation enacted in response to the COVID-19 pandemic. The timing of the various legislative provisions increased the number of Forms 941-X, *Adjusted Employer's QUARTERLY Federal Tax Return or Claim for Refund*, filed by employers to amend their original Form 941. Employers entitled to COVID-19 related employer credits that did not claim them on their original Form 941 or that wanted to increase the amount originally claimed filed a Form 941-X to reduce their tax liability and receive a direct payment resulting from any refundable credit amount. However, we found that ongoing and considerable delays in the processing of amended Forms 941 filed by businesses resulted in businesses not timely receiving the immediate financial relief for which this legislation was enacted. As of February 1, 2022, there were 447,435 Forms 941-X waiting to be processed. Over 90 percent (402,814) of these Forms 941-X were over-aged, *i.e.*, have not been processed within 45 calendar days. In addition, 60,885 (13.6 percent) of the Forms 941-X were not processed within 180 calendar days. Figure 2 shows that there was a steady increase in the number of over-aged cases received with COVID-19 related employer credits.

**Figure 2: Forms 941-X Over-Aged Inventory Through February 1, 2022**



Source: Treasury Inspector General for Tax Administration (TIGTA) analysis of the IRS's Standard Aged Reports.

In contrast, Figure 3 shows that the IRS was not closing over-aged cases at the same pace as the cases were received until January 2022.

**Figure 3: Forms 941-X Over-Aged Inventory Closed Through February 1, 2022**



*Source: TIGTA analysis of the IRS's Standard Weekly Closure Reports.*

The IRS took corrective actions to identify and prevent potentially fraudulent employer tax credits claimed on Forms 941 in response to the concerns raised in our July 2021 report.<sup>18</sup> These actions included:

- Updated an identity theft fraud filter, previously implemented in September 2020, to identify during processing suspicious Forms 941 with employer tax credit claims meeting certain criteria. As of March 10, 2022, the IRS had identified 11,096 returns with more than \$2 trillion in credits claimed. In addition, in April 2022, the IRS implemented new processes to identify potentially fraudulent claims by businesses with questionable characteristics.
- Implemented processes and procedures to identify erroneous employer tax credit claims associated with ineligible government entities. Specifically, the IRS identified returns filed by employers claiming COVID-19 related business credits over a specific threshold amount and with employment codes indicating the employer is a government entity. Once potentially ineligible government entities are identified, the Employer Identification Numbers (EIN)<sup>19</sup> are sent to the Tax Exempt and Government Entities function for validation. If determined to be ineligible, the IRS reverses the credits. Using this process, the IRS identified 7,400 ineligible government entities and reversed credits totaling \$124 million as of March 2022.

<sup>18</sup> TIGTA, Report No. 2021-46-043, *Implementation of Tax Year 2020 Employer Tax Credits Enacted in Response to the COVID-19 Pandemic* (July 2021).

<sup>19</sup> A unique nine-digit number used to identify a taxpayer's business account.

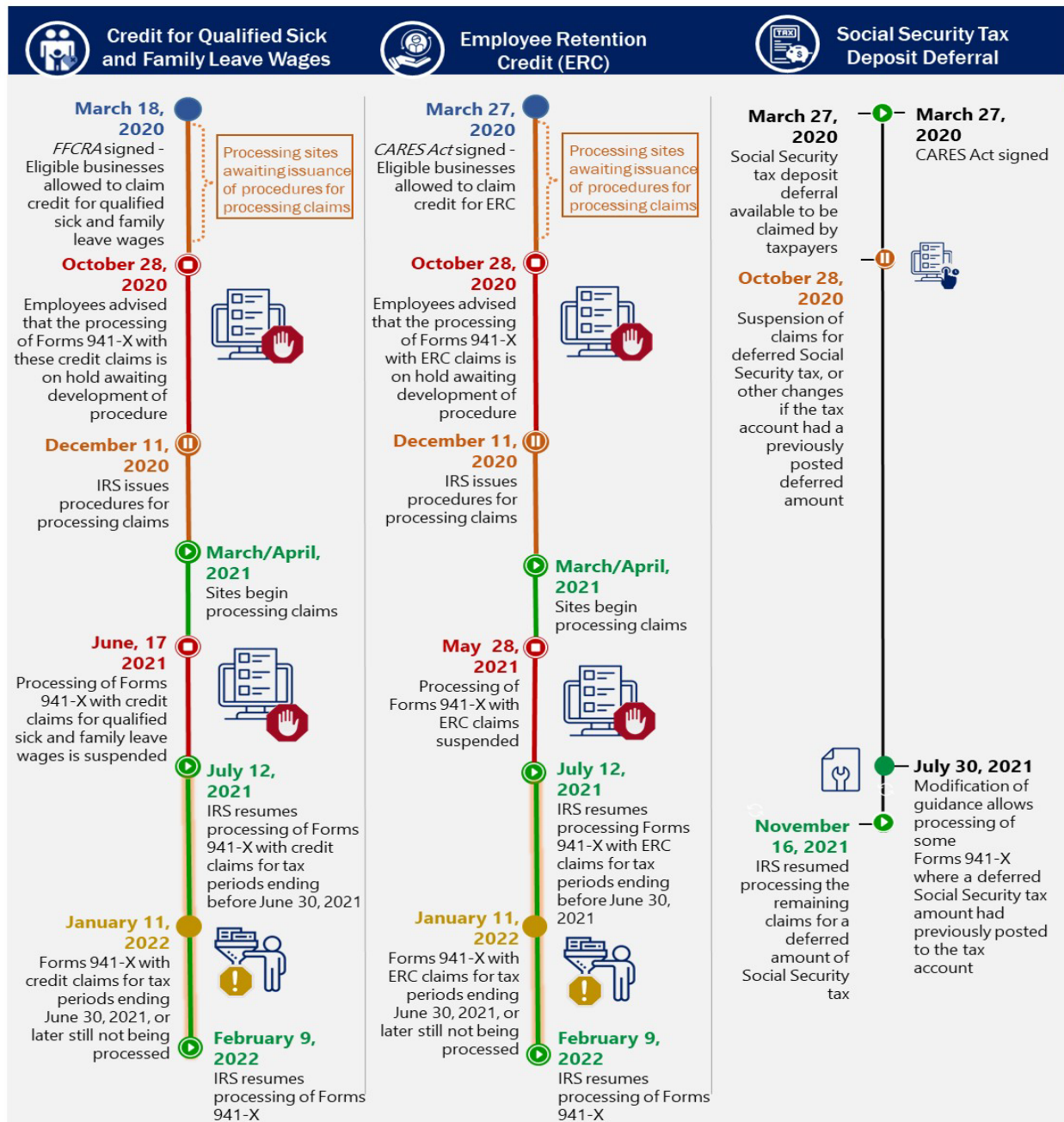
While the IRS's corrective actions improved the detection of potentially fraudulent employer tax credits claimed on Forms 941, additional actions are needed to better identify and address potentially erroneous refunds.

### **Due to Continued Processing Delays, Many Businesses Have Not Yet Received Pandemic Relief Benefits**

The IRS did not immediately begin processing Forms 941-X with pandemic relief claims. Figure 4 shows that the IRS did not begin processing amended returns reporting qualified Sick and Family Leave Credits and the ERC for 12 months after the pandemic relief legislation was enacted. The IRS did not begin processing amended returns reporting changes to Social Security tax deferral for 16 months.

**Delays Continue to Result in Businesses  
Not Receiving Pandemic Relief Benefits**

**Figure 4: IRS Amended Return Processing Timelines for Pandemic Relief**



Source: TIGTA summary of Servicewide Electronic Research Program Alerts related to amended returns requesting pandemic relief.

Figure 5 provides the volumes of claims the IRS had in its suspended inventory, *i.e.*, claims being held, while the IRS continued to delay processing Forms 941-X with pandemic relief claims.

**Figure 5: Number of Suspended  
Amended Employment Tax Returns**

Date	Number of Claims Suspended		
	Social Security Tax Deposit Deferral	Qualified Sick and Family Leave Credits and the ERCs	Total CARES Act Credits
May 29, 2021	4,537	2,806	7,343
June 19, 2021	5,831	2,681	8,512
July 17, 2021	6,155	7,153	13,308
November 20, 2021	12,831	31,855	44,686

*Source: IRS-provided inventory data for the ERC, Sick and Family Leave Credits, and Social Security tax deposit deferrals.*

We notified IRS management twice during this review of our concerns with actions taken on the part of management to assist businesses in the processing of their claims for qualified Sick and Family Leave Credits, the ERC, and deferred Social Security taxes. For example:

- On June 21, 2021, we notified IRS management of our concerns regarding the IRS's suspension of processing of all Forms 941-X with claims for COVID-19 related employer credits after processing claims for only two months after a 12-month delay. IRS management stated that the delays in processing Forms 941-X with claims for COVID-19 related employer credits were attributable to development of processing procedures as well as programming issues associated with processing claim adjustments. However, we do not agree that the legislative changes would justify a delay of more than eight months to update the internal guidelines and more than 15 months to update programming to process the claims with employer credits on Forms 941-X. The IRS was able to process employer credits claimed on Forms 941 and advanced tax credits claimed on Forms 7200, *Advance Payment of Employer Credits Due to COVID-19*, without an extended delay.
- On February 2, 2022, we notified IRS management of our concerns regarding the continued delay of processing Forms 941-X with claims for COVID-19 related employer credits, and management stated the delay was due to a lack of procedural guidance for claims received for tax periods ending June 30, 2021, and later. Specifically, management noted that it was "difficult to engage in delivering multiple complex procedural updates simultaneously, or in close chronological proximity, particularly if they are intricately related to existing guidance or guidance that is in flux." Although the IRS was tasked to update its processes several times to accommodate claims received due to legislative changes, we do not agree that the changes warrant a significant delay in processing.

In response to the explanation provided by management, we requested information supporting management's claim of significant processing differences between COVID-19 related employer credits reported on Forms 941-X for tax periods ending before June 30, 2021, and those claims received for tax periods ending June 30, 2021, and later. According to IRS management, coordination was required with various functions to

ensure comprehensive implementation of the legislative changes. IRS management also noted the changes in the law were complex, the handling was complex, and new handling must be layered onto previous handling that had already vastly increased in complexity since the beginning of 2020. For example, the IRS cited 11 new tracking numbers to record changes to the accounts. As noted previously, we do not agree that the differences between employer credits for tax periods ending June 30, 2021, and after and credits for tax periods ending before June 30, 2021, justified the significant additional processing delays.

### **Steps were not immediately taken to prioritize backlogs of suspended Form 941-X claims**

The IRS did not take immediate steps to prioritize Form 941-X claims that were suspended. As noted previously, the IRS resumed processing Forms 941-X with claims for COVID-19 related employer credits in July 2021 after several delays. However, IRS management did not begin its weekly calls to engage Headquarters and processing sites to make COVID-19 business credit cases priority work until August 2021. The IRS did not begin tracking the processing of amended employment tax returns with COVID-19 related employer credits until September 2021. As such, the IRS did not begin prioritizing amended employment tax returns with COVID-19 related employer credits or tracking the processing of the backlog of suspended Forms 941-X for eight months after procedures to process the amended employment tax returns were available. As of January 29, 2022, the IRS reported having 27,790 Form 941-X claims previously suspended that need to be processed.

According to IRS management, additional steps were taken to address the backlog of suspended Forms 941-X after it began processing the suspended Forms 941-X. For example, IRS management stated that training was provided to more than 600 customer service representatives in the Accounts Management function to work COVID-19 related employer credit claims and 125 customer service representatives to work deferrals of Social Security tax claims while they are working paper cases. However, as we reported in March 2022,<sup>20</sup> many Accounts Management employees split their time between working Accounts Management cases and answering IRS toll-free telephone calls, and a dedicated staff to work Accounts Management inventory is needed to address the ongoing challenge. As such, training additional staff may not immediately impact the over-aged inventory or give any priority to the backlogged amended employment tax returns.

Over-aged Accounts Management inventory has been an ongoing challenge for the IRS. The COVID-19 pandemic and recent pandemic-related tax law changes have further exacerbated the over-aged inventory.<sup>21</sup> Providing training alone is not sufficient to address the ongoing backlog of over-aged inventory.

COVID-19 related employer credit claims were intended to provide relief to businesses that have been impacted by COVID-19. The delay in processing Forms 941-X and the significant backlog prevented businesses from timely receiving the monetary benefits intended by the FFCRA and the CARES Act to provide immediate relief to employers. In addition, processing delays could result in unnecessary interest paid by the IRS when the claims were processed.

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<sup>20</sup> TIGTA, Report No. 2022-46-027, *Program and Organizational Changes Are Needed to Address the Continued Inadequate Tax Account Assistance Provided to Taxpayers* (Mar. 2022).

<sup>21</sup> TIGTA, Report No. 2021-40-038, *Interim Results of the 2021 Filing Season* (May 2021).



In addition to the causes that IRS management cited for significant delays in processing COVID-19 related employer credit claims, we found that the following contributed to these delays:

- ***Lack of trained staff caused additional delays to processing COVID-19 related employer credits.*** The IRS issued procedures to process Forms 941-X with claims for qualified Sick and Family Leave Credits and the ERC on December 11, 2020. However, the IRS did not provide training for its employees to process these claims until March and April 2021. As such, the IRS could not begin processing these claims at either the Cincinnati or Ogden sites due to a lack of training until the end of April 2021 contributing to the significant backlog of unprocessed Forms 941-X with COVID-19 related employer credit claims. The IRS subsequently ceased processing claims again in May and June of 2021 due to programming issues identified. The IRS did not continuously process claims until July 2021 at which point it had more than 13,300 amended employment tax returns in inventory waiting to be processed.
- ***Erroneously suspended Forms 941-X with COVID-19 related employer credit claims.*** On October 28, 2020, the IRS issued guidance to suspend processing of Forms 941-X with an adjustment to the amount of deferred Social Security tax or if the tax account had a previously posted deferred Social Security tax amount. IRS management stated that they needed to suspend the processing of these amended employment tax returns because of “technical and administrative complexities” associated with claims of deferred Social Security tax. Specifically, IRS management attributed it to the lack of procedures and programming in place to ensure that amended employment tax returns are processed accurately.

Our review of a statistically valid sample<sup>22</sup> of 74 Forms 941-X included in the suspense inventory found that 24 (32 percent) of the amended employment tax returns were suspended erroneously. These amended employment tax returns should not have been suspended because they did not meet the IRS’s criteria to suspend the claim. Specifically, these amended employment tax returns did not include an adjustment to the amount of deferred Social Security tax or meet the exception criteria for processing. These 24 Forms 941-X also had an average age of 201 days in inventory or more than six months. Based on the results of our statistically valid sample, we project that 4,001<sup>23</sup> of the 12,337 amended employment tax returns in the suspense inventory were suspended erroneously.

**Recommendation 1 (E-Mail Alert):** On November 22, 2021, we notified the Director, Customer Account Services, Wage and Investment Division, that IRS employees were erroneously suspending Forms 941-X when the amended employment tax return did not include an adjustment to the amount of deferred Social Security tax. We recommended that the Accounts Management function immediately review the Forms 941-X that are identified in the suspense

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<sup>22</sup> We selected a statistical sample using a confidence level of 90 percent, an expected error rate of 5 percent, and a precision factor of  $\pm 5$  percent.

<sup>23</sup> The point estimate projection is based on a two-sided 90 percent confidence interval. We are 90 percent confident that the actual total amount is between 2,899 and 5,237.



inventory as an adjustment to the amount of deferred Social Security tax to ensure that they are categorized properly.

**Management's Response to Alert:** IRS management agreed that the majority of the amended employment tax returns TIGTA identified were erroneously suspended. IRS management implemented additional reviews of suspended inventory to evaluate whether the cases were correctly suspended. Random sample reviews of the unworkable lists continue to be conducted at the Accounts Management sites to determine if cases controlled there are workable, and if so, reassign them accordingly. As of July 8, 2022, management determined that they have 76,079 Form 941-X claims suspended that need to be processed.

- ***Lack of prioritization resulted in a delay processing 96 percent of tentative refund claims.*** The IRS did not process claims for tentative refunds within 45 days. Our review of the IRS's inventory of tentative refund claims on the Form 1139, *Corporation Application for Tentative Refund*, found that 8,229 (96 percent) of the 8,613 tentative carryback claims in inventory as of January 29, 2022, were over-aged. Although the IRS has implemented plans to reduce the backlog, such as shifting Accounts Management employees away from answering telephones to working paper returns, authorizing overtime, and increasing inventory levels for trained employees, the IRS has not prioritized the processing of tentative refund claims and does not have a specific plan to address the backlog.

**Recommendation 2:** The Commissioner, Wage and Investment Division, should evaluate the current inventory of backlogged claims related to pandemic relief and develop specific plans to prioritize claims and develop timelines to process backlogged claims.

**Management's Response:** The IRS agreed with this recommendation and has continued its efforts to reduce the inventory increases from the pandemic. Those efforts included increased staffing with overtime and 100 percent of the campus employees' time focused on paper inventory. Through June 25, 2022, these actions have reduced the inventory of the Form 1139 carrybacks to under 1,100 applications.

## **Processes Are Needed to Address Legislative Changes Affecting the Employee Retention Credit**

On November 15, 2021, the President signed into law the *Infrastructure Investment and Jobs Act*,<sup>24</sup> which limited the availability of the ERC only to wages paid before October 1, 2021, unless the employer is an RSB.<sup>25</sup> As such, all businesses that were not RSBs became ineligible for the credit for wages paid after September 30, 2021. Our review of the IRS's processes to implement these retroactive changes to the ERC identified the following concerns:

<sup>24</sup> Pub. L. No. 117-58 (2021).

<sup>25</sup> An RSB is defined in I.R.C. § 3134(c)(5) as an employer that began carrying on any trade or business after February 15, 2020, for which the average gross receipts of the employer for the three-taxable-year period ending with the taxable year before the quarter the credit is determined does not exceed \$1 million and is not otherwise an eligible employer due to the full or partial suspension of operations or a decline in gross receipts.

- ***The IRS does not have processes to verify whether a business claiming the ERC is in fact an RSB.*** According to IRS management, the IRS will rely on the taxpayer's attestation on the employment tax return **signed under penalties of perjury**, at filing, that the business is eligible for the ERC solely because the business is an RSB. Our analysis of Forms 941 received for the third quarter of Tax Year 2021 as of January 31, 2022, identified 928 business entities, claiming nearly \$17.5 million in refundable ERCs, which had an EIN issued **before** February 15, 2020.<sup>26</sup> As such, these business might not qualify as an RSB. Furthermore, our analysis of fourth quarter Forms 941 as of February 16, 2022, identified 26 businesses that attested under penalties of perjury that they were an RSB *but did not identify as an RSB on their third quarter Form 941*.

When we shared our results with IRS management, they noted that an examination may be necessary to determine whether a business qualifies as an RSB and therefore qualifies for the ERC. According to IRS management, factors such as changes in gross receipts or a partial or full suspension of operations could result in a business qualifying as an RSB in one quarter, but not another. We agree that an RSB determination would likely need to be reviewed in a post-processing compliance environment. However, the IRS has not developed processes to identify specific claims to be selected for an examination.

- ***The IRS does not have effective controls to deny the ERC for non-RSBs.*** The IRS did not properly deny the ERC for businesses that did not identify as an RSB. According to IRS management, in December 2021, programming was implemented to allow only businesses that indicated that they are an RSB on the Form 941 to claim the ERC. However, our analysis of Forms 941 submitted for fourth quarter Tax Year 2021 as of February 2, 2022, identified 920 businesses that received nearly \$12.6 million in the ERCs when there was no indication that the business was an RSB. When we shared our results with the IRS, it noted that electronically filed Forms 941 are not accepted until the tax period ends thereby preventing non-RSB filers from submitting pre-legislation change forms. However, paper-filed returns are accepted and processed at any time within a quarter. Therefore, Forms 941 submitted on paper for fourth quarter Tax Year 2021 could have been processed before the programming was implemented that prevented claims of the ERC without the RSB box checked. The IRS has developed an examination workstream to address Forms 941 that have already been processed. This workstream is scheduled to begin in summer 2022.

**Recommendation 3:** The Commissioner, Wage and Investment Division, should review the 928 business entities identified that do not appear to qualify as an RSB and take actions needed to recover the ERCs that are determined to be erroneous.

**Management's Response:** The IRS agreed with this recommendation and plans to review the 928 returns to identify the returns exceeding its thresholds. IRS management also plans to determine if other noncompliance indicators are present and take compliance action if warranted of those that exceed the thresholds.

**Recommendation 4:** The Commissioner, Small Business/Self-Employed Division, should identify all fourth quarter Tax Year 2021 paper-filed Forms 941 processed prior to when the programming was implemented and identify amended employment tax returns receiving the

<sup>26</sup> The instructions for Form 941 list one of the basic requirements to be considered an RSB is the employer had to have begun to carry on a trade or business after February 15, 2020.

ERC for which there was no indication that the business was an RSB and take actions needed to recover the ERCs that are determined to be erroneous.

**Management's Response:** The IRS agreed with this recommendation. IRS management also identified this issue on February 24, 2022, independent of TIGTA's audit. Management began development of a process to identify and address this issue and plans to finalize and implement the process once completed.

### **Amended Returns With Employee Retention Credit Claims Were Not Referred to Examination for Review As Required**

Our review identified that some returns with ERC claims were not referred to Examination as required. During our review, we determined that the IRS's internal guidance did not include processes to refer amended employment tax returns with significant refundable employer credit claims to Examination for review.

Accounts Management employees are required to refer certain Forms 941-X to Examination during processing. This process is in place in an effort to identify potentially fraudulent claims prior to refund issuance. However, the referral criteria only related to nonrefundable employer credits and was not updated to include Forms 941-X that resulted in a material refundable employer credit. As such, refundable credit claims were not being referred because they are considered not to result in a decrease to tax. We notified IRS management of this inconsistency on May 13, 2021.

**Recommendation 5 (E-Mail Alert):** On May 13, 2021, we notified the Director, Examination, Small Business/Self-Employed Division, about the inconsistent referral criteria and recommended that the IRS update referral criteria to include Forms 941-X with refundable credits.

**Management's Response to Alert:** The IRS agreed with our recommendation. On July 22, 2021, the IRS updated its referral criteria to include Forms 941-X with refundable credits. IRS management also subsequently monitored quality reports to ensure correct referrals to Examination.

In addition, we determined that tax examiners were not referring some returns with only nonrefundable employer credit claims that met initial criteria. Specifically, our review identified 209 Forms 941-X processed as of July 28, 2021, that met the referral criteria. We reviewed a statistically valid sample<sup>27</sup> of 56 Forms 941-X and found that 41 (73 percent) were not referred to Examination. These 41 Forms 941-X contained nonrefundable COVID-19 related employer credit claims totaling more than \$12 million. Based on the results of our statistically valid sample, we project that 153<sup>28</sup> of the 209 amended returns were not referred as required resulting in \$45 million in potentially erroneous nonrefundable employer tax credits being allowed. We notified IRS management on November 23, 2021. IRS management issued a

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<sup>27</sup> We selected a statistical sample using a confidence level of 90 percent, an expected error rate of 5 percent, and a precision factor of  $\pm 5$  percent.

<sup>28</sup> The point estimate projection is based on a two-sided 90 percent confidence interval. We are 90 percent confident that the actual total amount is between 133 and 170.

Service-wide reminder to its employees on December 1, 2021, to follow the CAT-A<sup>29</sup> referral criteria.

**Recommendation 6 (E-Mail Alert):** On November 23, 2021, we alerted the Director, Customer Account Services, Wage and Investment Division, that Forms 941-X were not being referred to Examination as required and recommended that the Accounts Management function provide additional guidance to its employees to reinforce established CAT-A referral criteria.

**Management's Response to Alert:** IRS management agreed and issued a Servicewide Electronic Research Program alert on December 1, 2021, reminding employees to follow the CAT-A referral criteria.

**Recommendation 7:** The Commissioner, Wage and Investment Division, should review the 41 Form 941-X claims identified with a nonrefundable COVID-19 related employer credit that meet CAT-A referral criteria and take actions needed to recover credits that are determined to be erroneous.

**Management's Response:** The IRS agreed with this recommendation and plans to review the cases and take appropriate action.

We interviewed a judgmental sample<sup>30</sup> of seven Accounts Management employees associated with the 41 returns that were not referred as required. According to the seven employees we contacted, amended employment tax returns were not referred due to the following reasons:

- Employees stated that they “just forgot” to refer the cases to Examination.
- Unclear guidance and training.
- Multiple changes to guidance.

As such, the issuance of a reminder may not be sufficient to address the unclear guidance and training.

The Commissioner, Wage and Investment Division, should:

**Recommendation 8:** Provide additional training to employees as it relates to referring Forms 941-X to Examination for review.

**Management's Response:** The IRS disagreed with this recommendation. IRS management stated that they completed subsequent reviews of completed Form 941-X claims and determined no additional training was needed.

**Office of Audit Comment:** The IRS's subsequent reviews do not address the concerns identified in our report. As previously stated, Accounts Management employees cited unclear guidance and training as reasons why 73 percent of the Form 941-X claims we reviewed were not referred to Examination as required. Further, IRS management noted in its response that 2,484 COVID-19

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<sup>29</sup> The CAT-A is the IRS's examination criteria.

<sup>30</sup> A judgmental sample is a nonprobability sample, the results of which cannot be used to project to the population.

**Delays Continue to Result in Businesses  
Not Receiving Pandemic Relief Benefits**

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Forms 941-X claims have yet to be processed as of August 1, 2022. As such, we continue to believe that additional training is warranted.

**Recommendation 9:** Submit a request for the development of a systemic process to identify Form 941-X claims that meet referral criteria and alert the Accounts Management employee when processing these claims of the need to refer the return to Examination.

**Management's Response:** The IRS agreed with this recommendation and plans to determine the feasibility of a systemic process and submit the necessary requests, if warranted.

## **Appendix I**

### **Detailed Objective, Scope, and Methodology**

The overall objective of this audit was to assess the IRS's processes and procedures to ensure the accuracy and validity of COVID-19 related employer tax credits on original and amended tax returns. To accomplish our objective, we:

- Reviewed guidance provided to Accounts Management in Servicewide Electronic Research Program Alerts, Internal Revenue Manual Procedural Updates, *etc.* related to processing Forms 941-X with COVID-19 related employer credits to determine whether accurate and timely information was provided.
- Identified the number of Forms 941-X with COVID-19 related business credits in Accounts Management's current inventory, including those still suspended due to a lack of Accounts Management processing procedures and determined the average age of the current inventory and suspended cases. We reviewed a statistically valid random sample of 74 Forms 941-X out of a total population of 12,337 with COVID-19 related employer credits in the suspense inventory to determine whether the claims were accurately suspended. We reviewed a statistically valid sample in order to project our results. Our sample was based on a confidence level of 90 percent, an expected error rate of 5 percent, and a precision factor of  $\pm 5$  percent. Our contracted statistician assisted with developing sampling plans and projections.
- Evaluated the IRS's processes to implement retroactive changes to the ERC that limited the ERC to the RSBs in the fourth quarter of Calendar Year 2021.
- Assessed the IRS's processes to ensure the accuracy of processing Forms 941-X with COVID-19 related employer credit claims on Forms 941-X, *i.e.*, referral of potentially fraudulent claims by Accounts Management to Examination for review. We reviewed a statistically valid sample of 56 Forms 941-X out of a population of 209 that met the examination referral criteria to determine whether claims were being referred to Examination when required. Our sample was based on a confidence level of 90 percent, an expected error rate of 5 percent, and a precision factor of  $\pm 5$  percent. Our contracted statistician assisted with developing sampling plans and projections.
- Evaluated the processes and procedures to identify erroneous COVID-19 related employer credits claimed by businesses associated with new EINs. We analyzed Tax Year 2021 Forms 941 filed using a newly issued EIN that claimed the ERC to assess whether the newly implemented filter was working as intended.

This review was performed with information obtained from the Small Business/Self Employed Division Headquarters located in Atlanta, Georgia, and the Wage and Investment Division's Accounts Management sites located in Covington, Kentucky; and Ogden, Utah, during the period June 2021 through March 2022. 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 objective. We believe that the evidence

obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

Major contributors to the report were Russell Martin, Assistant Inspector General for Audit (Returns Processing and Account Services); Linna K. Hung, Director; Van Warmke, Audit Manager; Mark Willoughby, Lead Auditor; Ian Maloney, Auditor; Brett Skaggs, Auditor; and Laura Haws, Information Technology Specialist (Data Analytics)

### **Validity and Reliability of Data From Computer-Based Systems**

We performed tests to assess the reliability of data extracts received from the Correspondence Imaging System and the Business Master File. We evaluated the data by performing electronic testing of required data elements and reviewing existing information about the data. In addition, we selected data from each extract and verified that the data in the extracts were the same as the data captured in the IRS's Integrated Data Retrieval System<sup>1</sup> and Correspondence Imaging System. We determined that the data were reliable.

### **Internal Controls Methodology**

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined that the following internal controls were relevant to our audit objective: procedures to review and process Forms 941-X. We evaluated these controls by reviewing the Internal Revenue Manual and interviewing employees responsible for processing Forms 941-X.

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<sup>1</sup> IRS computer system capable of retrieving information, which works in conjunction with a taxpayer's account.



## Appendix II

### Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to Congress.

#### **Type and Value of Outcome Measure:**

- Taxpayer Burden – Potential; 4,001 taxpayer accounts that had refunds delayed because the Forms 941-X were erroneously suspended from processing due to errors by IRS employees (see Recommendation 1).

#### **Methodology Used to Measure the Reported Benefit:**

In October 2020, the IRS issued guidance to its employees to suspend processing of Forms 941-X with an adjustment to the amount of deferred Social Security tax or if the tax account had a previously posted deferred Social Security tax amount. IRS management stated that they needed to suspend the processing of these claims because of the lack of procedures and programming in place to ensure that claims are processed accurately.

We identified a population of 12,337 Forms 941-X in inventory that were in a suspended status. We reviewed a statistically valid sample<sup>1</sup> of 74 of those Forms 941-X and found that 24 (32 percent) of the claims were erroneously suspended. These claims should not have been suspended because they did not include an adjustment to the amount of deferred Social Security tax or meet the exception criteria for processing. Based on the results of our statistically valid sample, we project that 4,001<sup>2</sup> of the 12,337 claims in the suspended inventory were suspended erroneously.

#### **Type and Value of Outcome Measure:**

- Cost Savings (Funds Put to Better Use) – Potential; \$45,310,431 in potentially erroneous nonrefundable employer tax credits processed on amended returns that did not receive review by Examination (see Recommendations 7, 8, and 9).

#### **Methodology Used to Measure the Reported Benefit:**

Accounts Management employees are required to refer Forms 941-X that result in a reduction in net tax of [REDACTED] or more to Examination during processing. This process is in place in an effort to identify potentially fraudulent claims prior to refund issuance. However, we found that the tax examiners were not referring some returns without a refundable credit claim as required.

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<sup>1</sup> We selected a statistical sample using a confidence level of 90 percent, an expected error rate of 5 percent, and a precision factor of  $\pm 5$  percent.

<sup>2</sup> The point estimate projection is based on a two-sided 90 percent confidence interval. We are 90 percent confident that the actual total amount is between 2,899 and 5,237.

Specifically, our review identified 209 Forms 941-X processed as of July 28, 2021, that met the CAT-A referral criteria. We reviewed a statistically valid sample<sup>3</sup> of 56 of these Forms 941-X and found that 41 (73 percent) were not referred to Examination as required. Based on the results of our statistically valid sample analysis, we project that 153<sup>4</sup> amended returns were not referred as required resulting in \$45,310,431 in potentially erroneous nonrefundable employer tax credits being allowed.

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<sup>3</sup> We selected a statistical sample using a confidence level of 90 percent, an expected error rate of 5 percent, and a precision factor of  $\pm 5$  percent.

<sup>4</sup> The point estimate projection is based on a two-sided 90 percent confidence interval. We are 90 percent confident that the actual total amount is between 133 and 170.

## **Appendix III**

### **Management's Response to the Draft Report**



COMMISSIONER  
SMALL BUSINESS/SELF-EMPLOYED DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

August 8, 2022

MEMORANDUM FOR HEATHER M. HILL

DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

Lia Colbert

Amalia C. Colbert

Digitally signed by Amalia C.  
Colbert  
Date: 2022.08.09 06:24:21 -04'00'

Commissioner, Small Business/Self-Employed Division

SUBJECT:

Response to Draft Audit Report – Delays Continue to Result in  
Businesses Not Receiving Pandemic Relief Benefits (Audit #  
202140623)

Thank you for the opportunity to review and comment on your draft audit report entitled *Delays Continue to Result in Businesses Not Receiving Pandemic Relief Benefits*. The Families First Coronavirus Response Act (FFCRA) and Coronavirus Aid, Relief, and Economic Security (CARES) Act were enacted in March 2020. These new provisions established the Qualified Paid Sick & Family Leave Credit, the Employee Retention Credit (ERC), the ability to receive an advance payment of these credit amounts, and the payroll tax deferral. Subsequent legislation in December 2020 (Consolidated Appropriations Act), March 2021 (American Rescue Plan Act) and November 2021 (Infrastructure Investment and Jobs Act) extended and/or modified limitations and qualifications for these credits. Each adjustment to the credit by legislation required IRS adjustment of programming to match the credit requirements. This audit presented unique challenges because TIGTA conducted this audit as we were implementing continuously changing legislation.

Although the last two years have been unprecedented with respect to evolving legislation, we expeditiously implemented extensive and complex legislative tax changes to ensure businesses received billions of dollars in credits and deferrals providing needed relief to American employers. Upon legislative enactment, we immediately established a cross-functional implementation team to review in detail the legislative impact to administrative processes and to develop the extensive programming changes required for these claims. The IRS successfully paid out over \$68 Billion in employer credits to 1.2 million taxpayers.

As your report noted, we took several significant corrective actions to identify and prevent potentially fraudulent employer tax credits claimed on Form 941, *Employer's Quarterly Federal Tax Return*. Our efforts included updating identity theft filters to identify suspicious Forms 941 meeting certain criteria and implementing procedures to identify erroneous employer tax credit claims associated with ineligible government entities. The IRS identified 11,096 suspicious returns during processing with more than \$2 trillion in credits claimed.

The IRS could not have processed amended returns immediately after the enactment of pandemic relief legislation. Given the resulting office closures and social distancing guidelines due to the pandemic, we were unable to immediately process original and amended employment tax returns. Amended returns cannot be processed until the original return is processed. Further, TIGTA failed to consider that regardless of when the legislation passed, the earliest an amended return was expected was August 2020, as the original return reporting credits were for the quarter ending June 30, 2020, and was not due until July 31, 2020.

We are committed to resolving processing delays to ensure that eligible American employers receive the benefits intended by the pandemic relief legislation. As such, key stakeholders and Subject Matter Experts (SMEs) meet weekly to prioritize amended return inventory and to address procedural or technical obstacles hindering timely processing of COVID business credits. Due to the complexity of these cases, we identified and trained hundreds of business master file SMEs to prioritize handling of the COVID Business Credit inventory. The report references 402,814 overage Forms 941-X, *Adjusted Employer's QUARTERLY Federal Tax Return or Claim for Refund*, as of February 1, 2022. This is the total Form 941-X inventory and is not specific to the COVID-19 Forms 941-X inventory. As of August 1, 2022, the current overall Form 941-X overage inventory is 90,684. The identified COVID-19 Forms 941-X claims have declined to 2,484 from over 68,000 at the start of fiscal year 2022. As the inventory numbers continue to improve, the over-aged COVID-19 related claims will decrease accordingly.

We appreciate TIGTA's feedback regarding the need for verification of businesses as Recovery Startup Businesses (RSB), and agree that as part of post processing compliance, such consideration should be made. However, it is important to note that the date an employer identification number (EIN) is issued does not determine whether a business qualifies as an RSB. Processing rejections based on the EIN issuance date alone would result in improper rejections serving only to increase taxpayer burden and withholding additional amounts from taxpayers legally entitled to the credits. Post-processing compliance considerations for this timeframe are still in an active and ongoing development phase.

**Delays Continue to Result in Businesses  
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Attached is a detailed response outlining our corrective actions to address your recommendations. If you have any questions, please contact me or Scott Irick, Director, Examination, Small Business/Self-Employed Division.

Attachment

Attachment

**RECOMMENDATION 1:**

**(Email Alert):** On November 22, 2021, we notified the Director, Customer Account Services that the IRS employees were erroneously suspending Forms 941-X when the claim did not include an adjustment to the amount of deferred social security tax. We recommended that the Accounts Management function immediately review the Forms 941-X that are identified in the suspense inventory as an adjustment to the amount of deferred social security tax to ensure that they are properly categorized.

**CORRECTIVE ACTION:**

We implemented additional reviews of suspended inventory to evaluate whether the cases were correctly suspended. The processing sites continue to conduct random sample reviews of the unworkable listings to determine if cases controlled there are workable and reassign them accordingly. As of July 8, 2022, we have 76,079 Form 941-X claims suspended that need to be processed.

**IMPLEMENTATION DATE:**

Implemented

**RESPONSIBLE OFFICIAL:**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN:**

N/A

**RECOMMENDATION 2:**

The Commissioner, Wage and Investment should evaluate the current inventory of backlogged claims related to pandemic relief and develop specific plans to prioritize claims and develop timelines to process backlogged claims.

**CORRECTIVE ACTION:**

We continue our efforts to reduce the inventory increases from the pandemic. Those efforts included increased staffing with overtime and 100 percent of the campus employees' time focused on paper inventory. Through June 25, 2022, these actions have reduced the inventory of the Form 1139, *Corporation Application for Tentative Refund*, carrybacks to under 1,100 applications.

**IMPLEMENTATION DATE:**

Implemented

**RESPONSIBLE OFFICIAL:**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN:**

N/A

**RECOMMENDATION 3:**

The Commissioner, Wage and Investment Division, should review the 928 business entities identified that do not appear to qualify as an RSB and take actions needed to recover the ERC's that are determined to be erroneous.

**CORRECTIVE ACTION:**

We will review the 928 returns to identify the returns exceeding our thresholds. Of those that exceed the thresholds, we will determine if other non-compliance indicators are present and take compliance action, if warranted.

**IMPLEMENTATION DATE:**

October 15, 2023

**RESPONSIBLE OFFICIAL:**

Director, Exam Case Selection, Headquarters Examination, Small Business/Self-Employed Division

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 4:**

The Commissioner, Small Business/Self-Employed Division, should identify all fourth quarter TY 2021 paper Form 941s processed prior to when the programming was implemented and identify amended employment tax returns receiving ERC where there was no indication that the business was an RSB and take actions needed to recover the ERCs that are determined to be erroneous.

**CORRECTIVE ACTION:**

Independent of TIGTA's audit, we identified this issue on February 24, 2022, and began development of a process to identify and address this issue. We will finalize and implement this process.

**IMPLEMENTATION DATE:**

March 31, 2023

**RESPONSIBLE OFFICIAL:**

Director, Exam Case Selection, Headquarters Examination, Small Business/Self-Employed Division



**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 5:**

**(Email Alert):** On May 13, 2021, we notified the Director, Examination, Small Business/Self-Employed Division, about the inconsistent referral criteria and recommended that the IRS update referral criteria to include Forms 941-X with refundable credits.

**CORRECTIVE ACTION:**

Internal Revenue Manual (IRM) 21.5.3, *Account Resolution – General Claims Procedures*, was updated on July 22, 2021, with IRM Procedural Update 21U964. We subsequently monitored Quality reports to ensure correct referrals to Examination.

**IMPLEMENTATION DATE:**

Implemented

**RESPONSIBLE OFFICIAL:**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN:**

N/A

**RECOMMENDATION 6:**

**(Email Alert):** On November 23, 2021, we alerted the Director, Customer Account Services, that Forms 941-X were not being referred to Examination as required and recommended that the Accounts Management function provide additional guidance to its employees to reinforce established CAT-A referral criteria.

**CORRECTIVE ACTION:**

Employees were reminded of the Examination referral criteria through Servicewide Electronic Research Program Alert 21A0403 issued on December 1, 2021. It is important to note that it is not possible to tell if the claims were actually erroneous without conducting an examination. Even if referred, the claim may have ultimately been accepted as filed.

**IMPLEMENTATION DATE:**

Implemented

**RESPONSIBLE OFFICIAL:**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN:**

N/A

**RECOMMENDATION 7:**

The Commissioner, Wage and Investment Division, should review the 41 Form 941-X claims with a non-refundable COVID-19 related employer credit identified that meet CAT-A referral criteria and take actions needed to recover credits that are determined to be erroneous.

**CORRECTIVE ACTION:**

We will review the cases and take appropriate action.

**IMPLEMENTATION DATE:**

December 15, 2022

**RESPONSIBLE OFFICIAL:**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

**RECOMMENDATION 8:**

The Commissioner, Wage and Investment Division, should provide additional training to employees as it relates to referring Forms 941-X to Examination for review.

**CORRECTIVE ACTION:**

We completed subsequent reviews of completed Form 941-X claims and determined no additional training was needed.

**IMPLEMENTATION DATE:**

N/A

**RESPONSIBLE OFFICIAL:**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN:**

N/A

**RECOMMENDATION 9:**

The Commissioner, Wage and Investment Division, should submit a request for the development of a systemic process to identify 941-X claims that meet referral criteria and alert the Accounts Management employee when processing these claims of the need to refer the return to Examination.

**CORRECTIVE ACTION:**

We will determine the feasibility of a systemic process and submit the necessary requests, if warranted.

**IMPLEMENTATION DATE:**

December 15, 2023

**RESPONSIBLE OFFICIAL:**

Director, Accounts Management, Customer Account Services, Wage and Investment Division

**CORRECTIVE ACTION MONITORING PLAN:**

IRS will monitor this corrective action as part of our internal management system of controls.

## **Appendix IV**

### **Abbreviations**

CARES	Coronavirus Aid, Relief, and Economic Security
COVID-19	Coronavirus Disease 2019
EIN	Employer Identification Number
ERC	Employee Retention Credit
FFCRA	Families First Coronavirus Response Act
IRS	Internal Revenue Service
RSB	Recovery Startup Business
TIGTA	Treasury Inspector General for Tax Administration



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**By Web:**

[www.treasury.gov/tigta/](http://www.treasury.gov/tigta/)

**Or Write:**

Treasury Inspector General for Tax Administration  
P.O. Box 589  
Ben Franklin Station  
Washington, D.C. 20044-0589

Information you provide is confidential, and you may remain anonymous.