



Safeguarding the Refund Process

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- John Bace
 - Revenue Solutions, Inc. (RSI)
 - Data Warehousing and Business Intelligence Practice



Fundamental Problem



Refundable credits and refund checks...

- *Stopping Fraud*
- *Addressing audit cases prior to issuing refunds instead of working on the “back end”*
- *Maintaining or improving taxpayer service and refund turnaround time for the “95% Group”*

“Return Review Overload”



Agenda



- Review of the basic problem
- How things are changing
- What works?
- Making improvements

Problem Reviewed



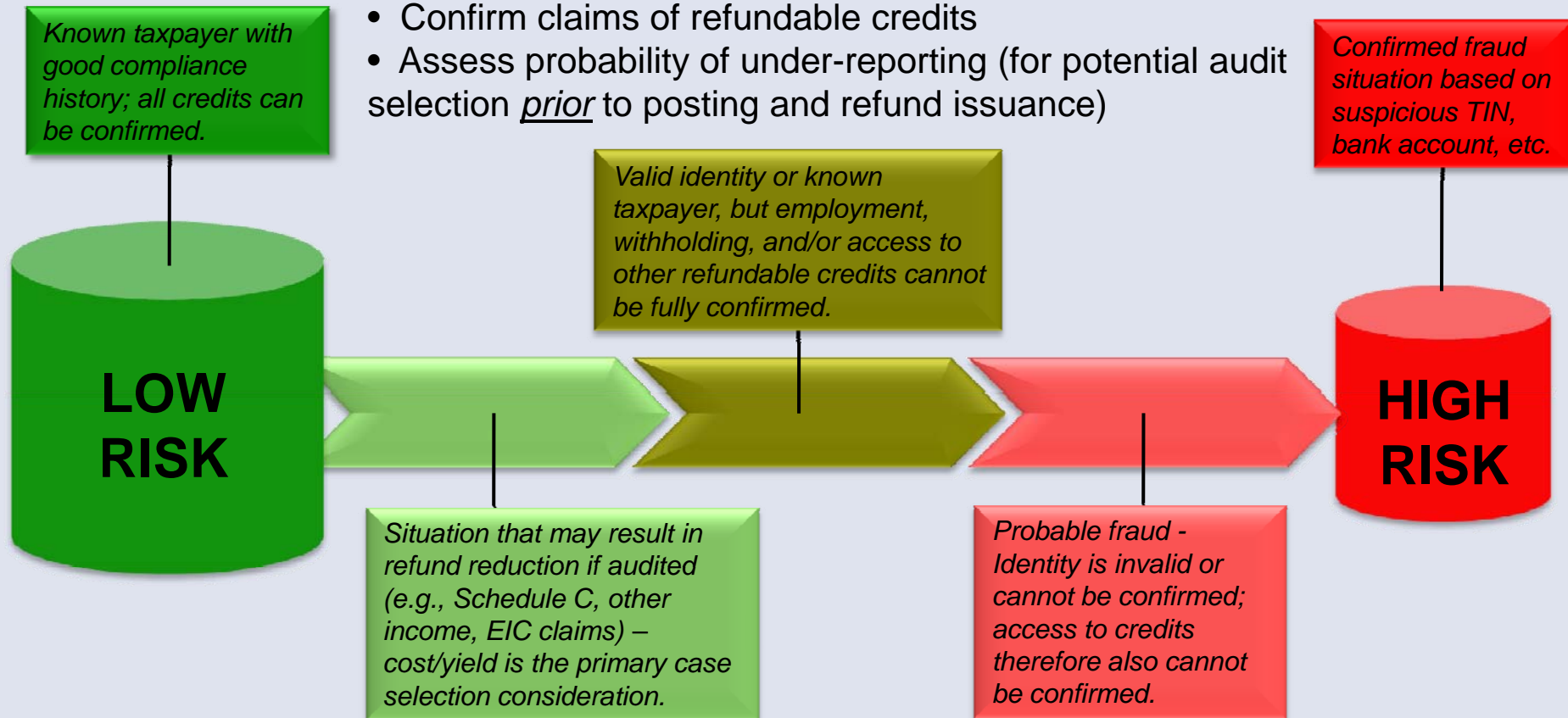
- Why aren't all refunds issued immediately?
 - Resolve return/form problems
 - Handle posting/accounting reconciliation
 - ... and **prevent fraud and address inflated refunds**
- **Priorities/goals**
 1. Stop fraudulent checks from going out
 2. Audits of some returns prior to sending refund
 - Confirming credits
 - Limited-scope audits

Refund Issuance Risk



When assessing risk:

- Confirm taxpayer identity
- Confirm claims of refundable credits
- Assess probability of under-reporting (for potential audit selection prior to posting and refund issuance)



Goals... review or interact with the fewest returns, stop the most fraud, and reduce overall impact to compliant taxpayers

How things are changing...



- When reviewing paper returns as they arrive
 - “*It looks suspicious*” → but, now most are e-filed
 - “*W-2 is missing*” → but, now they’re not required or reviewed
- When invoking rules against return line items
 - *Simple thresholds by Refund Amount or Wages/Withholding ratio*
→ but, scammers detect the thresholds
- More recent trends
 - More e-filing and less paper
 - Increase in fraud schemes
 - Less staff to review returns
 - Technology improvements (which make automation possible!)

What has worked in the past ...



- Isolated, “known” problems
 - FTA Suspicious Filer list
 - Specific individuals (TINs/Names)
 - Specific bank accounts
 - Specific addresses

- Simple rules based on return line item patterns
 - Ratios of Withholding to Wages
 - Refund amount over specific thresholds
 - Specific credit claims

What has worked in the past ...



■ Perform common checks

- Disallow name/address change at same time
- Suspend multiple refunds to one bank account or address
- Higher scrutiny of Non-Resident returns
- Stop second return filed under the same SSN (which could be keying errors, simple mistakes, or possible identify theft)
- SSN and ITIN “valid number” algorithms

But these methods are incomplete...

More can be automated with data & technology

Basic Points of What Works

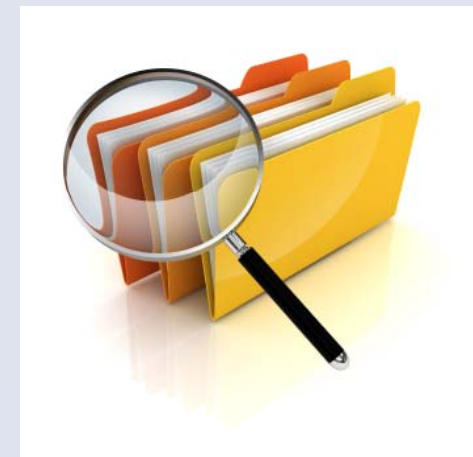


- Automate ... carefully
 - What procedures are followed for manual research/inspection, and can they be automated?
- Use taxpayer history
- Verify what you can in advance
- Use more data
 - Not just simple rules based on current return line items
- Prioritize all work according to risk
- Ask taxpayer to respond
 - And then inactivate automatically if they don't
- Adapt – *the schemes do*

What works? ... Use your history



- You have a lot ...
 - Taxpayer information
 - Prior returns
 - Payment history
 - Prior refunds that were suspended but released
 - State W-2s, and other employer filings
 - Withholding accounts and payments
 - Patterns of prior fraudulent refund returns



What works? ... Verify in advance



- **Verify who you know already**
 - Processing intensive, so do it ahead of time; when it doesn't need to occur in less than 1 second during return processing!
 - Take your time and iterate, perfect data mining and adjust rules
 - Allows you to then just focus on the new taxpayers
- **Verification options**
 - TINs
 - Employment
 - Employer-Employee relationships
 - Withholding credits by TIN (from State W-2s)
- **Develop “pre-validated” taxpayer list**

What works? ... Verify in advance



- Identify “suspicious” scenarios
- Conduct data mining from prior years
 - Find existing registration data anomalies
 - Find multiple instances of Names, SSNs
 - Identify schemes/patterns – and expand across all filed returns
 - Use confirmed fraud identification from prior cases

What works? ... More State Data



- **Other state agencies and organizations**
 - Motor Vehicles
 - Health and Human Services
 - Licensing Boards
 - Lottery Winners
 - Labor Filings
 - Unemployment Benefits
 - Criminal Records
 - Vital Statistics (Death Records)

- **State-to-state exchanges**
 - Use to confirm non-resident refund requests
 - Share rejected refund information

What works? ... Other Data Sources



- **3rd party data providers**
 - Aggregate data from multiple sources
 - Proprietary data “linking” technologies
 - Overcome differences in data
 - Flexibility: specialized products and pricing models

- **Property Ownership/Tax Data**
 - Counties/municipalities
 - Private data aggregation companies
 - Confirm identity
 - Confirm eligibility for refundable “circuit breaker” credits

What works? ... The IRS Can Help!



- IMF/IRTF extracts and TIN Validity Code
 - SSN/Name combinations from Social Security Administration
- Monthly ITIN issuance extract
- Legacy ELF and MeF (Modernized e-File)
 - IRS performs SSN and name control verification
 - Available with the transmission prior to State posting
- TIN Matching program
 - Part of IRS eServices suite for Payers (States use as Payers)
 - Send files of TINs to IRS
 - IRS returns indicators whether TIN is valid or not
 - ***For information → contact your local IRS liaison***

What works? ... Payer Withholding Reporting at TIN Level

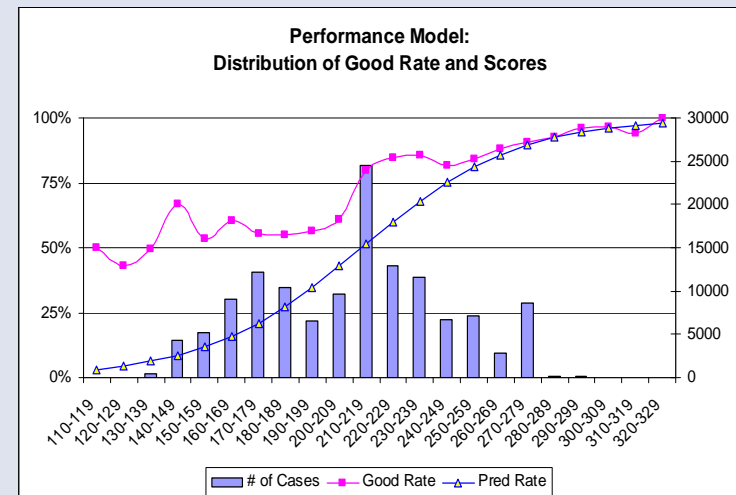


- **WH credit accounting from employers/payers**
 - Detailed reporting of WH allocation to TIN level (quarterly)
 - Should match 1099s or W-2s at year end
 - Increasing requirement among States
 - Combine with other employment tax filing requirements
 - Capturing more data through e-filing and keying
 - Provides ability to cross-check against taxpayer claims
 - Also applies to WH for Pass Thru Entities (particularly for non-resident partners); should follow same reporting requirements as other WH accounts (i.e., allocated to TINs, and matching K-1s)

What works? ... Decision Analytics



- **Build statistical models**
 - Predict probability of fraud
 - Rely on prior case results
 - Refine over time
- **Use to prioritize leads**
 - You can't work all of them!



Tax Preparer-level comparative analysis during the filing season to identify those with a disproportionate number of “high risk” returns

What works? ... Automated Handling



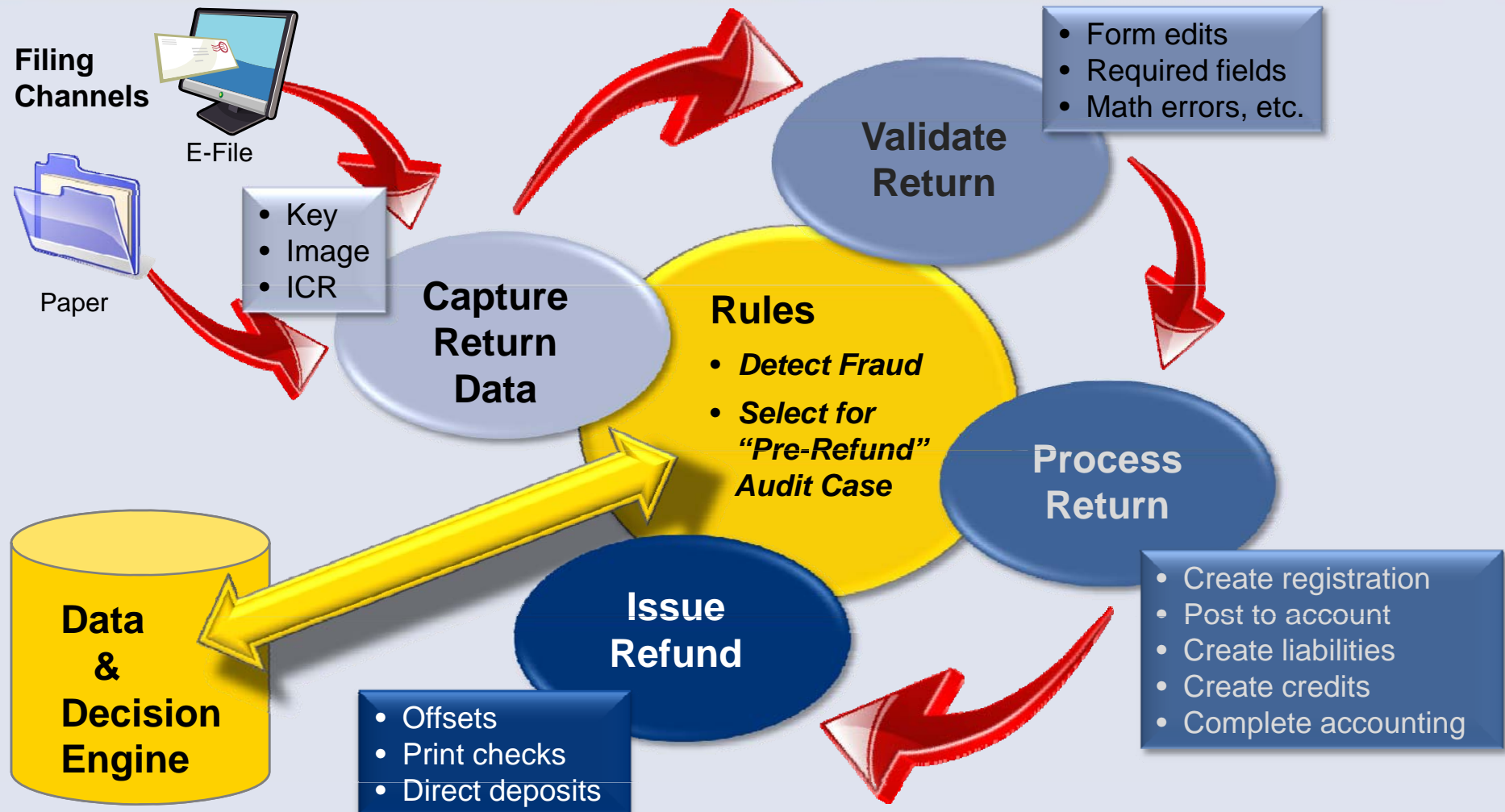
- Notices to ask taxpayers to respond
 - Confirm identity and TIN (SSN or ITIN)
 - Confirm claims on refundable credits
- Careful messaging:
 - *“Thank you for understanding...”*
 - *“These precautions are necessary...”*
 - *“We need to protect taxpayers against rising identify theft...”*
 - *“We were not able to verify your Taxpayer ID number and/or specific credits through available means”*
 - *“Kindly contact the DOR (by phone # or web site) to provide verification, so that we may release your refund”*
- If no response, automate removal

What works? ... Effective Technology



- **Portfolios and data matching capabilities**
 - Assemble and use various sources of data
- **Decision engine**
 - Flexibility and full configurability in rules definition
- **Case tracking and review tools**
 - Multiple worklists for different pools of cases
 - Ability to “release” or “reprocess” cases in bulk
- **Detailed performance tracking for monitoring**
 - Refund turnaround time
 - Results by pattern/rule
- **Alongside ITS with new integration technologies**

Refund Process Flow



Expected/Target Metrics



Percentage of refund request returns that can be safely “pre-validated” through various means, prior to receipt	92-96%
Percentage of refund requests that are not pre-validated but which can be subsequently released automatically when filed, after detailed rules evaluation (confirming identity and credit claims, assessing risk, etc.)	75%+
Percentage of all refund requests that are not pre-validated and cannot be released automatically when filed through detailed rules, and where return is suspended and taxpayer is contacted for confirmation of identity, credits, etc.	1% to 2%
Percentage of all refund request returns and refunded amount that is fraudulent or otherwise invalid and can be largely automatically prevented from being issued	0.75% to 1.5%

Making Improvements

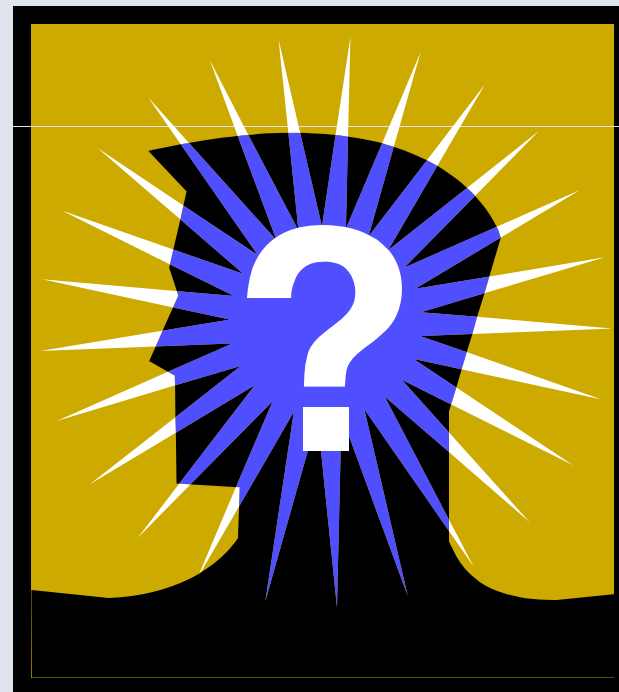


- Evaluate current practices
 - Assess risk exposure
 - Establish baseline performance metrics
- Assemble multi-year plan
 - Plan for incremental, continuous improvement
- Make targeted annual adjustments to:
 - Process
 - Organization/Roles
 - Technology
 - Risk models; Business rules; Use of data

Questions and Contact Information



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Revenue Solutions, Inc.



Mission Statement

“Assist revenue agencies to maximize collections, increase compliance, improve customer service and streamline operations through the use of enabling technologies, in particular, integrated tax and tax data warehouse solutions”



www.RevenueSolutionsInc.com

- Incorporated in May 1996
- Headquartered in Pembroke, MA with Solution Centers in Roseville, CA and Charlotte, NC
- Dedicated exclusively to providing products & services to tax agencies
- Over 200 people with 800 combined years of revenue systems consulting
- Deep tax administration domain expertise
- Software Solutions for Integrated Tax and Integrated Compliance Management
- Committed to client partnerships in delivery of strategic projects

