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INSIGHT

Audits of EITC Returns: By the Numbers

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The Internal Revenue Service (IRS) audits taxpayers to determine whether they are in compliance with tax law and have accurately reported tax liability. Some policymakers are concerned that the IRS is auditing low-income taxpayers—in particular taxpayers who claim the earned income tax credit (EITC)—at disproportionately high rates compared to higher-income taxpayers. These higher audit rates may be in response to the high improper payment rates associated with the EITC.

This Insight examines recent data related to audits of EITC returns. For the purposes of this Insight, an *EITC return* is defined as a return which includes a claim of the EITC. For comparison, data on audits of other individual income tax returns that do not include an EITC claim (*non-EITC returns*) are also provided. These two types of taxpayers—taxpayers filing EITC returns and non-EITC returns—represented about 90% of all audits of 2017 tax returns (see IRS Databook Table 17). The remaining 10% includes corporations, estates, and employers and is not discussed in this Insight.

A Small Share of Taxpayers—Claiming the EITC or Not—Are Audited

Audits of individual returns, whether *with* or *without* an EITC claim, are relatively uncommon, as illustrated using IRS data for 2017 tax returns below. (While the IRS has published data on 2018 and 2019 audits, the data are incomplete since returns filed for those years are within the statute of limitations where examinations may be ongoing.)

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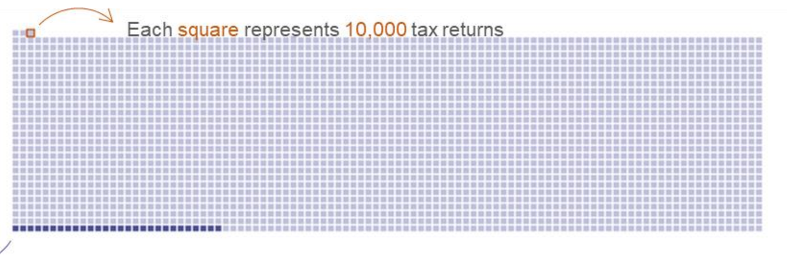
Share of EITC Tax Returns Audited

Of the over **150 million** tax returns filed by individuals for the 2017 tax year, over **27 million** included a claim for the EITC (i.e., **"EITC returns"**), as illustrated by more than 2,700 squares in this figure.

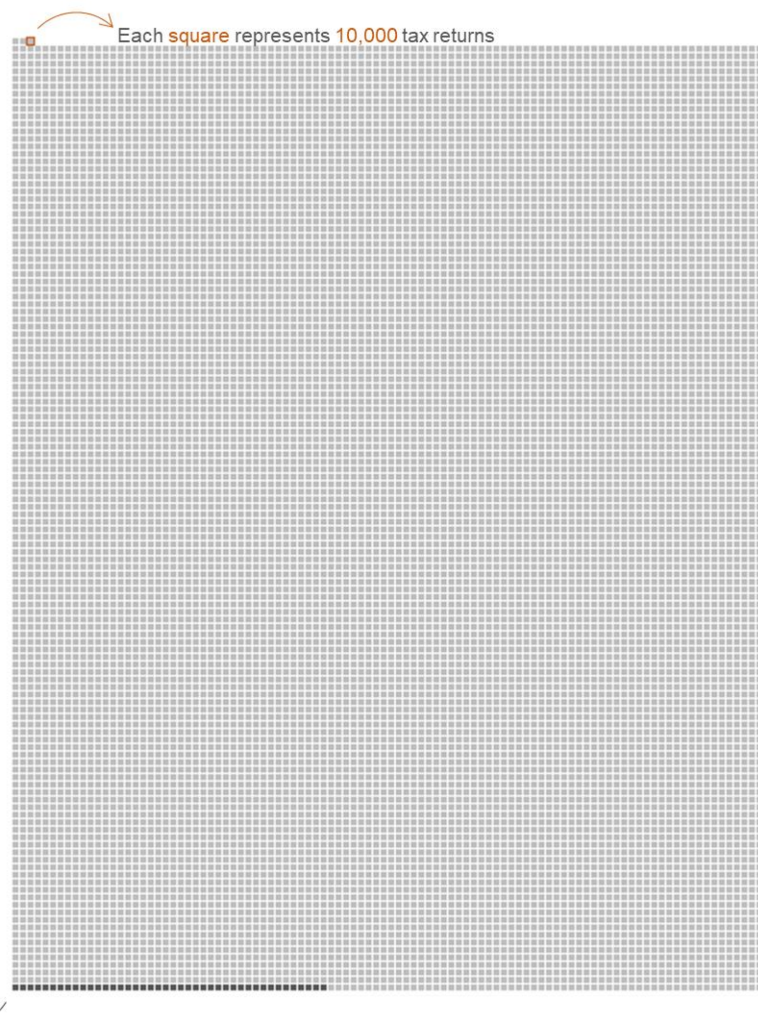
Of these **27 million EITC returns**, about **280,000** were audited, represented by the 28 squares. This is an audit rate of **1.0%**.



Share of Non-EITC Tax Returns Audited

Of the over **150 million** tax returns filed by individuals for the 2017 tax year, over **126 million** did not include a claim for the EITC (i.e., "**non-EITC returns**"), as illustrated by the more than 12,600 squares in this figure.

Of these **126 million non-EITC returns**, about **420,000 were audited**, represented by the 42 squares. This is an audit rate of **0.3%**.



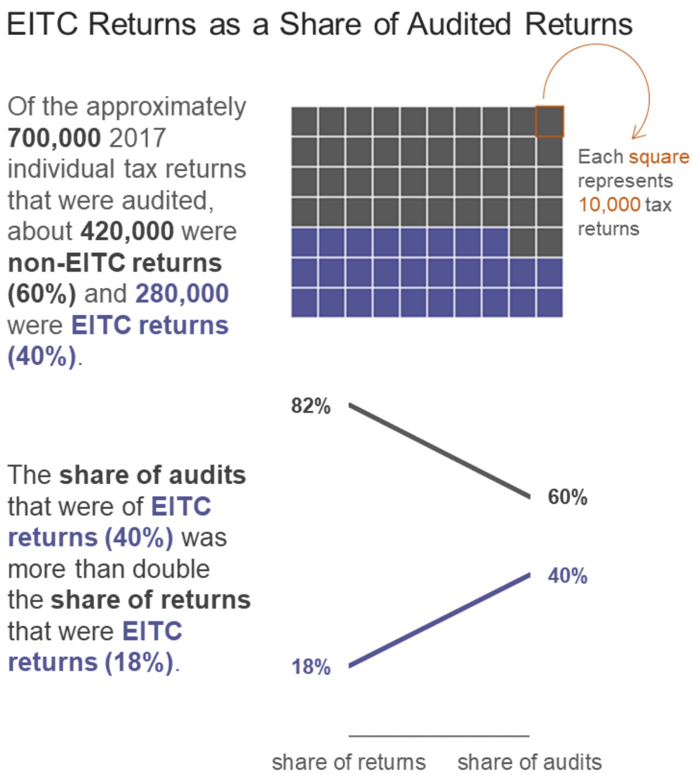
Source: CRS calculations based on IRS Databook Table 17.

Note: Audited returns include those closed and in-process.

A recent Government Accountability Office (GAO) report indicates audit rates have declined over the past decade: 2010 EITC returns were audited at a rate of 1.8%, compared to 0.7% of 2010 non-EITC returns. Audit rates for non-EITC returns declined about 57% between 2010 and 2017. For EITC returns, that decline was about 44%. These averages mask differences by income group. The GAO report indicates that over the past decade, audit rates have fallen the fastest for higher-income taxpayers.

Among Audited Taxpayers, a Large Share Claim the EITC

Audit rates for EITC returns are disproportionately high compared to the share of taxpayers who claim the credit, as illustrated below. These estimates are in line with trends over the past decade, where individual taxpayers claiming the EITC represent about 2 out of 10 individual taxpayers and about 4 out of every 10 individual audits.



Source: CRS calculations based on IRS Data Book Table 17.

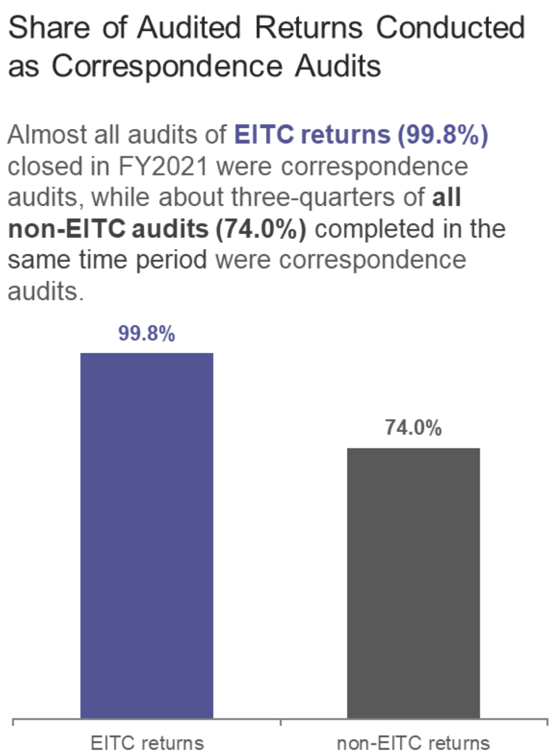
Note: Audited returns include those closed and in-process.

Because of the higher audit rate of EITC returns, areas of the country with a higher share of taxpayers claiming the EITC—including southeastern states and some western states—would be expected to have a larger share of their taxpayers audited (as discussed in a ProPublica investigation). In other words, a taxpayer in Mississippi is more likely to be audited than a taxpayer in New Hampshire, in part because they are more likely to be a taxpayer who claims the EITC.

Research also indicates that when looking *exclusively* at households that claim the EITC, audits of EITC returns tend to be higher in certain southern states than in northern states (see Figure A.17 and Table 7). In other words, an EITC claimant in Mississippi is more likely to be audited than an EITC claimant in New Hampshire. A 2021 report from the Treasury Inspector General for Tax Administration (TIGTA) notes that the IRS states it does not select EITC returns for audit based on geographic location. Instead, the report suggests that EITC claimants from these states are more likely to be flagged as noncompliant (and hence more likely to be audited) than EITC claimants in other areas, although the report provides no explanation as to why.

Most Audits of EITC Returns Are Done via Paper Mail Correspondence and Are Conducted *Before* a Refund is Issued

Audits can be conducted in one of three ways: by mail (correspondence audits); in person at IRS offices (office audits); or in person at the taxpayer's home or business (field audits). Virtually all audits of EITC returns are conducted as correspondence audits, as illustrated below.



Source: CRS calculations based on IRS Data Book Table 18.

As the National Taxpayer Advocate (NTA) explains, generally during a correspondence audit of an EITC return,

> the IRS notifies a taxpayer of an audit by sending a notice, such as Notice CP 75 or 75A, by certified mail. The first lines of the audit notice state that the IRS is auditing the income tax return for the specified year, that the taxpayer needs to send supporting documentation, and that the IRS is holding the EITC portion of any claimed refund (and the refundable portion of the Child Tax Credit, if it was claimed) pending the results of the audit.

The majority of EITC audits are conducted *before* the EITC (and any other applicable tax benefits) are issued (i.e., pre-refund audits). A 2019 NTA report found that 75% of EITC audits in FY2018 were pre-refund audits.

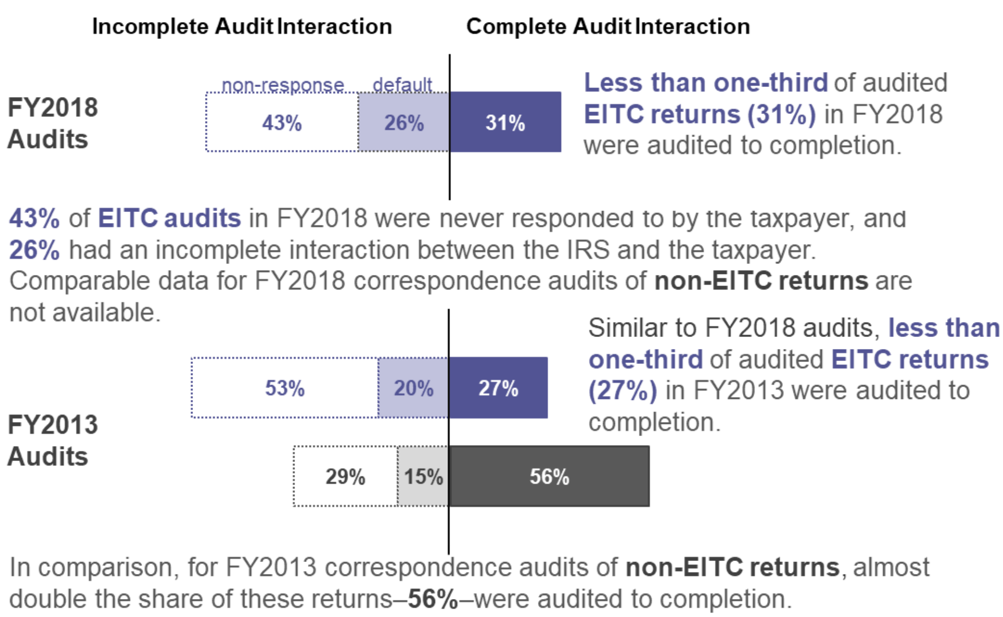
The Majority of EITC Audits Are Never Completed

An audit is ultimately closed as a result of

- a complete interaction between the taxpayer and the IRS that leads to a resolution (either no change in the original tax/refund calculation, an agreed-upon change, or an appeal);
- an incomplete interaction between the taxpayer and the IRS whereby documentation is exchanged initially between the two parties, but not to resolution (i.e., the taxpayer stops responding to notices). This is sometimes called default; or
- no response from the taxpayer to the initial IRS notice. This is called "non-response."

Since EITC audits are generally conducted pre-refund, when the audit is closed due to non-response or default, the IRS can retain the additional tax they recommend the taxpayer owes (the "recommended additional tax") using less personnel time than if the audit were closed due to a completed interaction with the taxpayer.

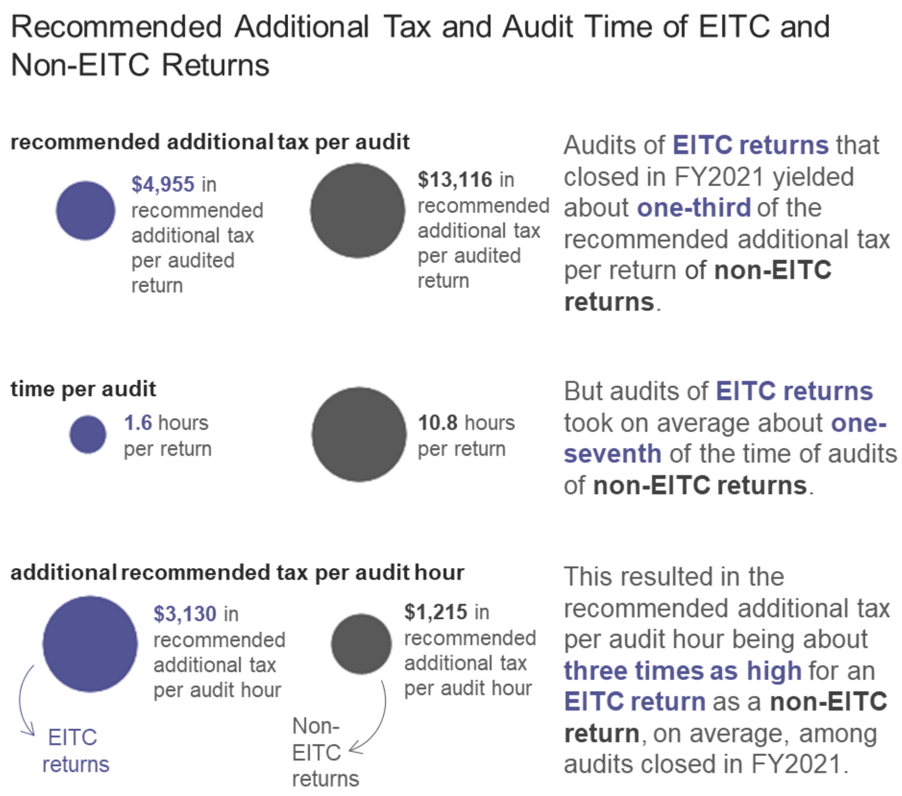
Audit Interactions for Correspondence Audits of EITC and Non-EITC Returns



Source: Figure 2 and Figure A.18 in Taxpayer Advocate Service Special Report to Congress, 2019 and CRS calculations of audits of filed returns in Table 7 of GAO-14-479 (excluding test cases).

Audits of EITC Returns Result in More Recommended Additional Tax per Audit Hour than Audits of Non-EITC Returns

EITC audits may be cost effective from the IRS's perspective, as they lead on average to higher recommended tax amounts per audit hour than non-EITC audits, as illustrated below.



Source: CRS calculations based on GAO-22-104960 Table 1 and Appendix IV Tables 4, 5, and 6.

However, research indicates that audits can be particularly burdensome to lower-income families, who may struggle to understand audit letters, including what documentation they need to provide to substantiate a claim.

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