United States Senate
WASHINGTON, D.C.

November 5, 2013

Daniel Werfel
Principal Deputy Commissioner
Internal Revenue Service
1111 Constitution Avenue, NW
Washington, D.C. 20230

Dear Principal Deputy Commissioner Werfel:

Recently, the Treasury Inspector General for Tax Administration (TIGTA) reported that the Internal Revenue Service (IRS) has "made little improvement in reducing the improper payment rate for the Earned Income Tax Credit (EITC) since being required to report estimates of these payments to Congress."[1] In 2012, the IRS allowed about $13.6 billion in improper EITC payments to tax filers who were ineligible for the credit. Unfortunately, that means that *up to 25 percent of EITC last year payments were improper*.

Back in 2008, TIGTA recommended that IRS come up with alternative methods for identifying and preventing improper payments. However, TIGTA's recent audit revealed that IRS has not taken any steps to address this recommendation.[2] In fact, TIGTA found that IRS does not even have a goal for reducing future improper payments, or a plan in place to meet such targets.[3] The IRS's failure to take recommended steps to increase program integrity means the program continues to be at risk. In 2011, up to $16.7 billion in tax credits were issued improperly, and in 2010, the amount was roughly the same—$18.4 billion.

This audit raises serious concerns about the IRS's unwillingness or inability to successfully prevent billions of taxpayer dollars being wasted on erroneous tax credit claims. We are particularly worried about these findings, given the IRS's role generally as the primary agency administering a range of credits and specifically in overseeing and implementing the premium tax credits under the Patient Protection and Affordable Care Act (PPACA).

Similar to the EITC, the Affordable Care Act offers refundable tax credits for certain eligible individuals. However, we believe that a range of provisions in federal law, regulations, and administrative practices actually leave the health care overhaul even more seriously susceptible to fraud or abuse than the EITC program already is.

First, to try to prevent improper payments for federally-facilitated exchanges, IRS will rely partly on personal attestations of income, and only audit a random sample of applicants who claim that their income decreased more than 10 percent from amounts found in last year's tax filing starting in 2014.[4] State-based exchanges will not be required to perform this audit until 2015.

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[1] http://www.treasury.gov/tigta/auditreports/2013reports/201340084fr.pdf
[2] Page 12 of the report.
[3] Page 13 of the report.
[4] http://healthaffairs.org/blog/2013/07/07/implementing-health-reform-final-rule-on-premium-tax-credit-medicaid-and-chip-eligibility-determinations-part-1/

Second, because of a change the Obama administration made this past summer, premium credit applicants in state-based exchanges can simply provide a personal attestation that they do not receive qualifying insurance through their employer to receive their premium credits in 2014. No further documentation is required.[5]

Third, a provision in current law actually limits how much the federal government can recover from sending a greater amount of subsidy to consumers than for which they were eligible.[6] In other words, the law currently prevents the recovery of overpayments paid to individuals who turn out not to be eligible for them. This cap on recovering overpayments will prevent federal officials from pursuing billions of dollars in overpayments. In fact, according to CBO, if that cap on recapturing subsidy overpayments were eliminated, taxpayers would save $43 billion over a decade.[7]

Finally, the concerns lie not just with the EITC, but with other tax requirements as well. A more recent TIGTA report found that even some of the standard income and withholding verification processes at the IRS may be failing to prevent fraudulent tax refunds.[8] As the IRS watchdog explained, "most current year third-party information is not available until well after the tax return filing season begins and tax returns are processed," and, as a result, a 2012 audit shows that nearly 1.5 million tax returns "were not detected by the IRS as potentially fraudulent despite having the same characteristics as IRS-confirmed identity theft fraudulent tax returns."

Overall, taken together, these realities paint a worrisome picture of the fraud that may be anticipated under PPACA. The premium tax credits vulnerability to fraud and abuse is significant because the Congressional Budget Office estimates that the credits cost taxpayers $796 billion over the coming decade.[9] If these health coverage premium tax credits experience an improper payment rate similar to that of the EITC, about $200 billion taxpayer dollars could be wasted or lost to fraud. Therefore, to better understand how IRS will manage the potential for significant fraud and abuse in applications for PPACA premium tax credits, we respectfully ask for responses to the following questions.

1. What is IRS's plan to avoid improper payments made to applicants for premium tax credits, and how will IRS recover such improper payments?
2. To what extent is IRS planning to identify or implement alternative compliance methods to avoid or recoup improper premium tax credits, similar to TIGTA's 2008 recommendation regarding EITC?
3. Given the history of high improper payments for EITC, what assurances can you provide that premium tax credits will not result in the same rate of fraud and abuse?
4. What lessons have you learned from addressing EITC improper payments that could be applied to implementing the ACA?
5. What are IRS's 2014 targets for premium tax credit improper payments?

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[5] CRS report # R43150, page 10 of the PDF.
[6] Citation: P.L. 112-9, Sec. 4 amends sec 36B(f)(2)(B) of the Internal Revenue Code.
[7] http://www.cbo.gov/publication/43191
[8] http://www.treasury.gov/tigta/auditreports/2013reports/201340083fr.html
[9] U.S. Congressional Budget Office, "CBO's May 2013 Estimate of the Effects of the Affordable Care Act on Health Insurance Coverage," May 2013, http://www.cbo.gov/sites/default/files/cbofiles/attachments/44190_EffectsAffordableCareActHealthInsuranceCoverage_2.pdf.

Please provide your response no later than November 25, 2013. Should you have any questions regarding this letter, please have your staff contact Kim Brandt of Senator Hatch's Finance Committee staff at (202) 224-4515 or Josh Trent of Dr. Coburn's office at (202) 224-5754.

Sincerely,

Orrin G. Hatch
U.S. Senator
Ranking Member,
Finance Committee

Tom Coburn, M.D.
U.S. Senator
Ranking Member
Homeland Security and
Government Affairs Committee