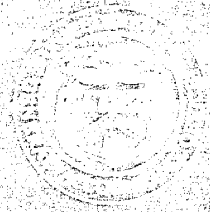


URBANPOOR

Tenant Income
Misreporting Deprives
Other Families of
HUD-Subsidized
Housing



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Human Resources Division

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July 17, 1992

The Honorable Alan Cranston
Chairman, Subcommittee on Housing
and Urban Affairs
Committee on Banking, Housing, and
Urban Affairs
United States Senate

Urban Poor:
Tenant Income
Misreporting Deprives
Other Families of
HUD-Subsidized
Housing

Dear Mr. Chairman:

This report responds to your request that we undertake, with the concurrence of the Joint Committee on Taxation, a study to determine whether the Department of Housing and Urban Development has sufficient internal controls to ensure that families in federally subsidized public and Section 8 housing accurately report their income.

In the report, we recommend that the Congress amend the Internal Revenue Code to authorize the Department temporary access to federal income tax data with which to verify family income, and that the Department take certain measures in preparation for such access.

As agreed with your office, we are sending copies of this report to the Chairman, Joint Committee on Taxation. Copies also are being sent to the Chairmen and Ranking Minority Members of the Senate and House Committees on Banking, Housing, and Urban Affairs, the Senate Committee on Finance, and the House Committee on Ways and Means; the Secretary of Housing and Urban Development; the Commissioners of Internal Revenue and Social Security; the Director of the Office of Management and Budget; and other interested parties. It will be made available to others on request.

This report was prepared under the direction of Joseph F. Delfico, Director, and Gregory J. McDonald, Associate Director, Income Security Issues. If you have questions about it, Mr. Delfico can be reached on (202) 512-7215. Other major contributors are listed in appendix V.

Sincerely yours,

Lawrence H. Thompson

Lawrence H. Thompson
Assistant Comptroller General

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Executive Summary

Purpose

The Department of Housing and Urban Development (HUD) provides more than \$13 billion in annual rent subsidies to nearly 4.6 million needy families in public and Section 8 housing. Despite these programs, at least 8 million very low-income families are without housing, live in substandard or overcrowded housing, or spend more than 30 percent of their incomes for housing. Recent studies by HUD's Office of Inspector General have disclosed significant underreporting of household income, resulting in HUD paying excess subsidies and providing subsidized housing to families whose incomes exceed eligibility limits, thereby depriving needier families of such housing.

Because of his concerns about household misreporting of income and its effects on HUD's rent subsidies, the Chairman of the Subcommittee on Housing and Urban Affairs of the Senate Committee on Banking, Housing, and Urban Affairs asked GAO to determine whether HUD had sufficient internal controls to ensure that subsidized households properly report their income. Specifically, the Subcommittee asked GAO to (1) conduct a one-time computer match of subsidized household records with federal tax records to determine the extent to which households accurately report their income and (2) determine the feasibility of HUD using federal tax data to verify household income. (See ch. 1.)

Background

Public housing is owned and operated by local public housing agencies, while Section 8 housing consists of private rentals whose owners agree to rent to low-income families. Nearly 4,100 public housing agencies and more than 20,000 private housing management agents administer these programs, processing and approving housing requests, verifying families' self-reported income, and ensuring that HUD's subsidies are accurate.

To qualify for subsidized housing, families must meet local limits for low or very low household income. Eligible families generally pay 30 percent of their income (after adjustments for allowances and expenses) as rent and must report promptly any changes in their income, family size, or allowable expenses. Public housing agencies and management agents annually recertify households and in the interim may adjust monthly rents on the basis of household-reported income changes.

To meet the Chairman's objectives, GAO developed a data base of 174,523 records containing wage, interest, and dividend income information as reported by subsidized households for the period January 1989 through June 1990. GAO computer-matched these records with income data in

third-party-reported tax records maintained by the Internal Revenue Service and the Social Security Administration. Because GAO could not refer its match results to HUD for follow-up, due to tax data disclosure restrictions, its results are characterized as "potential." GAO also assessed HUD's need to centrally automate public housing and Section 8 household data for matching with state wage and federal tax data. (See ch. 1 and app. I.)

Results in Brief

At a time when millions of needy urban poor—very low-income families and the homeless in central cities—are without decent, safe, and sanitary housing, many subsidized households may not be paying appropriate rents and less needy families may be occupying subsidized units. HUD lacks sufficient information to ensure that federally subsidized housing units are occupied by needy low-income families and that those living in such units are paying correct rents. Public housing agencies and management agents cannot effectively verify the accuracy of most subsidized households' self-reported wage, interest, and dividend income.

GAO's computer match of approximately 175,000 HUD-subsidized households' records (less than 4 percent of such records) with federal tax data revealed that, in 1989, 21 percent of the matched households may have understated their incomes to HUD by \$138 million. This would have resulted in potential excess federal subsidies of \$41 million. Of households that may have understated their incomes, 63 percent reported no wage, interest, or dividend income in 1989.

A centralized household income and eligibility verification system would help HUD ensure that households pay appropriate rents and that needy low-income households have access to subsidized housing units. After many false starts over the last decade and a half, HUD recently initiated steps to develop two centralized management information systems. A public housing system is to be completed in late 1992; a larger Section 8 system by 1995. By incorporating appropriate data safeguards in these systems and with authorizing legislation, HUD could gain access to federal tax data to computer-match with households' self-reported income and use these systems for income and eligibility verification purposes. This could significantly reduce the incidence of income underreporting and, in turn, considerably strengthen HUD's internal controls over its low-income housing assistance programs.

Principal Findings

Computer Matching Reveals Significant Differences in Reported Household Incomes

In its computer match of subsidized households for 1989, GAO found that 35,800 households had \$138 million in potential understated income—\$119 million in wages and \$19 million in interest and dividends. Among 12,400 households that had reported no income to HUD for 1989 and had been in subsidized housing since 1986 or earlier, 69 percent had wage, interest, or dividend income, not only in 1989, but also in at least 2 of the previous 3 tax years. GAO estimates potential excess rent subsidies to have been about \$41 million in 1989 for the matched households. As GAO's household data base represents fewer than 4 percent of HUD's 4.6 million subsidized households, the potential excess rent subsidies paid by HUD in 1989 could have been much larger. Some households' incomes as recorded in tax records might have required them to pay full market rent or made them ineligible for subsidized housing. (See ch. 2.)

HUD Needs Centralized Household Income and Eligibility Verification Systems

HUD's failure to discover underreporting of household income in its low-income housing assistance programs partly stems from a lack of centralized information systems. Despite numerous reports by HUD's Office of Inspector General, GAO, and others detailing these problems, HUD made little progress between 1975 and 1989 in developing such systems for the millions of individual records of household information maintained by public housing agencies and management agents.

In 1989, however, HUD contracted to computerize and centralize its public housing data by late 1992. It also hired consultants to study internal control weaknesses in the Section 8 program. In 1991, as a result of the consultants' recommendation, HUD initiated a multiyear system development plan to centralize management information for the Section 8 program. As conceived, this system would be able to computer-match Section 8 household annual wage data with state wage data by 1994. With appropriate data safeguards to preclude unauthorized disclosures of tax data and authorizing legislation, it could also match against federal tax data. HUD has told GAO that appropriate safeguards could be incorporated in both the public housing and Section 8 systems. (See ch. 3.)

Computer Matching With Tax Data Would Strengthen HUD's Ability to Identify Understated Income

Access to federal tax data would enable HUD to make housing subsidy payments more accurate and readily identify most instances of potential understating of household wage, interest, and dividend income for follow-up investigation. Such tax data would complement recently enacted legislation allowing HUD and local authorities to access state wage data.

Computer matching with federal tax data would be the most comprehensive way for HUD to obtain reliable information leads for later investigation and verification of true household income. Use of state wage data alone will not identify the full range of potentially understated wage, interest, and dividend income. State data exclude certain types of earnings, including self-employment earnings and unearned income, such as interest and dividends. Other major, federally funded, needs-based programs already are authorized access to federal tax data for income and eligibility verification purposes. From these, significant monetary and other benefits have been reported or are anticipated.

But before HUD can be given access to tax data, it needs to ensure that the centralized information systems it now has under development include appropriate data safeguards to prevent unauthorized disclosures of tax information. Also, while the use of tax data for income and eligibility verification in other federal needs-based programs has proven cost-beneficial, HUD should conduct a cost-benefit analysis of using tax data to identify household income misreporting to aid the Congress in its deliberation of HUD's access to tax data. (See ch. 4.)

Recommendations to the Agency

GAO recommends that, to gain access to tax data, HUD (1) incorporate in its assisted housing information systems appropriate data safeguards and (2) conduct a cost-benefit analysis of using tax data to identify subsidized households' misreporting of income and report the results to the Congress. (See ch. 5.)

Recommendations to the Congress

GAO also recommends that, when HUD's centralized public housing information system is fully operational and data safeguards are in place, the Congress amend the Internal Revenue Code to allow HUD temporary access to federal tax data to validate its cost-benefit analysis. If HUD's use of tax data is indeed cost-beneficial, the Congress should further amend the Internal Revenue Code to broaden and make permanent HUD's access to federal tax data, including its use in the Section 8 program when that

program's centralized management information system becomes fully operational. (See ch. 5.)

Agency Comments

HUD generally agrees with GAO's recommendations that its automated systems be designed to include appropriate safeguards and to permit effective use of federal tax data. But HUD disagrees as to the need to conduct a cost-benefit analysis before being granted access to tax data. IRS opposes granting HUD access to federal tax data because of IRS's continuing concern about the potential negative impacts of using tax data for nontax administration on the nation's tax system. The Department of Health and Human Services had no comments to offer. (See ch. 5.)

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Abbreviations

ASTEC	Automated System for Tenant Eligibility Certification
CFS	Control File Subsystem
DEFRA	Deficit Reduction Act of 1984
HHS	Department of Health and Human Services
HUD	Department of Housing and Urban Development
IRS	Internal Revenue Service
MA	management agent
MTCS	Multifamily Tenant Characteristics System
NHP	NHP Property Management, Inc.
OIG	Office of Inspector General
PHA	public housing agency
SSA	Social Security Administration
TRACS	Tenant Rental Assistance Certification System
VA	Department of Veteran Affairs

Introduction

The Department of Housing and Urban Development (HUD) provides more than \$13 billion annually in rent subsidies to about 4.6 million families residing in assisted housing. Household eligibility for assisted housing and the amounts of rent subsidies depend almost exclusively on tenants' self-reported income. Concerns in the early 1980s about inaccurate beneficiary income reporting in other federal needs-based programs led the Congress to enact legislation granting federal and state program administrators access to federal tax data for income and eligibility verification purposes. In recent years, similar income misreporting problems in HUD's assisted housing programs have been identified by its Office of Inspector General (OIG) through a series of computer-matching studies using state wage data. In response to a request from the Chairman of the Subcommittee on Housing and Urban Affairs, Senate Committee on Banking, Housing, and Urban Affairs, we examined HUD's internal controls over households' income reporting and the feasibility of using federal tax data to help verify household income.

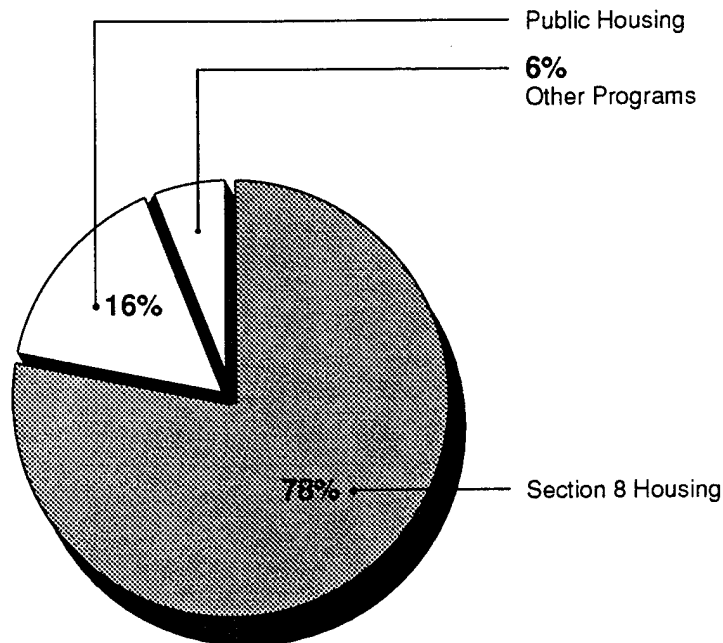
HUD and Its Assisted Housing Programs

HUD is responsible for the proper expenditure of federal funds and ensuring that all statutory, regulatory, and administrative requirements for its assisted housing programs are met. It does this through its headquarters, regional, and area offices and its OIG. At HUD headquarters, responsibility for assisted housing programs is divided between two Assistant Secretaries.

The Assistant Secretary for Public and Indian Housing is responsible for management of the Public Housing, Indian Housing, and Section 8 Existing Housing Programs, including the Section 8 Rental Certificate, Rental Voucher, and Moderate Rehabilitation Programs. The Assistant Secretary for Housing/Federal Housing Commissioner is responsible for management of the Section 8 New Construction and Substantial Rehabilitation Programs. These are HUD's major assisted housing programs and are described in more detail below; other assisted housing programs include rental housing assistance and rent supplements.

Local administration of HUD's assisted housing programs is carried out through some 4,100 local government agencies, called public housing agencies (PHAs), and more than 20,000 private owners or managers of rental properties, called management agents (MAs). As shown in figure 1.1, Section 8 and Public Housing accounted for 94 percent of all HUD housing subsidies in fiscal year 1990.

Figure 1.1: Proportion of HUD Housing Subsidy Payments, by Housing Program (Fiscal Year 1990)



Section 8 Assisted Housing

First authorized in 1974 under section 8 of the U.S. Housing Act of 1937, Section 8 assisted housing consists of several major components: Rental Certificate, Rental Voucher, Moderate and Substantial Rehabilitation, and New Construction. Each program is designed to aid a category of families that HUD calls very low-income—those whose incomes are at or below 50 percent of the median income for the locality—in obtaining decent, safe, and sanitary housing in private accommodations. Some programs also aid low-income families—those whose incomes are between 50 and 80 percent of the median.

The Rental Certificate Program places the choice of housing in the hands of the assisted family. Under this program, an eligible very low-income family is issued a Certificate of Family Participation. The family then locates a suitable dwelling unit within or outside the rental housing market of a PHA's jurisdiction. If the unit meets the program's fair market rent and other requirements, the family and owner sign a lease for the family's share of the monthly rent—generally 30 percent of the family's adjusted

monthly income.¹ The PHA then contracts with the owner for the fair market rent and pays the remainder of the monthly rental amount.

The Section 8 Rental Voucher Program, while similar to the Rental Certificate Program, gives assisted families a greater choice in selecting a rental unit. The voucher permits families to choose units with rental rates above or below the local fair market rents as well as rent units outside the jurisdiction of the PHA. Monthly housing assistance payments are based on the difference between a payment standard for the area, which is based on the average fair market rent for a particular size unit—not the actual rent—and 30 percent of the family's adjusted monthly income. The family then pays the balance of the rent.

For example, if a four-member family's adjusted monthly income is \$1,000 and the local subsidy payment standard is \$500 for a rental unit to accommodate this size family, the Section 8 voucher would be valued at \$200 (\$500 less 30 percent of the family's income, or \$300). If the family then rents a dwelling unit for an amount higher or lower than \$500 per month, the HUD subsidy/voucher amount remains at \$200 and the family pays the balance of the rent, even if that amount represents more or less than 30 percent of its adjusted income.

The Section 8 programs involving newly constructed and moderately or substantially rehabilitated housing also cover privately owned and managed units. Very low-income families are eligible to occupy the assisted units. Nationwide, no more than 5 percent of the available subsidized units may be rented to low-income families.

Public Housing

The Public Housing Program, the oldest of the assisted housing programs, was established by the U.S. Housing Act of 1937. Under the program, PHAs and Indian housing authorities develop, own, and operate low-income public housing projects, financing them through the sale of tax-exempt obligations and, in recent years, non-tax-exempt, short-term Treasury notes. In lieu of a unit-based rent subsidy, HUD provides two kinds of direct financial assistance to PHAs: (1) federal grants to cover the capital costs of constructing and modernizing public housing projects and (2) annual contributions for operating and maintaining the projects. Low-income families occupying units in these projects generally pay 30 percent of their adjusted monthly income as their rent contribution.

¹Adjusted monthly income, in general, is reportable income of all household members, excluding earned income of members under age 18, less allowances for certain expenses such as medical and child care.

Assisted Housing Subsidies Increase, Yet Millions More Need Housing They Can Afford

With the introduction of Section 8 housing programs in the mid-1970s, HUD's spending for housing assistance to needy families has grown dramatically. As shown in figure 1.2, HUD's spending for housing assistance subsidies has tripled from about \$4.5 billion in fiscal year 1980 to more than \$13.5 billion in fiscal year 1990. During this same period, however, the number of subsidized household units increased less dramatically, from about 3.3 million to about 4.6 million. HUD's budget estimates for fiscal year 1992 call for subsidies of more than \$16.5 billion for more than 4.6 million units.

During the last decade, subsidies in the Section 8 housing assistance programs increased five-fold while Public Housing Program subsidies nearly doubled. In fiscal year 1980, rent subsidies under the Public Housing and Section 8 Programs were nearly equal, at just over \$2 billion. But by fiscal year 1990, Section 8 subsidies reached nearly \$10.6 billion, while public housing subsidies totaled about \$3.9 billion, as shown in figure 1.3.

Chapter 1
Introduction

**Figure 1.2: HUD Assisted Housing
Subsidies and Units (Fiscal Years
1980-90)**

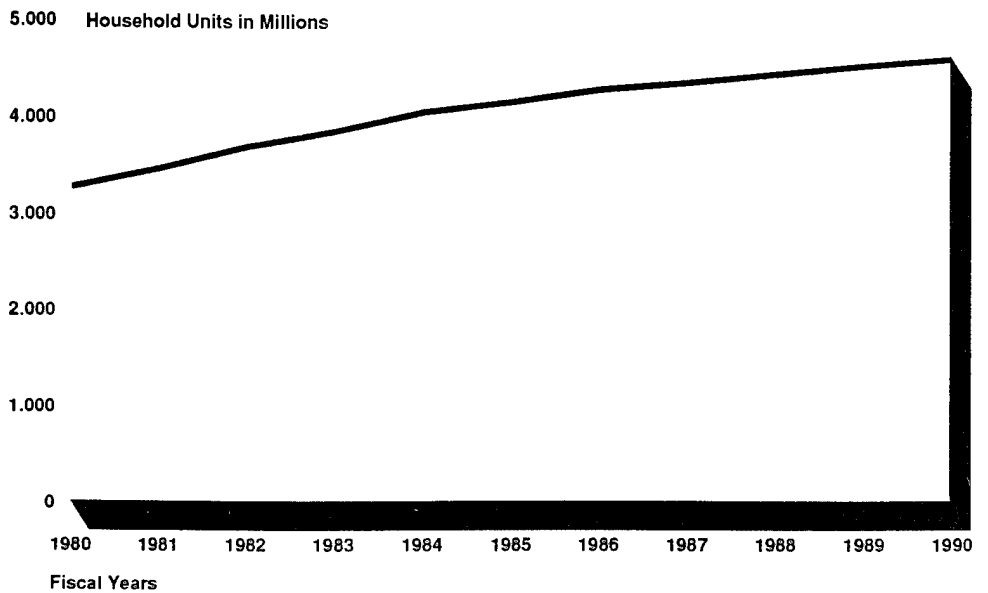
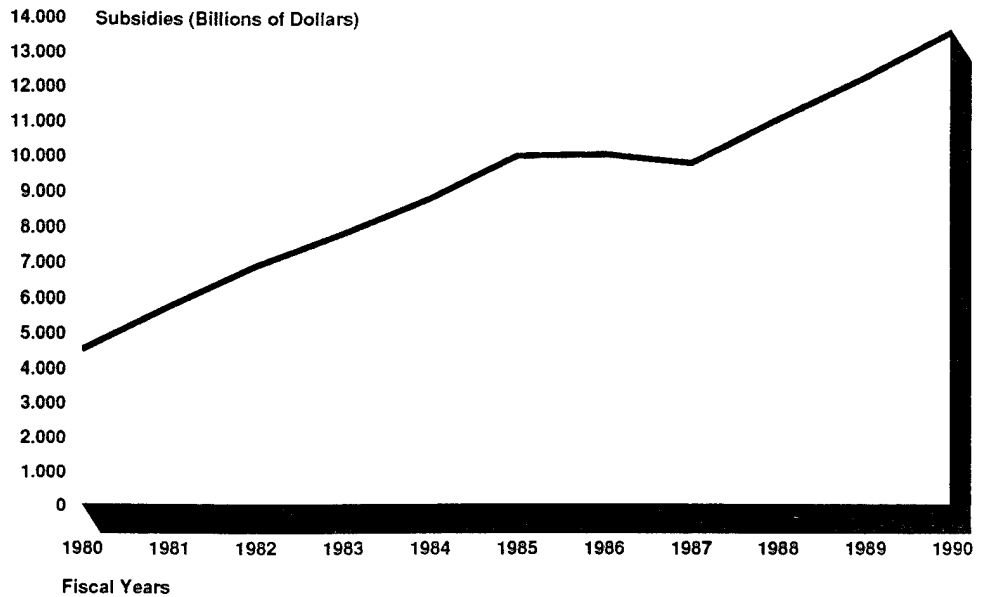
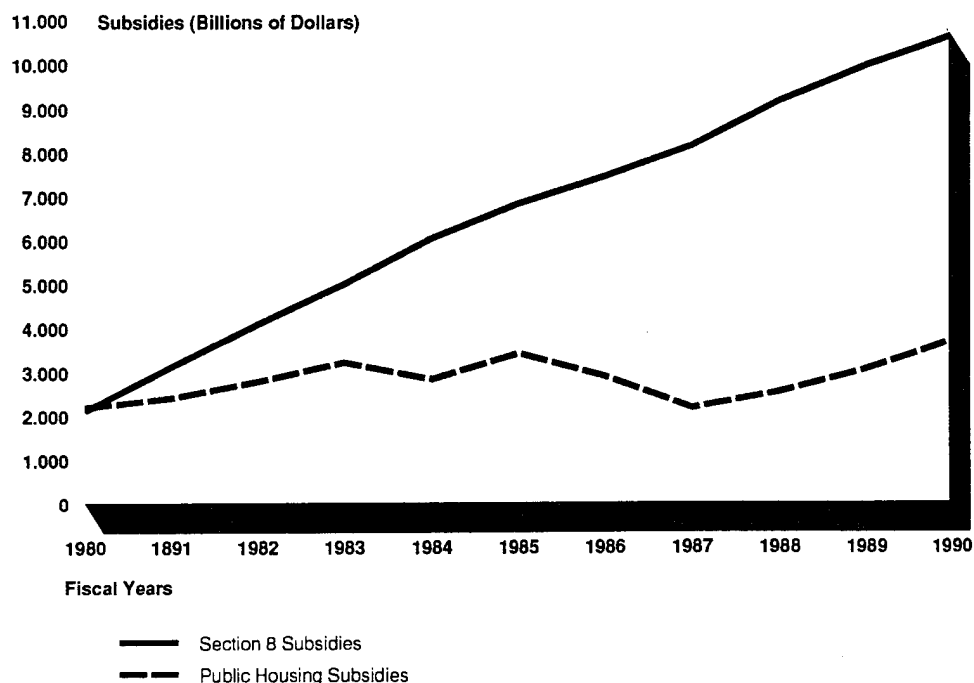


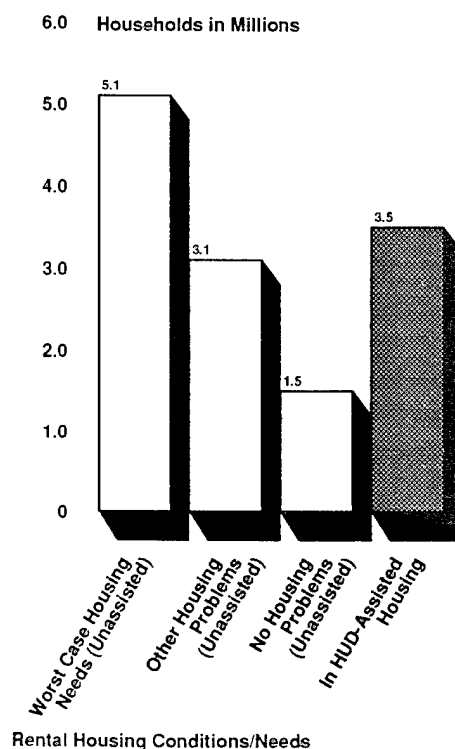
Figure 1.3: Subsidy Growth in HUD Assisted Housing Programs (Fiscal Years 1980-90)



Although HUD subsidies help provide 4.6 million families with housing they can afford, many more families in the United States are in need of subsidized housing. In June 1991, HUD reported to the Congress that, of the 13 million very low-income households in rental housing in 1989, an estimated 5 million lived in severely substandard housing or had rent burdens exceeding 50 percent of their reported income. These 5 million renters, categorized as having "worst case" housing problems, received no financial assistance from HUD. Nearly three-fifths were poor, having incomes below 25 percent of the area median family income, and more than half—2.6 million—lived in central cities. HUD also reported that an additional 3 million unassisted very low-income renters had other housing problems, such as overcrowding, structural inadequacies, or rent burdens between 31 and 49 percent of reported income. (See fig. 1.4.) None of the above estimates included homeless persons, whose population ranged from 230,000 to 750,000, according to the HUD report.²

²Priority Housing Problems and "Worst Case" Needs in 1989: A Report to Congress (HUD, June 1991).

Figure 1.4: Housing Conditions/Needs of Very Low-Income Renters (1989)



Note: The "Worse Case Housing Needs" category includes households in severely inadequate housing and/or having a rent burden greater than 50 percent of total reported household income. The "Other Housing Problems" category includes households in moderately inadequate or overcrowded housing or having a rent burden between 31 and 49 percent of total reported household income. This chart excludes the estimated 230,000 to 750,000 homeless persons in need of housing.

Source: Priority Housing Problems and "Worst Case" Needs in 1989: A Report to Congress (HUD, June 1991).

Importance of Accurate Household Income Reporting

With HUD annually spending several billion dollars in rent subsidies and millions of unassisted families in need of low-income housing, it is important that only eligible families occupy subsidized units. Thus, it is critical that families applying for and receiving rent subsidies accurately report their incomes to PHAS and MAS.

Applicants for HUD-assisted housing go through an admission process that includes two basic criteria for determining eligibility—income and family status. Using the information applicants report, PHAS and MAS project the

family's income for the next 12 months—adjusting for allowances and expenses—and compute the monthly rent subsidy. Although policies may vary among PHAS and MAS, families generally are required to report changes in income and family status during the year so that their rental payments can be adjusted. MAS are required to obtain third-party verification of subsidized families' self-reported income sources. PHAS also are required to verify family income and composition. However, depending on the program and local policies, PHAS can rely on the statements by the family, provided they have supporting documentation. Both PHAS and MAS are required to recertify each family's continued eligibility at least annually, and otherwise as circumstances dictate. Thus, a family's income has a direct bearing on its eligibility and rent subsidy. Information on assisted families' initial eligibility determination and subsequent recertifications is contained in household files maintained by PHAS and MAS.

Recent OIG Computer Matches and Income Verifications Identify Household Misreporting of Income

Recent HUD-OIG computer matches and income verifications identified over \$36 million of misreported family income. Between 1985 and 1991, the OIG issued 15 reports on computer matches of assisted housing programs. The matches covered 13 geographically dispersed locations and involved about 68,000 families, or fewer than 2 percent of HUD's 4.6 million subsidized families nationwide. The OIG matched household-reported wage data with state unemployment insurance data bases and several federal departments' and agencies' payroll data bases.

In the aggregate, the OIG results identified about 2,500 families, or about 4 percent of those matched, that underreported their wage income by over \$36 million, resulting in an estimated \$9 million in excess HUD subsidies. These estimates of underreported income and excess subsidies were conservative, because the OIG's studies were limited to (1) households that had valid social security numbers for computer matching with state wage data bases and (2) matched households whose underreporting generally exceeded various OIG-established dollar thresholds ranging from \$3,000 to \$15,000 annually.

Inaccurate Income Reporting in Other Needs-Based Programs Prompts Congressional Action

Like HUD's assisted housing programs, other federal needs-based programs rely on beneficiaries' accurate self-reporting of income in determining program eligibility and benefit payments. By fiscal year 1983, the federal government was spending about \$65 billion annually on needs-based benefit programs, including HUD's assisted housing. Anticipating the potential monetary benefits of improved payment integrity through better income verification, and in the face of mounting federal budget deficits,

the Congress enacted the Deficit Reduction Act of 1984 (DEFRA). Section 2651 of DEFRA amended section 6103(l)(7) of the Internal Revenue Code to give selected federal and state agencies access to federal tax data for income and eligibility verification purposes for selected needs-based programs, among them Aid to Families With Dependent Children, Supplemental Security Income, Food Stamp, and Medicaid. HUD's assisted housing programs were not included.

Federal and state managers of the programs included under DEFRA are required to verify claimants' reported information on earned and unearned income, using (1) earnings and pension income data reported to the Social Security Administration (SSA) and (2) interest, dividends, and other unearned income data reported to the Internal Revenue Service (IRS). This tax information cannot be used, DEFRA specifies, to determine or deny a person's benefit entitlement or payment amount without the program administrator first verifying the accuracy of the tax information and allowing that person to exercise his or her due process rights to challenge the verified information.

Since DEFRA's enactment in 1984, one additional federal agency has been granted access to federal tax data for income verification purposes. In November 1990, as a result of a 1988 GAO report,³ the Department of Veterans Affairs (VA) obtained authority to access tax data to match against VA pension and certain other VA benefit programs. The Congressional Budget Office estimated that giving VA access to this data could result in net savings of \$639 million in benefits to ineligible beneficiaries over a 5-year period. In July 1991, VA's initial computer match with IRS tax data indicated that 116,000 beneficiaries did not report about \$338 million in unearned income received in 1989. VA is following up on its match results to determine the actual extent of income underreporting and program savings through repayment of unentitled benefits, reductions of ongoing benefits, and termination of ineligible beneficiaries.⁴

Objectives, Scope, and Methodology

The Chairman, Subcommittee on Housing and Urban Affairs, Senate Committee on Banking, Housing, and Urban Affairs, asked us to assess the adequacy of HUD's internal controls over household income reporting in its subsidized housing programs. We also were asked to determine the

³Veterans' Pensions: Verifying Income With Tax Data Can Identify Significant Payment Problems (GAO/HRD-88-24, Mar. 16, 1988).

⁴Veterans' Benefits: Millions in Savings Possible From VA's Matching Program With IRS and SSA (GAO/HRD-92-37, Dec. 23, 1991).

feasibility of using federal tax data to verify household income. In requesting this review, the Chairman asked that we conduct a one-time computer match and in doing so,

- assemble as much housing program data as are readily available that would provide a fair assessment of the extent of income reporting problems and
- base our assessment on comparisons with earned and unearned income as reported to IRS (and SSA).⁵

GAO is permitted to access tax information for its audits only to the extent that the agency being audited may do so, unless GAO is acting as an agent of an authorizing congressional committee. HUD is not authorized to use federal tax information in auditing and administering its housing programs. Therefore, the Chairman asked the Joint Committee on Taxation to designate GAO as the Joint Committee's agent, pursuant to section 6103(f)(4)(A) of the Internal Revenue Code of 1986, as amended, to conduct our review for the Senate Subcommittee on Housing and Urban Affairs. The Joint Committee authorized us to use only such tax information as was necessary to evaluate the accuracy of income reported by HUD subsidized households. We also were subject to all Internal Revenue Code restrictions that apply to disclosure of tax information.

HUD lacks a centralized data base containing all assisted households. Therefore, to conduct our study, we used three readily available automated household data bases covering portions of the assisted housing population. These data bases—one public and two Section 8 housing—contained computerized household data extracted from HUD forms and were obtained from HUD and NHP Property Management, Inc., one of the largest managing partnerships for Section 8 housing. In matching these files with federal tax data, we used only HUD household records with valid social security numbers for household members age 18 or older.

The three data bases yielded suitable records for a total of 174,523 subsidized households—that is, households where all members age 18 and over had valid social security numbers—for computer matching purposes. One data base—HUD's Multifamily Tenant Characteristics System (MTCs)—consisted of national data from over 400 midsize PHAS on families

⁵SSA initially processes the earned income data reported by third-party payers and then forwards these data to IRS for federal income tax administration and enforcement purposes. In this process, SSA acts as an agent for IRS.

residing in public housing.⁶ It contained 162,371 suitable household records. The other two data bases—NHP's and HUD's Automated System for Tenant Eligibility Certification (ASTEC)—consisted of both national and HUD Region III data from MAS administering Section 8 housing projects.⁷ These contained 7,374 and 4,776 usable, unduplicated household records, respectively. The income data in the MTCS data base covered the period of July 1989 to June 1990;⁸ data in the NHP and ASTEC data bases covered calendar year 1989.

To identify potential income-reporting differences, we computer-matched our three data bases with wage income data maintained by SSA and interest and dividend income data in tax records maintained by IRS for calendar year 1989. In doing so, and to ensure that our results would be conservative, we excluded differences that were outside upper and lower dollar thresholds we established.⁹ We then estimated the effects of the remaining potential income differences on HUD's annual rent subsidies. Because the Internal Revenue Code precludes us from disclosing any person's individually identifiable earned or unearned income information obtained from tax data, we were unable to validate the identified income differences by contacting the families involved or other third-party reporters of tax data. Thus, we report the income differences identified through our computer matches as being potential.

To test the reliability of the income data in the household data bases we used, we sampled 367 households from the three data bases. We obtained copies of household certification or recertification forms—HUD 50058 and 50059—prepared by PHAS and MAS, respectively, to verify the income data in our data bases. The limitations of our study and a description of the processes we used to assemble, match, and assess the household income data are described in appendix I.

⁶Each midsize PHA administers between 500 and 5,000 household units in one or more public housing projects.

⁷HUD's Region III includes the states of Delaware, Maryland, Pennsylvania, Virginia, and West Virginia, and the District of Columbia, and is headquartered in Philadelphia.

⁸The period of July 1989 to June 1990 was chosen for MTCS data to provide sufficient numbers of MTCS households for computer matching purposes. MTCS contained few households with initial certification or recertification dates before July 1989. Although this meant computer-matching MTCS and tax data for different time frames, the income differences resulting from the match, in our view, are conservative.

⁹We used an upper threshold of \$30,000 for all 1989 income differences and lower thresholds of \$1,000 for wages and \$200 for interest and dividend income. Most households with annual incomes or income differences at or above the \$30,000 threshold generally would be expected to pay full market rent, thereby removing them from a subsidized rent status. Also, annual income differences below the lower dollar thresholds, in most instances, would not be expected to be sufficient to warrant an upward adjustment of a household's rent contribution, thereby reducing HUD's rent subsidy amount.

To assess HUD's efforts to develop a centralized income reporting and eligibility verification system for its assisted housing programs, we interviewed various HUD headquarters officials, as well as representatives from Arthur Andersen and Company, HUD's contract consultant for the design of a Section 8 management information system. We also reviewed various HUD and HUD-OIG reports and documents.

In assessing the feasibility of HUD using federal tax data for income verification purposes, we addressed the various concerns of IRS and the Congress that surround any proposed use of tax data for nontax purposes. Our assessment paralleled the approach we used in assessing VA's use of tax data in its veterans' pension programs,¹⁰ and we updated our information where necessary.

Our review was conducted from September 1989 to December 1991 in accordance with generally accepted government auditing standards, with the following exception. We did not assess IRS or SSA internal controls over the computer-based data systems used in our study because our prior studies and those by IRS and SSA have determined that the data in these systems are generally reliable.

We requested comments from HUD, IRS, and the Department of Health and Human Services (HHS) on a draft of this report. HHS had no comments to offer. The HUD and IRS comments are summarized and evaluated in chapter 5 and presented in detail in appendixes III and IV.

¹⁰GAO/HRD-88-24.

Tax Data Reveal Substantial Household Misreporting of Income

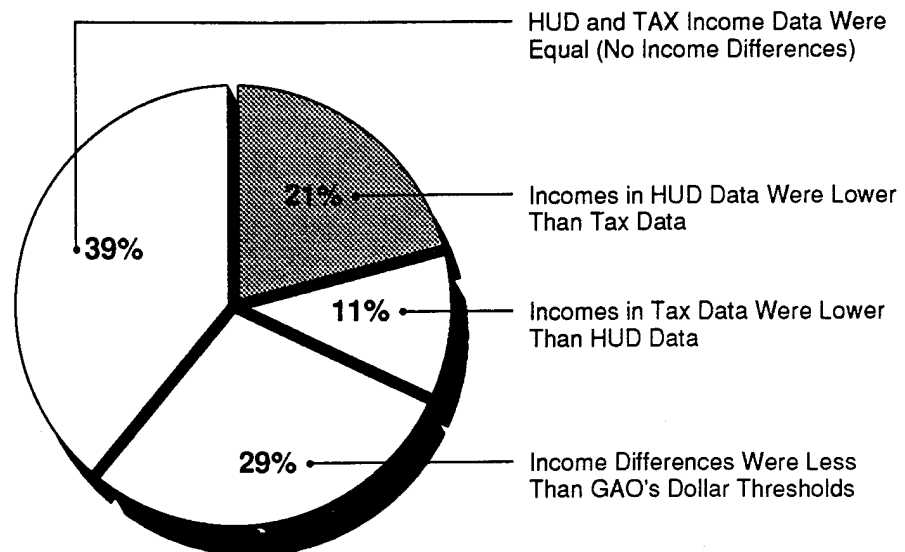
Our computer match of HUD household records and 1989 federal tax records revealed substantial income misreporting—totaling \$231 million—by families in HUD's assisted housing programs. About 21 percent of those matched, or about 35,800 households, may have underreported about \$138 million in income, thereby paying about \$41 million less rent than they should have. For nearly 69 percent of the 12,400 households that reported no wage, interest, or dividend income to PHAS and MAS in 1989 and had moved into subsidized housing in 1986 or earlier, tax records showed substantial income in 1989 and at least 2 of the 3 previous years. Interest and dividends accounted for as much as 49 percent of the misreported income among Section 8 households.

As the households we matched represented less than 4 percent of the 4.6 million subsidized households, HUD's potential excess rent subsidies in 1989 could have been much higher. Under current income verification procedures, HUD could not have identified the full extent of this potential income misreporting, because it lacks access to federal tax data and has no centralized way of matching with such data.

Substantial Income Misreporting by Subsidized Households

Our computer match with 1989 federal tax data revealed that 55,253 of the 174,523 households matched had substantial income differences—totaling \$231 million—between PHA or MA records and federal tax records. An additional 50,254 households, or about 29 percent of those matched, also had wage, interest, or dividend income differences, but these differences were less than the respective dollar thresholds—\$1,000 for wages and \$200 for interest and dividends—that we established to be conservative (see p. 22). Our match of subsidized household and tax records showed no income differences for 69,016, or about 39 percent of the households matched. Most of these, 98 percent, had no reported income from wages, interest, or dividends recorded in household or tax records. (See fig. 2.1.)

**Figure 2.1: Results of Matching
 174,523 Households With 1989 Tax
 Data**



Of the household records matched, 35,835, or about 21 percent, showed about \$138 million less income on PHA and MA records than on tax records. Understated wages accounted for about \$119 million, or about 87 percent of that total, averaging \$4,800 per underreporting household. Understated interest and dividend income, about \$19 million total, averaged \$1,500 per household. These figures suggest that such households potentially paid about \$41 million less rent than they should have. Moreover, to the extent that any of this misreporting occurred at the time of initial certification, ineligible persons or families may have received subsidized housing, thus depriving other qualified low-income families of access to scarce subsidized housing.

Of the 35,835 households that potentially understated their incomes in 1989, 22,300 households reported no wage, interest, or dividend income in 1989 but had income on 1989 tax records. A sizeable portion of these likely had income in previous tax years as well. Of the 22,300 households, 12,398 had been in subsidized housing since 1986 or earlier. Of these, 8,525, or nearly 69 percent, had wage, interest, or dividend income in 1989 and at least 2 of the 3 preceding tax years.

We did not confirm whether the 22,300 households that reported no wage, interest, or dividend income to PHAS and MAS in 1989 consistently reported

no income during earlier recertifications. However, as stated above, the results of matching these households with 1986-1988 tax data indicate that 8,525 of them had income for at least 2 of the 3 years. In the absence of a long-term loss of employment or a significant reduction in income-producing assets, we believe these households should have reported some form of current income—wages, interest, or dividends—during their 1989 recertifications. In light of the income history shown by the tax data, their failure to do so, in our opinion, provides a strong indication of a possible pattern of income misreporting.

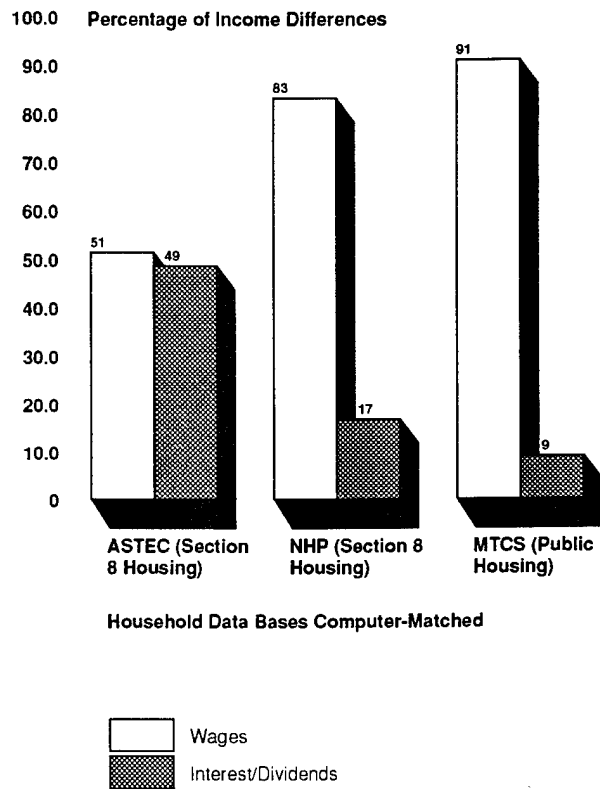
While our computer matching indicated significant understating of income, an additional 19,418 subsidized households' records, or 11 percent of those matched, showed \$92.9 million more income than recorded in federal tax records for 1989. Because we believe it unlikely that families in subsidized housing would knowingly report more income to the PHAS or MAS than they actually received, we attempted to determine, through random samples of the matched household data bases, whether income decreases were reported after the recertification dates. While 28 percent of the households having less income on tax records had interim income changes recorded in the PHA or MA records, the numbers of households that reported income increases and decreases were about evenly divided. Therefore, absent any information to the contrary, we can only conclude that not all of these households' actual income was reported by third-party payers to SSA or IRS or, if reported, was not recorded in the federal tax records we computer-matched.

Misreported Interest and Dividend Income Substantially Higher Among Section 8 Subsidized Households

Interest and dividends, which cannot be easily detected and verified without tax data, accounted for a substantially higher portion of the potential misreported income among the Section 8 households than the public housing households we computer-matched with tax data. Thus, programwide, total misreported interest and dividends could be very high, in that Section 8 households account for about 78 percent of the more than \$13.5 billion in annual HUD subsidies. As figure 2.2 shows, misreporting of interest and dividends for the two Section 8 data bases we computer-matched—ASTEC and NHP—represented about 49 and 17 percent, respectively, of all potential income misreporting by subsidized households in each data base. For the MTCs public housing data base, interest and dividends accounted for only about 9 percent of the potential misreported income identified.

Chapter 2
Tax Data Reveal Substantial Household
Misreporting of Income

Figure 2.2: Income Differences Due to Wages and Interest/Dividends
(Calendar Year 1989)



For additional information on the potential misreported income disclosed through our computer match with tax data, see app. II.

HUD Needs Centralized Eligibility Verification and Financial Control Systems

Income reporting and verification problems in HUD's multibillion-dollar federal housing assistance programs have been long-standing. Since the mid-1970s, HUD has been aware of misreporting of household income. The remedies—centralizing data on subsidized households and developing systems for eligibility verification and financial control—have been known to HUD officials for nearly a decade, but HUD's efforts to implement them have been slow. Plans have been revised repeatedly, and due to conflicting departmental concerns, proposed systems have been extensively reevaluated and redesigned. Some systems never proceeded beyond the conceptual stage.

The current Secretary of Housing and Urban Development, however, has affirmed his commitment to improving internal control and management of the assisted housing programs, giving priority to systems development. He has assigned to HUD's Chief Financial Officer the responsibility for ensuring that this objective is achieved. Comprehensive efforts are underway to develop centralized data systems for both the Public Housing and Section 8 Programs. In fiscal year 1992, HUD expects to be able to computer-match reported household income of public housing assistance applicants with other income data bases for verification of eligibility and to do the same for the Section 8 program by 1995.

Problems Reported, Remedies Suggested Over Many Years

Over the last decade and a half, numerous HUD OIG, GAO, and private consultant reports have addressed inadequacies in HUD's processes for household certification and income verification in its assisted housing programs. HUD was paying millions of dollars annually in excess subsidies, the reports estimated, because PHAS and MAS lacked effective means to detect and prevent households' underreporting of income. For example:

- Over 70 percent of subsidized households with wage or salary income understated their income in 1981, resulting in millions of dollars in excess subsidies, according to a study funded by HUD's Office of Policy Development and Research.¹
- HUD's Section 8 Existing Housing Program could use \$200 million in annual program funds more effectively if underreporting households accurately reported their income, the HUD-OIG concluded in a 1982 study based on prior audits.

¹Applied Management Sciences, Inc., *Cost of Procedural Errors in Section 8, Public Housing and Section 236 Rental Assistance Projects*, prepared under contract with HUD, Aug. 15, 1983.

In the last 6 years, numerous OIG computer matches and income verifications have provided additional evidence of households underreporting their income.

Over the past decade, remedies for this income misreporting problem have been suggested and tried, among them independently verifying household income by matching automated household files to state wage data bases. However, HUD's lack of a centralized system for recording household data has precluded effective use of such computer-matching techniques.

HUD's Failed Efforts at Automating Subsidized Household Information

For nearly as long as unreported household income has been a problem in the federal assisted housing programs, HUD has been attempting to develop a centralized data system to improve its management and internal control of the programs. With many false starts, the Department has had little success to date. Of eight systems begun since 1975, two never progressed beyond the conceptual stage, two more were terminated before they were fully implemented, and four are currently underway. The eight systems are described below and in the next section.

Low-Income Assisted Housing Program System

HUD's initial impetus for developing centralized data systems was to facilitate collection and maintenance of household characteristics data and housing occupancy information. Although it had always maintained demographic and occupancy data on its housing programs, the process was fragmented and ineffective. The administering HUD offices used different forms to obtain information from the various housing agencies. To centralize the process, HUD developed the Low-Income Assisted Housing Program System in the mid-1970s, using a private contractor to collect and enter the household data. However, data entry errors and other problems led to termination of this system in 1979.

Section 8 Payment Vouchering and Multifamily Certification/ Recertification System

Started in 1980 and terminated in 1982, the Section 8 Payment Vouchering and Multifamily Certification/Recertification System did not go beyond the conceptual stage. In addition to maintaining Section 8 household characteristics and housing occupancy data, it was intended to automate the subsidy payment and billing processes.

Automated System for
Tenant Eligibility
Certification

In the early 1980s, HUD's Region III, headquartered in Philadelphia, developed the Automated System for Tenant Eligibility Certification. This was a data system intended to perform Section 8 subsidy processing functions. By validating household certification data against the applicable billing information, ASTEC was to verify the accuracy of subsidy payments in Region III. However, concerns about the number of staff needed to enter the certification and billing data into ASTEC led to its termination as an operating system in 1989.²

Tenant Eligibility and
Housing Assistance
Voucher System

In continuing efforts to automate the certification processing functions, HUD decided to develop a Tenant Eligibility and Housing Assistance Voucher System in 1987. It was to have automated the data collection and input functions. But it never progressed beyond the conceptual stage, and in 1988 HUD redirected its efforts to other data systems projects that are still under development.

Now Under
Development,
Separate Systems for
Public and Section 8
Housing

Hoping to build on these early experiences in system development, HUD is now designing separate systems for its two major housing programs: the Multifamily Tenant Characteristics System for Public Housing and the Section 8 Information System for Section 8.

Multifamily Tenant
Characteristics System

Since its beginnings in 1982, MTCS has undergone several permutations. Originally, it was to be a management information system for Public Housing and Section 8 programs. Its centralized household data base was to include income data suitable for computer matching with other data bases. Unlike ASTEC or the Tenant Eligibility and Housing Assistance Voucher System, this system was not intended to include subsidy processing functions. HUD suspended development of MTCS in 1983 after complaints that plans for implementing the system were unclear and fragmented, and lacked departmental coordination. Its various intended users had different and conflicting objectives for it.

After a reevaluation to clarify the objectives, HUD resumed development of MTCS in 1985. But about 1987, the Department decided to separately automate the Section 8 subsidy and billing processes. HUD attempted to do

²Although ASTEC was no longer an operating system, we were able to use its archived Section 8 household data in our computer match with federal tax data (see ch. 2 and app. I).

so initially under the Tenant Eligibility and Housing Assistance Voucher System and later with the Tenant Rental Assistance Certification System (TRACS) and its Control File Subsystem (CFS), described below. MTCS then was developed for the Public Housing program only, and HUD began implementing the system in December 1989.

In February 1992, a contractor began collecting MTCS data on public housing households from 3,200 public housing agencies. These PHAS represent about 1.3 million public housing households nationwide. Also, in April 1992 HUD advised us that MTCS will be collecting household data for the Section 8 Rental Certificate and Voucher and Moderate Rehabilitation programs administered by PHAS. In fiscal year 1992, HUD plans to begin computer-matching MTCS household income data with state wage data. Safeguards needed for using federal tax data can be incorporated into MTCS if HUD is authorized access to such data, HUD officials say.

Section 8 Information System

HUD also is moving forward with development of the Section 8 Information System, a fully integrated, automated management information system for Section 8 housing programs. HUD plans to incorporate into this system two linked Section 8 system development efforts: the Tenant Rental Assistance Certification System and that system's Control File Subsystem. These are successors to the original conceptual design for the Tenant Eligibility and Housing Assistance Voucher System, which HUD refined in 1988. Individually and in combination, the components are expected to operate as follows:

- CFS will contain all the official project, building unit, and funding data needed to validate the accuracy of payment vouchers.
- TRACS will collect household certification data from MAS and verify it through matching with third-party sources. It will determine whether household incomes are within eligibility limits, housing subsidies are calculated correctly, and household data are consistent with CFS information.
- In combination, for the Section 8 programs, these components will also (1) generate subsidy payments, (2) determine potential funding shortfalls, and (3) provide household characteristics and financial data.

Initially scheduled for completion by 1989, CFS has undergone extensive evaluation, and project development has been slow. Now undergoing system testing at three HUD field offices, CFS is scheduled to be fully operational by October 1992. After establishing functional requirements

for TRACS, putting it through system design, and doing preliminary testing, HUD expects several modules of that system to be operational by December 1992. HUD's Office of the Chief Financial Officer, which is heading the TRACS/CFS development efforts, contends that these goals will be met.

The Section 8 Information System implementation plan was developed in 1991 by Arthur Andersen & Company, a consulting firm under contract with HUD. Estimated to cost about \$32 million, the multifunctional financial management system is planned to be completed by 1995. In addition to the TRACS/CFS subsidy processing components discussed above, this system is being designed to have the capability of on-line matching with external data sources, such as state wage and federal tax data bases, to verify household income. However, no specific plan has been developed for how this income-matching component, scheduled for completion in 1994, will function.

OIG's Program Integrity Division Director and HUD's Director of Financial Systems Integration question the feasibility of on-line matching with 50 or more state wage data bases. With respect to federal tax data, they suspect that IRS would be reluctant to allow such on-line matching capability. Instead, to perform computer matching, HUD might have to obtain magnetic tapes (or some other form) of the state wage data and IRS data bases, as is done by other federal and state matching agencies. Regardless of which matching method is used, the Section 8 Information System would incorporate the necessary safeguards for accessing federal tax data, HUD's Director of Financial Systems Integration stated.

Systems Development Given Priority by Secretary of HUD

The Secretary of Housing and Urban Development has made development of centralized household data systems for the assisted housing programs a major HUD priority. In an April 1991 letter to the Chairman of the Senate Appropriations Subcommittee on VA-HUD-Independent Agencies, he affirmed that HUD would have such systems for the Public and Section 8 Housing Programs by 1992 and 1995, respectively. In addition to improving internal control over the subsidy payment processes, these data systems would be used to computer-match household members' income with third-party income sources, the Secretary said. Because in the past HUD has had problems with its system development efforts, the Secretary has assigned to HUD's Chief Financial Officer the responsibility of ensuring that the new system development goals are met.

Accessing Tax Data to Verify Household Income

Traditionally, the use of tax information for nontax administration purposes has been and continues to be a sensitive issue. Both the Congress and the Internal Revenue Service are concerned about the effects of tax data sharing on the integrity of the federal income tax system, taxpayers' privacy, and their voluntary compliance with the tax system. The Congress has authorized IRS to share certain types of tax information with federal, state, and local agencies administering certain federal needs-based programs, but only for specific purposes. HUD has not received such authorization.

For HUD, access to tax data reported to IRS by third parties would provide the most efficient, effective, and economical means of verifying income reported by subsidized households and identifying erroneous reports. Such access, under the same procedures as those authorized by the Deficit Reduction Act of 1984, would enable HUD to improve its management of assisted housing programs. Moreover, it has not been demonstrated that allowing access to tax information for income verification in needs-based programs adversely affects voluntary tax compliance.

However, before the Congress allows HUD access to federal tax data, HUD would need to take several steps: (1) establish appropriate safeguards in its centralized public housing and Section 8 management information systems, now being developed, to preclude unauthorized disclosure of federal tax data; (2) improve its existing procedures for collecting income data from subsidized households; and (3) conduct a cost-benefit analysis of using tax data to identify errors in household income reporting.

Alternatives to HUD's Use of Tax Data

Use of federal tax data is one of several data sources we considered for HUD to verify households' self-reported income. Any source chosen should be

- readily accessible, preferably from an automated system;
- complete, including all major earned and unearned income; and
- accurate, in that no inherent bias exists in how the income is reported and some management effort has been made to ensure that the information is free from error.

Among the alternative data sources we considered were state unemployment compensation files and individual payers of interest and dividends, such as banks and corporations. Also, subsidized households

could be required to provide copies of their IRS form 1040 income tax returns.

Using State Wage Files for Nationwide Matching Is Impractical

While quarterly wage information in the files of individual state agencies that administer the Unemployment Compensation Program is automated, HUD and the PHAS would have to access it on a state-by-state basis. Although previous use of these files by us and HUD's Office of Inspector General resulted in some program savings, for HUD to do verification matches individually with each of the state wage files on a nationwide basis is impractical.¹ The HUD OIG's limited, but effective use of state wage data helped bring about passage of legislation in 1988 authorizing state agencies to disclose wage information to HUD and the PHAS.² However, as of September 1991, only 9 of the 50 states had negotiated agreements with PHAS to disclose state wage data for matching with local PHA records.

Additionally, while state wage data are more current than federal tax data, use of state wage data exclusively is inadvisable because they lack

- the completeness of federal tax data, as they exclude earned income for such categories of individuals as military personnel, federal civilian employees, railroad workers, and the self-employed, and
- information on unearned income such as interest and dividends, which can be obtained only from tax records.

Obtaining Interest and Dividend Data From Banks, Corporations Is Impractical

Another single source from which data are available on interest and dividends paid to subsidized household members is the individual payer of such income, including banks and corporations. But in the absence of voluntary disclosure by household members, it would be virtually impossible for HUD to independently identify and impractical for it to obtain such information from each institution.

Requiring Copies of Individual Tax Returns Not an Acceptable Option

HUD could require households to annually provide copies of their IRS form 1040 income tax return to verify self-reported income information. But this approach has the following drawbacks:

¹A Central Wage File for Use by Federal Agencies: Benefits and Concerns (GAO/HRD-85-31, May 21, 1985).

²Stewart B. McKinney Homeless Assistance Amendments Act of 1988, title IX, sect. 904.

- It does not provide the independent means necessary to verify household-reported income information because the income data on the tax return are also self-reported.
- The many HUD households having gross incomes under the established minimum for filing a return would have no form 1040 to provide.
- It would be intrusive, from a privacy standpoint, because the form 1040 contains more information than HUD would need to administer its low-income housing programs.
- Households that are intent on misreporting their incomes might either not file tax returns, file erroneous returns, or deny to the PHAS or MAS that they filed tax returns.

IRS, SSA Tax Data Best Alternative

Third-party-reported federal tax data are the best of several alternative sources of household income data for verification purposes. Both IRS and SSA maintain data on earned income, and IRS does so on unearned income, in automated, readily accessible files. Also, IRS and SSA data constitute the most complete national record on individual income, such as wages, pensions, annuities, interest, and dividends. Further, maximum accuracy is ensured. IRS and SSA data are reported, not by the taxpayer, but independently by third parties. These include employers and payers of pensions, interest, dividends, and the like—none of whom would have an incentive to report inaccurately. Moreover, both agencies check such data for accuracy before posting them to their files.

Using Tax Data to Enhance Program Effectiveness

The effectiveness of assisted housing programs is diminished if households underreport their income at the time of initial certification. By doing so, they may be charged incorrect rents and may deprive needier families of scarce subsidized housing. At this time, HUD cannot be sure that subsidized households properly report their income.

If HUD successfully implements eligibility verification systems for its Section 8 and Public Housing Programs, giving HUD managers access to tax data could enable them to

- detect whether information provided by households is different from that reported by third parties to IRS and SSA and act to resolve the differences,
- better control subsidies paid to PHAS and MAS, and
- ensure that needier families have access to scarce subsidized housing.

Benefits Versus Costs of Using Tax Data

Because HUD lacks a centralized source of household information, insufficient data exist to conclusively determine or accurately estimate the costs and benefits to HUD from using tax data to identify households that underreport their incomes. However, previous studies and estimates of using federal tax data for income and eligibility verification indicate that such activities can be carried out cost-effectively. For example:

- On the basis of our 1988 report on VA's pension program,³ the Congressional Budget Office estimated 5-year net savings of \$639 million through use of tax data for income verification in certain VA needs-based programs.
- In that same report, we also pointed out that as a result of computer-matching with IRS unearned income data, SSA projected in 1986 that it would save \$50 million over a 2-year period through recoveries of Supplemental Security Income overpayments. Additional savings of \$35 million would be realized through ongoing benefit payment reductions and persons' withdrawals from the program. This match, including follow-up action, would cost \$6 million, SSA estimated, resulting in a net savings of about \$79 million.
- HUD could save \$200 million annually by computer-matching Section 8 households' reported incomes with state wage and federal tax data and through greater internal control of subsidy payments, according to Arthur Andersen and Company, designers of HUD's integrated Section 8 program management information system.

Increase in Program Compliance by HUD Households Seen

If subsidized households knew that the income they annually report to HUD was subject to verification using third-party-reported tax data, compliance with program income reporting requirements likely would increase. Such data are reported by employers on IRS form W-2, by payers of pensions and annuities on IRS form W-2P, and by payers of interest and dividends on IRS form 1099. IRS uses the data to verify income that taxpayers report on their annual income tax returns.

Third-party-reported data offer the best tool for detecting income differences on a mass scale and increasing compliance with program income reporting requirements, IRS and our studies have shown. IRS estimates that its computer-matching of form 1099 data with individual form 1040 tax returns resulted in \$1.5 billion in additional income taxes collected in 1990.

³Veteran's Pensions: Verifying Income With Tax Data Can Identify Significant Payment Problems (GAO/HRD-88-24, Mar. 16, 1988).

In addition to facilitating verification, use of third-party-reported federal tax data could add an important fraud deterrent to HUD's internal controls. False claims or statements by subsidized households about their income could subject individuals to serious criminal penalties (up to a \$10,000 fine and/or up to 5 years' imprisonment) under sections 287 and 1001 of title 18, U.S. Code.

Data Confidentiality, Taxpayer Privacy, and Voluntary Tax Compliance Unaffected

The potentially harmful impact on compliance with the nation's tax law is the single most important issue in deciding whether HUD or other federal programs should be granted access to tax information. According to IRS, preserving the confidentiality of tax information is prerequisite to the integrity of the tax system, and using tax information for nontax purposes compromises that integrity. However, IRS acknowledges that there are no studies showing that use of such data for income verification purposes in federally funded, needs-based programs, when authorized by the Congress, adversely affected taxpayers' voluntary compliance with federal tax laws.

Currently, records of over 82 million recipients of federally supported benefit programs are matched or are eligible to be matched for enforcement purposes against third-party-reported tax data. Absent any studies to the contrary, we believe it is likely that an additional 4.6 million HUD household records would have little incremental effect on voluntary tax compliance, given appropriate safeguards.

Disclosure of Tax Data Allowed for Limited Use

Although the Internal Revenue Code generally prohibits disclosure of tax data, exceptions added to section 6103 of the Code allow disclosure to federal, state, and local agencies for limited uses. These include state and local tax enforcement and income and asset verification in specified entitlement programs. Users of tax data must conform to the Code's stringent safeguarding requirements. To this end, IRS has issued a booklet, "Tax Information Security Guidelines for Federal, State, and Local Agencies." All users of tax data are subject to (1) criminal penalties for illegal disclosures and (2) GAO and IRS on-site data security reviews. In centralizing its household data and developing its eligibility verification systems, HUD must be mindful of the Internal Revenue Code's safeguarding requirements.

Nonetheless, granting access to tax data, even data provided by third parties, presents a special case regarding privacy and confidentiality

issues. Taxpayers and third parties have little choice in reporting income information for tax administration purposes, because they are mandated by law to do so and are subject to criminal and civil sanctions if they do not. But once reported, should such information be used for other unrelated purposes, such as income verification in needs-based benefit programs? There is a trade-off between a potential increase in the efficiency and effectiveness of a legitimate government function and possible government intrusion into individuals' private lives. In enacting DEFRA in 1984, the Congress established a significant precedent. It decided in effect that it was in the public's best interest to authorize selected benefit programs to access third-party-reported tax data for income verification purposes. In amending the Internal Revenue Code in 1990 to allow VA access to tax data for its needs-based benefit programs, including veterans' pensions, the Congress continued this precedent.

Safeguards Required

The Congress intended that privacy safeguards be in place to protect the information used for verification and that individuals receive appropriate notification before any adverse action is taken to reduce or curtail benefits. In a 1986 report,⁴ we discussed improvements that federal agencies, including HUD, needed to make in administering their Privacy Act operations. For example, federal agencies should systematically provide training to ensure that personnel are aware of the act's requirements and Office of Management and Budget guidance pertaining to certain functions. These include automating systems of records and conducting computer matching programs. Thus, in considering gaining access to tax data, HUD should be prepared to demonstrate that it can provide applicable privacy safeguards in the systems it is developing.

Because of HUD's decentralized administration, the privacy issue poses a significant, but not insurmountable, barrier to HUD's qualification for tax data access. IRS tax disclosure officials advised us that HUD would need to (1) conform to IRS guidelines for safeguarding tax data to preserve the privacy and confidentiality of individually identifiable tax records and (2) incorporate such additional physical and procedural safeguards to preclude disclosure outside the Department to PHAS, MAS, or other third parties. To comply with these requirements, HUD believes it would need additional staff resources.

⁴Privacy Act: Federal Agencies' Implementation Can Be Improved (GAO/GGD-86-107, Aug. 22, 1986).

Preparing for Access to Federal Tax Data

In light of the above issues, HUD would need to take several actions before it could be authorized access to federal tax data. It would need to

1. complete development and implementation of its departmental automated information systems for Section 8 and Public Housing Programs. As discussed in chapter 3, these systems, which will contain centralized data on subsidized households' self-reported incomes, are needed to facilitate effective computer matching with federal tax data and other income data bases.
2. incorporate appropriate safeguards in these automated systems to preclude unauthorized disclosure of federal tax data. HUD thus would preserve taxpayer privacy and the confidentiality of tax data.
3. improve its procedures for collecting income information from households. Through a better standardization of the certification forms PHAS and MAS use, households' sources of income would be classified in a manner that best matches with third-party-reported tax data at IRS and SSA. Doing so would facilitate computer matching with third-party-reported tax data. In our own computer matching with tax data, we were unable to separately identify pension income data in HUD records because HUD permits such household income to be combined with social security and other benefits.⁵
4. conduct a cost-benefit analysis of using tax data to identify misreported household income, to aid the Congress in deliberations on the matter. In doing so, HUD would need to (a) estimate the costs of computer matching of the data, adjudicating any income misreporting, and investigating and prosecuting cases of fraud; (b) compare costs and benefits to matching against state wage data, which it already has legislative authority to access; and (c) weigh such other benefits as households' increased compliance with income reporting requirements and improved internal controls over assisted housing programs.

⁵In April 1992, HUD advised us that it is currently revising its tenant certification form (HUD-50058) used by PHAs to include the PHA-administered Section 8 programs and to make the income categories better support computer matching.

Conclusions, Recommendations, and Agency Comments

Conclusions

Inaccurate reporting of household income by those seeking or occupying assisted housing may deprive more needy low-income families of subsidized housing and affects the subsidies HUD pays. HUD's internal controls over its assisted housing programs could be strengthened if the Department had access to federal tax data. Computer-matching assisted households' income records against such data and, to the extent practical, state wage data offers great potential for identifying households that misreport their incomes.

Access to federal tax data is and should remain tightly controlled. However, in the past decade the Congress has responded to concerns about inaccurate income reporting in federal needs-based programs by allowing several federal agencies access to tax data for income verification purposes. The benefits in improved government operations from these agencies' use of tax data for non-tax-administration purposes more than offset the costs, and the concerns of IRS and others about possible adverse effects have not materialized. Thus, to reduce fraud, waste, and abuse in federally subsidized housing, HUD should be granted access to data that other departments and agencies have obtained.

However, HUD has much to do before it is authorized access to tax data. HUD's access should be contingent on its completing the development and implementation of centralized and automated eligibility verification and financial control systems. HUD also needs to establish and demonstrate effective implementation of data safeguards necessary to protect taxpayer privacy and prevent improper disclosures of tax data. These are especially needed in light of HUD's highly decentralized administration of assisted housing by more than 4,000 public housing agencies and 20,000 management agents. In addition, HUD needs to (1) revise its classification of household income sources to ensure compatibility with income classifications in federal tax data and (2) conduct a cost-benefit study of using tax data to identify subsidized households' misreported income. Once these are done, we believe HUD should be able to appropriately use and safeguard federal tax information.

Recommendations to the Secretary of Housing and Urban Development

To attain better reporting of household income information and facilitate future computer matching with federal tax data bases, we recommend that the Secretary

- ensure that HUD's assisted housing information systems containing centralized household data, now under development, adequately meet IRS safeguards against unauthorized disclosure of federal tax data and
- standardize the classification of income sources for all assisted housing programs to parallel sources of income derived from federal tax data bases.

We also recommend that the Secretary conduct a cost-benefit analysis of using tax data to identify misreporting of income by subsidized households, and report the results to the Congress.

Recommendations to the Congress

We recommend that, after HUD completes action on the above recommendations and fully implements its Multifamily Tenant Characteristics System for the Public Housing Program, the Congress amend the Internal Revenue Code to allow HUD temporary access to federal tax data so that it can validate the costs and benefits of using such data to identify household income reporting errors. If HUD subsequently demonstrates that its use of tax data is indeed cost-beneficial, the Congress should further amend the Internal Revenue Code to broaden and make permanent HUD's access to federal tax data, including its use in the Section 8 program when that program's centralized management information system becomes fully operational.

Agency Comments

We requested comments on a draft of this report from HUD, IRS, and HHS. HHS responded that it had no comments to offer at this time. The HUD and IRS comments and our evaluation of them are summarized below. Their written comments are presented in full in appendixes III and IV, respectively.

HUD Comments and Our Evaluation

The Secretary of HUD stated that, generally, the Department agrees with our recommendations that HUD (1) design its automated systems to include appropriate safeguards against unauthorized disclosure of federal tax data and (2) standardize the classification of income sources for all assisted housing programs to permit effective use of tax data. However, he disagrees with our recommendation that HUD conduct a cost-benefit

analysis of using the data, contending that this is unnecessary and impractical given our analysis and current restraints on the use of tax data. In addition, the Secretary favors our recommendation that the Congress grant HUD access to federal tax data. Matching federal tax data to a centralized tenant database, he stated, can significantly aid in promoting integrity in HUD's assisted housing programs. In this regard, the Secretary indicated that HUD has taken several other initiatives to promote tenant integrity (see app. III).

The Department's detailed comments focused on several specific areas, as follows.

Potential Versus Actual Income Differences

HUD argues that the actual income differences resulting from our computer matching with tax data might have been half the computed potential differences identified in our report had we been permitted to do the income verification process. To bolster its point, HUD cites its own OIG matches with state wage data that produced similar potential income differences, but that when verified were substantially reduced. Nonetheless, HUD believes this misreporting of income still represents a significant problem.

We agree that the actual income differences, had we not been precluded from doing verification, might have been less. However, neither HUD nor we have any way of knowing how much less. It is also possible that the actual differences could be much closer in number and amount to our computed potential differences because we validated all social security numbers used in our matches. The OIG did not use validated social security numbers in its state wage data matches, which resulted in actual income differences substantially lower than its initially identified potential differences.

Federal Tax Data Disclosure Limitations

HUD contends that it would be precluded from effectively using federal tax data if disclosure of this information would be limited to HUD employees. The Congress, HUD argues, must either increase HUD's budget to provide sufficient staffing for conducting the computer matching and tenant income verifications, or permit disclosure of the tax information to HUD contract agents or employees of state housing finance agencies. Currently, the Department has allocated 4 staff years to conduct matching projects by its OIG, with this function being transferred to the Office of Public and Indian Housing as of October 1, 1992.

HUD points out that DEFRA permits the Food Stamp and AFDC programs to disclose tax data to state employees. It believes this should also be allowed for its assisted housing programs and that the constraint we cite in chapter 4—incorporating such additional physical and procedural safeguards to preclude disclosure outside the Department to PHAS, MAS, or other third parties—is too restrictive. HUD believes IRS and the Congress should consider permitting disclosure to PHAS whose staff HUD views as employees of a government entity. HUD contends that, even if the Department does the actual income matches, the PHAS or MAS would have to perform any required checking with the income sources, give the tenants an opportunity to respond, and take whatever corrective actions may be necessary.

We agree that HUD will need additional resources to effectively use tax data for income verification purposes, but we disagree that HUD should be allowed to disclose tax data to its contract agents, employees of state housing finance agencies, or PHAS. Because of the large number of PHAS—some 4,100—and the tens of thousands of PHA employees who could be involved, HUD might have considerable difficulty assuring that tax data would be adequately safeguarded at the PHA level to preclude unauthorized disclosure or other misuse of the data. For this reason, we believe it is in HUD's and the federal government's best interests that the tax data be disclosed only to authorized HUD staff. Therefore, HUD should seek sufficient staff resources to effectively use the tax data at the federal level for income verification purposes.

We agree that actual checking of income sources would have to be done at the local level. However, to avoid unauthorized disclosure of tax data to persons or organizations outside HUD, the Department should work closely with IRS to devise the appropriate data safeguards so that tax data obtained from IRS are used only to identify leads as to possible undisclosed sources of income. HUD could then contact such income sources and request that any tenant employment and/or income information be furnished directly to the appropriate PHA or MA. Such a process, in our view, would avoid tax data disclosure problems while identifying income source leads for local followup and investigation.

State Wage Versus Federal Tax Data

HUD agrees that the use of federal tax data provides a more comprehensive source of information than state wage data. However, it disagrees that using state wage data is impractical. HUD argues that, while it may be impractical to use state wage data for nationwide matches with household data, state wage data can be effectively used locally. It points out that state

wage data are more current than federal tax data and are sufficiently accurate for matching purposes despite the lack of state verification for accuracy.

We agree and have modified our report to reflect the value to HUD of its use of state wage data for state or local level matches. We believe, however, that HUD still needs the capability to perform national level matches of household income with federal tax data to identify the full scope of income misreporting within its assisted housing programs. As we have stated in chapter 4, the federal tax data available through IRS and SSA constitute the most complete national record on individual income, such as wages, pensions, annuities, interest, and dividends. Further, maximum accuracy is assured.

Cost-Benefit Study

HUD disagrees that a cost-benefit study is needed to aid the Congress in its deliberations on whether to grant HUD access to federal tax data. HUD argues that the cost-beneficial use of tax data by other agencies has already been documented and that it does not seem logical for HUD to provide what has already been established in similar benefit programs. Moreover, until the Congress grants HUD the authority to access tax data, HUD believes it cannot do any more to develop cost-benefit information than we have already done for this report.

We disagree. Although the Computer Matching and Privacy Protection Act of 1988 does not mandate cost-benefit analyses for new federal computer matching programs, it does require matching agreements, which contain specific estimates of savings. We believe that, in this instance, a preliminary analysis could develop specific estimates of savings, which would be of considerable value to the Congress as it deliberates the highly sensitive issue of granting HUD access to confidential federal tax data for income verification. Since the mid-1980s, HUD's OIG has done extensive computer matching with state wage data and other federal agency wage data bases. We believe HUD could draw on this extensive experience and develop at least a preliminary analysis of the benefits it could achieve and the costs it might incur in matching with federal tax data, especially in light of the highly decentralized local administration of its assisted housing programs by PHAS and MAS. Once granted access to tax data, HUD could then conduct computer matches and validate the results of its preliminary cost-benefit analysis.

Other Technical Comments

HUD also offered technical comments on factual information in the report draft. We considered the comments in finalizing this report and made changes where appropriate.

IRS Comments and Our
Evaluation

The Commissioner of Internal Revenue stated that IRS continues to have serious concerns that the disclosure of tax information to additional government agencies for nontax purposes will erode taxpayers' confidence in the integrity of the federal tax system and consequently affect their willingness to voluntarily comply with the tax laws. She added that, while it is difficult to determine whether there is any adverse effect from a single program's access to tax information, IRS is concerned that the cumulative effect of disclosing additional tax information for nontax purposes will ultimately have a negative impact on tax administration. Our recommendation to give HUD access, she stated, is another in a long line that would permit access to tax information for nontax purposes.

IRS's reasons for opposing proposals to grant government agencies access to federal tax data, as our recommendation does for HUD, focus on three issues:

- The safeguarding of tax information,
- The impact on the tax system of additional access to confidential tax information, and
- The need to establish substantial cost savings to the government as a result of such tax data access.

IRS's opposition to allowing other government agencies access to tax data for nontax administration purposes is long standing. Recognizing this opposition, we devoted a chapter of this report to a detailed discussion of the issues that must be addressed in considering HUD's use of tax information for nontax purposes (see ch. 4). Having fully considered the issues, we concluded that it would be in the best interests of the government and the taxpayers to authorize HUD access to tax data to verify the income and eligibility of households in HUD-assisted housing.

Safeguard Concerns

The Commissioner points out that, under current law, IRS is charged with the responsibility of safeguarding the confidentiality of tax information. IRS must ensure that agencies receiving tax data use the data properly and have adequate safeguards in place. If more federal, state, or local agencies are given access to tax information, she states, it becomes more difficult to safeguard the information or assure that it will not be used improperly.

The Commissioner asserts that nothing in our report convinces IRS that there is a full appreciation for the extent of safeguard measures needed should HUD be granted access to federal tax data. She questions how follow-up verification and investigation of inconsistent income data would be conducted in view of HUD's decentralized use of 4,100 PHAS and more than 20,000 MAS to contact assisted housing applicants and beneficiaries. In this regard, she asserts that if access were extended to such local entities through legislation, the safeguard oversight responsibilities would be expanded monumentally. She concludes that the costs of safeguarding this information would have to be considered in any cost-benefit analysis.

We share the Commissioner's concerns about data safeguarding. As we pointed out in chapter 4, to gain access to tax data, HUD needs to demonstrate that it can incorporate applicable safeguards in the data systems it is developing. Because of HUD's decentralized administration, the privacy and data confidentiality issue poses a significant but not insurmountable barrier to HUD's qualification for access to tax data. By working closely with IRS, we believe HUD can develop sufficient controls and procedural safeguards to keep the tax data within the federal sector while accomplishing its income verification objectives. We would not advocate allowing PHAS or MAS to directly or indirectly access federal tax data. We also agree that data safeguarding costs should be included in HUD's cost-benefit analysis of computer matching with tax data.

The Commissioner commented that using tax data to verify household income could involve tax information relating to several taxpayers in the same household. Because tax information of one party generally may not be disclosed to other taxpayers, she reasons, it is possible that tax information relating to one or more household members could not be discussed freely with other household members, thus complicating how HUD might effectively use federal tax information. We do not believe that this issue presents a problem to HUD safeguarding tax information. Currently, households must report the incomes for all household members to qualify for assisted housing. We do not foresee a need to change this procedure. Moreover, HUD's use of the tax data would be to identify sources or payers of income for followup contacts, not to confront individual household members directly with tax information obtained from IRS.

The Commissioner notes our several references to HUD's use of contractors in developing its centralized files and points out that federal agencies receiving tax information are not currently authorized to disclose

such information to contractors. Although contractors are indeed involved in the development of HUD's automated systems, we do not envision that contractors would operate HUD's systems or be permitted access to tax information. As with other agencies having access to tax data, only HUD's authorized officers and employees should be provided access.

Impact on the Confidentiality of
Tax Information

The Commissioner expressed concern that as other benefit programs are authorized access to tax information, the cumulative effect is that confidential tax information may no longer be confidential. There may be some validity to this argument, but in legislating changes to the Internal Revenue Code, the Congress has determined that the public's best interests would be served by allowing such programs to use tax data to verify the incomes of program beneficiaries. The Congress would need to similarly weigh this issue in authorizing HUD access to tax information.

Substantial Cost Savings
Should Be Established

The Commissioner asserts that the Computer Matching and Privacy Protection Act of 1988 mandates a cost-benefit analysis before approval of any computer match involving a federal benefit program, the intent being to guarantee that any abridgement of citizens' rights to privacy is warranted by specific and significant savings to the government.

As we pointed out in our analysis of HUD's comments, and contrary to the Commissioner's assertion, the 1988 act does require a matching agreement with specific estimates of savings, but it does not mandate cost-benefit analyses for new federal computer matching programs. However, in chapter 4 and this chapter, we clearly recognized the need for HUD to conduct such an analysis to aid the Congress in its deliberations on legislating HUD's access to tax data for computer matching purposes.

Other IRS Comments and
Concerns

The Commissioner asserts that there are some very real practical problems alluded to, but not resolved, in our study, including

- our matching of MTCs tenant income data for the July 1989-June 1990 period with tax data for calendar year 1989 and how this timing difference affected our match results,
- the value of tax data on interest and dividend income that are unavailable for matching until 1 or 2 years after it is earned, and
- how interest and dividend information on jointly held accounts could be used to accurately reflect income of persons included in a particular household or how it could be provided without the consent of all parties.

As to the timing difference in our MTCS data match, we recognized that this was not the ideal situation, but these MTCS data were the only information available from the relatively new national data base at the time of our study. From our perspective, the match results were sufficient to demonstrate that, if given access to tax data, HUD could obtain useful leads as to assisted households' undisclosed income sources. In its matches with tax data, HUD will be able to overcome this timing problem by capturing tenant income data from MTCS that closely aligns with the calendar year covered by the tax data.

Tax data on interest and dividend income, even though it may be provided by IRS as much as 2 years—usually 12 to 18 months—after the period in which it was earned, is still valuable for income verification purposes. This has been demonstrated effectively in other federal needs-based benefit programs that have had access to this information. For example, VA's July 1991 match against IRS tax data showed that 116,000 beneficiaries did not report nearly \$340 million in unearned income (such as dividends and interest) received in 1989—about 13,600 of these beneficiaries had underreported such income by at least \$4,000. In this or any matches of interest and dividend income, the possibility of the income being jointly received by, for example, both husband and wife, presents no practical disclosure problems. The income data are reported to IRS under one social security number for tax purposes and can therefore be attributed to the person whose number appears on the reporting form.

Scope and Methodology of GAO Computer Match

For this study, we compared income information reported by members of subsidized households with IRS and SSA tax data reported by third parties. To determine the feasibility of using federal tax data to verify household income, we designed our study to parallel, to the extent possible, tax access procedures established under the Deficit Reduction Act of 1984 for other needs-based programs. DEFRA allows programs to access data from SSA on earned income and from IRS on unearned income reported by third-party payers and the self-employed. Stringent physical and procedural safeguards to protect taxpayer privacy, with which we complied, are also required.

Internal Revenue Code provisions limited our use and disclosure of tax data. Consequently, our study was restricted to (1) matching and analyzing the subsidized households' records and tax data bases and (2) investigating and reporting our results in a manner that avoided disclosure of any person's individually identifiable earned or unearned income information. We also could not refer to HUD for adjudication and resolution any potential cases of misreported household income identified through using tax data.

Selection of HUD Assisted Housing and IRS Data for Computer Matching

Because HUD did not have a centralized automated data base for all assisted housing programs, we obtained copies of 20 readily available automated data bases of subsidized households, including 11 for Public Housing and 9 for Section 8 housing projects. Together, they represented 953,752 household members residing in assisted housing. To computer-match the members' reported income contained in these data bases with SSA and IRS automated tax data bases, we needed valid social security numbers for each member. After eliminating members with invalid or no numbers, we selected three data bases: Multifamily Tenant Characteristics System (Public Housing) and NHP Property Management, Inc., and Automated System for Tenant Eligibility Certification (both Section 8 housing). We believed these would best accomplish our objectives, while providing geographic coverage and representation of both public and Section 8 assisted housing. The three data bases included data on 330,518 household members with valid social security numbers residing in 231,644 subsidized households.

In each of the three data bases, we grouped household members with valid social security numbers by their respective subsidized households. We eliminated from these data bases households that (1) did not have valid numbers for all members of the household who were 18 years of age or

older and (2) had eligibility certification or recertification dates before January 1989. As a result of this screening, our computer match was limited to 174,523 households that reported annual income or changes between January 1989 and June 1990. (See table I-1.)

Table I.1: Subsidized Household Data Bases Used in GAO's Computer Match With Federal Tax Data

Data base	Assisted housing type	Number of households	Range of certification/recertification dates
MTCS	Public	162,371	Jul. 1989-Jun. 1990
NHP	Section 8	7,374	Jan.-Dec. 1989
ASTEC	Section 8	4,778	Jan.-Dec. 1989
Total		174,523	

Because of IRS's and SSA's tax data processing cycles, 1989 tax data were the latest available for our study. Tax data used for income verification procedures under DEFRA usually are not available to authorized agencies until about 18 months after the end of the calendar year to which they pertain. We requested and received 1989 tax data from IRS and SSA for all subsidized household members with valid social security numbers in our three data bases. IRS provided interest and dividend income data, and SSA provided wage and self-employment income data. Also, to identify patterns of household-reported income in tax records for years before 1989, we requested and received wage, self-employment, interest, and dividend income data from consolidated IRS files for calendar years 1986, 1987, and 1988.

Computer Match and Analysis

To computer-match household members' reported income, we merged income data from the IRS and SSA tax data bases with income records in our three data bases of subsidized households. We focused our computer matching on household members' wage, interest, and dividend income. Other sources of income, such as private pensions and Social Security and SSI benefits, are not separately identified by PHAS and MAS and, therefore, could not be computer-matched.

Working with the initial results of our computer match, which disclosed a wide range of income differences between the households and tax records, we performed three different levels of analysis to refine and enhance our study results.

1. In the interest of conservative reporting, we imposed dollar thresholds for reportable income differences. We did so by (a) considering only

differences exceeding \$1,000 for annual wages and \$200 for annual interest and dividend income; (b) excluding wage, interest, and dividend income in excess of the first \$30,000 for each household having an income difference that large; and (c) excluding earned income of household members under 18 years of age. The latter adjustment was made because HUD regulations exclude such members' earned income in determining the household's rent contribution.

2. We estimated the erroneous rent subsidies that may have been caused by the income misreporting. We did this by multiplying 30 percent times the total understated wage, interest, and dividend income, after applying the above dollar thresholds. In using the 30 percent, which is the proportion of subsidized households' income generally paid in rent, our intent was to provide a reasonable representation of the magnitude of potential excess HUD subsidies for the households in the three data bases matched. Each dollar of underpaid rent represents a dollar of excess subsidy. In reality, some assisted housing programs impose limits on HUD's rent subsidies, such as the full fair market rent (or a percentage thereof) for a dwelling unit or a specified payment standard for the area in which the unit is located. As these data were not available in our data bases, we could not consider them in estimating excess subsidies. Our upper threshold of \$30,000 for total income differences was intended to compensate for this situation.

3. We validated the reliability of the data bases we used. Because the Internal Revenue Code prohibits us from revealing tax information to HUD, we could not refer the potential income misreporting cases to HUD for follow-up investigation and adjudication. However, as an alternative, we drew a random sample of 367 of the 174,523 households in our computer match to check the accuracy of the income data recorded in our data base. Our sample included 150 MTCS, 67 NHP, and 150 ASTEC cases and covered a variety of income reporting circumstances. These included cases of potentially misreported income and no apparent income differences. We asked the respective PHAS and MAS for these 367 households to provide copies of selected certification or recertification forms—HUD 50058 and 50059—on file for the households. In addition, we obtained information on any changes that households might have reported between annual recertifications to (a) assess the frequency and type of interim changes, such as reported increases or decreases in income, and (b) determine whether substantial income changes were reported after the recertification dates. Responses were received for 346, or 94 percent, of our sample cases.

Appendix I
Scope and Methodology of GAO Computer
Match

Our sample results indicated an acceptable error rate of 3.8 percent. Therefore, we consider the MTCS, ASTEC, and NHP data bases reliable for our purposes. Of the 312 usable reports received from PHAS and MAS,¹ only 12 reports (3.8 percent) showed wage, dividend, or interest income data different from those in the computerized data bases. The remaining 300 reports had wage, dividend, and interest income data identical to those recorded in the respective data base. This error rate ranges between 2.2 percent and 6.1 percent at the 95-percent level of statistical confidence.

¹Some reports were not usable, because they were illegible or referred to the wrong time period.

Details of GAO's Computer Match Results by Household Data Base and Type of Income Difference

Data base (period) and income type	Incomes in tax data greater than in HUD data			Incomes in tax data less than in HUD data			Total differences		
	House-	Income differences		House- holds	Income differences		House- holds	Income differences	
		Amount	Percent		Amount	Percent		Amount	Percent
MTCS (7/89-6/90)									
Wages	23,369	\$111,534,475	87.3%	15,965	\$85,365,644	96.2%	39,334	\$196,900,119	91.0%
Interest/dividends	10,750	16,163,007	12.7	2,461	3,399,853	3.8	13,211	19,562,860	9.0
Total		\$127,697,482	100.0		\$88,765,497	100.0		\$216,462,979	100.0
Combined income ^a	32,779	\$127,036,750		18,196	\$88,188,969		50,975	\$215,225,719	
ASTEC (1/89-12/89)									
Wages	242	\$1,360,805	53.5	82	\$345,047	44.5	324	\$1,705,852	51.4
Interest/dividends	870	1,182,294	46.5	398	430,356	55.5	1,268	1,612,650	48.6
Total		\$2,543,099	100.0		\$775,403	100.0		\$3,318,502	100.0
Combined income ^a	1,077	\$2,524,978		471	\$757,280		1,548	\$3,282,258	
NHP (1/89-12/89)									
Wages	1,183	\$6,459,400	78.0	566	\$3,795,457	93.6	1,749	\$10,254,857	83.2
Interest/dividends	951	1,816,158	22.0	197	258,005	6.4	1,148	2,074,163	16.8
Total		\$8,275,558	100.0		\$4,053,462	100.0		\$12,329,020	100.0
Combined income ^a	1,979	\$8,188,939		751	\$3,998,406		2,730	\$12,187,345	
Grand totals									
Wages	24,794	\$119,354,680	86.2	16,613	\$89,506,148	95.6	41,407	\$208,860,828	90.0
Interest/dividends	12,571	19,161,459	13.8	3,056	4,088,214	4.4	15,627	23,249,673	10.0
Total		\$138,516,139	100.0		\$93,594,362	100.0		\$232,110,501	100.0
Combined income ^a	35,835	\$137,750,667		19,418	\$92,944,655		55,253	\$230,695,322	
Average difference per household									
Wages		\$4,814			\$5,388			\$5,044	
Interest/dividends		1,524			1,338			1,488	
Combined income ^a		\$3,844			\$4,786			\$4,175	

Note: Results were calculated after applying our dollar thresholds—\$30,000 maximum difference and \$1,000 and \$200 minimums for wages and interest/dividend differences, respectively.

^aCombined household income results were calculated by adding the household's wages and interest/dividends and comparing that total to the sum of IRS/SSA wages and interest/dividends. In the process, some netting of income occurred; thus these results are somewhat lower than the "total" line above.

Comments From the Department of Housing and Urban Development



U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
THE SECRETARY
WASHINGTON, D.C. 20410-0001

April 8, 1992

Mr. Joseph F. Delfico
Director, Income Security Issues
U.S. General Accounting Office
441 G Street, NW
Washington, DC 20548

Dear Mr. Delfico:

In response to your February 27, 1992 letter, enclosed are comments on the draft report, ASSISTING THE NEEDY: Tax Data Reveal Substantial Income Misreporting in HUD Subsidized Housing (GAO/HRD-92-60). Generally, the comments agree with the GAO recommendations that HUD design its automated systems to include appropriate safeguards and to permit effective use of Federal tax data. This will facilitate identifying subsidized households' misreporting income. However, I disagree with the GAO recommendation that HUD conduct a cost-benefit analysis of using the data. This is unnecessary and impractical given GAO's analysis and current restraints on use of the tax data.

Tenant fraud for HUD's assisted housing programs has been a problem from the inception of the programs. Matching Federal tax data to a centralized tenant database can significantly aid in promoting integrity in HUD's assisted housing programs. HUD has taken actions in the past few years to create a central tenant database. The first page of the enclosure describes these and other HUD initiatives to promote tenant integrity.

I appreciate Congressional passage of Section 904 of the McKinney Amendments of 1988 permitting HUD access to state wage data needed for computer matching. This legislation will expire October 1, 1994. I would strongly encourage Congress to provide HUD with permanent authority for state wage data access. In addition, I favor GAO's recommendation that Congress grant HUD access to Federal tax data.

Finally, I would like to express my interest in and support for the idea of consolidating the income verification function among the various Federal assistance programs. There is a great deal of overlap among the families participating in HUD's programs and those receiving benefits under Aid to Families of

Appendix III
Comments From the Department of Housing
and Urban Development

Dependent Children, Supplemental Security Income and other programs serving poor families. If the determination and verification of income under these programs were consolidated, there would be substantial savings on both the Federal and state level and the affected families would find the process more convenient and less intrusive.

Very sincerely yours,



Jack Kemp

Enclosure

Appendix III
Comments From the Department of Housing
and Urban Development

Comments on the GAO Draft Report
ASSISTING THE NEEDY: Tax Data Reveal
Substantial Income Misreporting in HUD Subsidized Housing
(GAO/HRD-92-60)

HUD's role in the verification process

The determination of participant income and rent in HUD's assisted housing programs is the responsibility of the public housing agencies (PHAs) or private owner. HUD is responsible for seeing that PHAs and owners establish controls to assure the integrity of the process and to monitor the quality of PHA and owner determination. In addition, HUD has a role in making available to PHAs and owners information and resources that they cannot obtain directly.

Income matching, as currently being performed by HUD and as proposed by GAO is an activity that involves both monitoring PHAs and owners and for making information available that supplements the information they obtain through interviews and the verification process. Still, the responsibility for determining income and setting rents lies with the PHA or owner and there is no way that HUD could assume that function directly.

As discussed below, even if HUD does the actual matches on a batch basis, the PHA or owner would have to perform any required checking with the income source, provide an opportunity for the tenant to respond and take whatever corrective action is necessary.

HUD Initiatives to Promote Program Integrity

Computer matching to Federal tax data as recommended by GAO is one additional tool needed to help promote integrity in assisted housing programs. Other actions taken by HUD will complement GAO's recommendation.

Major HUD initiatives to promote integrity in assisted housing programs include:

- o developing a centralized tenant database for all assisted housing tenants; a central database already exists for public housing tenants. HUD will begin to collect information on participants in the Section 8 Rental Certificate, Rental Voucher and Moderate Rehabilitation programs this year. Work is underway to develop a database for tenants serviced by management agents and owners of subsidized multifamily projects,

**Appendix III
Comments From the Department of Housing
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- o implementing a Tenant Integrity Program to help public housing agencies and management agents and owners of subsidized housing projects prevent and detect fraud,
- o doing computer matching to state wage data and to Federal wage sources, and verifying matching results; this process has detected tenant fraud and facilitated administrative and legal actions,
- o helping public housing agencies in Delaware gain on-line access to state wage and welfare data when individuals apply for housing assistance.

Potential vs. Actual Income Differences

It is important that readers of the GAO report understand that actual income differences will be less than the GAO-computed "potential income differences." GAO reported potential income differences for 21 percent of the households tested. Although GAO used some conservative techniques in estimating these differences and excess rental assistance, the report indicates that the matching to tax data was by social security number only.

Had GAO been permitted to do the income verification process, the actual income differences would have been less than the potential differences. Neither HUD, nor GAO, can estimate with any precision the actual income differences. However, the actual households with under-reported income might be only about half of the 21 percent of cases with "potential income differences." This still represents a significant problem.

Page 28 of the draft report shows that the annual income amounts identified in Federal tax records ranged from \$1,001 to \$175,087. The verification process for matching to the \$175,087 "hit" would identify reason(s) this "hit" may be invalid. Perhaps an employer incorrectly reported income to the Social Security Administration, or two or more individuals are using the same social security number.

HUD Office of Inspector General (OIG) matching of tenant social security numbers to state wage data has produced similar potential income differences. However, the verification process has substantially reduced the number of actual differences in unreported income. Most cases that "fall out" are because the names do not match even though the social security numbers do. The HUD OIG used different criteria in selecting cases for detailed analysis. Therefore, it is not possible to provide a definitive percentage of the "potential income differences" that will result in actual differences in under-reported income.

Deleted from final report.

Resources Required for Verification Processes

Readers of the GAO report must understand that the verification of income data requires substantial resources; albeit, the benefits will exceed the costs. Income verification processes will be needed for state wage agency matching and Federal tax data matching. Although HUD has not conducted detailed studies of the resources required, experience suggests that the analysis of tenant-provided information, confirmation of income with employers and computation of excess benefits owed can average 4 to 8 hours per case.

Benefits of computer matching can only be fully realized with an efficient income verification process. This requires resources to: analyze tenant-provided information, confirm income with employers, compute excess benefits owed, recertify tenants, provide tenants with their due process in benefit determinations, seek administrative remedies such as repayment agreements, investigate and prosecute flagrant abuses.

The GAO report mentions the need for income verification, but does not describe the verification processes. GAO probably did not discuss this process in the report because restrictions on use of tax data precluding GAO verification of the potential income differences.

The Congress and GAO must recognize the resource requirements resulting from the verification process. For HUD matches conducted to date, the HUD OIG staff have conducted the matching and income verification processes. Public housing agencies and management agents have recertified tenants and taken administrative actions.

Currently the Department has allocated only 4 staff years to conduct matching projects. Given limited HUD resources to do income verifications, the Department may place verification responsibilities on public housing agency staff. This may require modifications to annual contribution contracts with public housing agencies. HUD program staff will be developing plans on this matter in Fiscal Year 1993. HUD plans to transfer the computer matching function from the HUD OIG to Public and Indian Housing on October 1, 1992.

In weighing the costs and benefits of various schemes of income matching, HUD must consider the use of staff time for this activity as it impacts other functions. In a period of scarce resources, it will be necessary to assess the ability to conduct the full scope of functions required by statute, regulation or

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Departmental requirements. Some of these may result in more costly losses (for example defaults and foreclosures on insured multifamily projects) if resources are insufficient to conduct all activities.

Disclosure Authority for Federal Tax Data

HUD will be precluded from effectively using Federal tax data if disclosure of this information is limited to only HUD employees. Congress must either increase HUD's budget to provide sufficient staffing for conducting the computer matching and tenant income verifications, or permit the disclosure of the information to HUD contract agents or employees of state housing finance agencies.

The Deficit Reduction Act for the Food Stamp and Aid for Families with Dependent Children programs permits disclosure of tax data to state employees. This should also be allowed for HUD assisted housing programs. The last constraint on tax data use cited on page 53 will be too restrictive. Congress and the Internal Revenue Service should consider permitting disclosure to public housing agencies whose staff are employees of a government entity. This would give HUD comparable disclosure authority to the other Federal benefit programs under the Deficit Reduction Act.

State wage vs. Federal tax data

We agree with GAO that the use of Federal tax data provides a more comprehensive source of information than state wage data. However, we strongly disagree with the statement on page 44 of the draft report that using state wage data is impractical. It would be impractical if you did matching to household data nationwide. HUD currently does not have, and will not have soon, the capability for wage matching and verification on a national basis. Matching of state wage data presently generates more tenant income verification work than can be done by HUD staff assigned this responsibility. It is important that public housing agencies be permitted to institute matching at the local level as part of their application and reexamination processes.

The first sentence on page 43, last paragraph, states that GAO considered state unemployment compensation files as unacceptable. The GAO statement appears to conflict with GAO's executive summary, page 4, last paragraph, that suggests continued matching to state wage data.

Page 45 of the draft report lists reasons for the inadvisability of using state wage data, citing the insufficient accuracy of state wage data for HUD's purpose. GAO may wish to rethink the relevancy of the statement. GAO says on page 45 that

Now on p. 38.

Now on p. 34.

Deleted from final report.

Now on p. 4.

Now on p. 34.

Now on p. 34.

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states do not verify the accuracy of their wage data. Despite this, HUD has found the wage data obtained from state agencies to be highly reliable. Nonetheless, HUD and public housing agencies are required to independently reverify all information before any adverse action can be taken. Therefore, the accuracy of the dollar amount shown on the state wage data is almost irrelevant. The identification of undisclosed employers is the real value of matching.

GAO's attempt to repudiate the effectiveness of using state wage data may lead the Congress to refuse to re-authorize the legislation that gives HUD and public housing agencies access to state wage data. If that occurs and the legislation for Federal tax data is not passed, HUD will have no access to wage data. HUD should be given access to use both Federal tax and state wage data. Again, this is consistent with authority for other Federal benefit programs.

Other comments concerning Federal tax and state wage data follow:

- o The report should recognize that state wage data provides more current wage data than Federal tax data. Generally, state wage data can be obtained that is only 4 to 6 months old. In contrast, the Federal tax data is at least 18 months old when received. However, timeliness of the data is not a serious concern because the income verification process requests income data for several years.
- o The statement on page 33 that HUD's lack of a centralized system of household data has precluded effective use of computer matching techniques, is misleading. It is true that the lack of a centralized system has precluded large-scale matching. However, HUD has used computer matching techniques effectively using household data received from public housing agencies and independent income sources. The HUD OIG currently has an ongoing computer matching project that will use household data from HUD's Multifamily Tenant Characteristic System in matching with District of Columbia, Maryland and Virginia wage data.
- o We agree with the last item on page 44 stating that state wage data excludes earned income for military and Federal civilian workers. But HUD has matched Department of Defense and Office of Personnel Management data to tenant data to obtain Federal employment and retiree data.

Now on p. 29.

Now on p. 34.

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Now on p. 39.

Cost-Benefit Study

We suggest that GAO delete item 4 on page 55. This item states that HUD would need to conduct a cost-benefit study to aid Congress in its deliberations on whether to grant access to Federal tax data. GAO cites the cost benefit that has been documented in other agencies that have been mandated to do the matching. It does not seem logical for HUD to provide what has already been established in similar benefit programs. Until the Congress grants HUD the authority to access tax data, HUD could not do any more to develop cost-benefit information than the GAO has already done. The re-disclosure limitation that GAO cites on page 24 of the draft report would preclude additional analyses. Further, the Office of Management and Budget's guidelines for computer matching require that cost-benefit analyses be done for each matching project.

Now on p. 21.

Note:

HUD also provided technical comments, not reproduced here, on factual information in a draft of this report. We considered these comments in finalizing this report and made changes where appropriate.

Comments From the Internal Revenue Service



COMMISSIONER

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

APR 24 1992

Mr. Joseph F. Delfico
Director, Income Security Issues
Human Resources Division
United States General Accounting Office
Washington, DC 20548

Dear Mr. Delfico:

Thank you for the opportunity to review your recent draft report entitled, "Assisting the Needy: Tax Data Reveal Substantial Income Misreporting in HUD Subsidized Housing." We offer the following comments regarding the recommended legislation to amend the Internal Revenue Code to authorize the Department of Housing and Urban Development (HUD) to access Federal tax information for use in determining eligibility for and the amount of benefits under assisted housing programs.

We continue to have serious concerns that the disclosure of tax information to additional government agencies for non-tax purposes will erode taxpayers' confidence in the integrity of our tax system and consequently affect their willingness to voluntarily comply with the tax laws. While it is difficult to determine whether there is any adverse effect from a single program's access to tax information, we are concerned that the cumulative effect of disclosing additional tax information for non-tax purposes will ultimately and negatively impact on tax administration. The present proposal is another in a long line that would permit access to tax information for non-tax purposes. Our reasons for opposing proposals such as this are:

Safeguard Concerns: Under current law, IRS is charged with the responsibility of safeguarding the confidentiality of tax information. This responsibility extends to ensuring the adequacy of safeguards and the proper use of tax data by agencies that receive tax data from the IRS. As more Federal, state or local agencies are given access to tax information, it becomes increasingly difficult to safeguard the information or assure that it will not be used improperly.

Nothing in the draft report convinces us that there is a full appreciation for the extent of safeguard measures that would be needed should HUD be granted access to Federal tax data as an expansion of IRC 6103(1)(7). If HUD receives tax information that shows income inconsistent with that reported by assisted housing program applicants or beneficiaries, how would the follow-up verification and

investigation be conducted? HUD contacts with applicants and beneficiaries seem to take place through its decentralized use of 4100 local public housing agencies (PHAs) and 20,000+ private management agencies (MAs) who, presumably, would not be entitled to access Federal tax information. If access were to be extended to these additional 24,100+ entities by legislation, the safeguard oversight responsibilities would be expanded monumentally. Clearly the costs of safeguarding this information would have to be considered in any cost-benefit analysis.

There are some very real practical problems that are alluded to, but not resolved in the GAO study. In one instance, because of deficiencies in the data, GAO compared income reported by applicants with tax data reported for a different time period. It is not clear what result this had on the overall estimates, but in an actual program such a match would be unusable. It is also not clear that information on interest and dividends would ever be available in time to be of any real value. Unlike state wage data that is generally available quarterly, federal information on unclaimed income is not available until one to two years after it is earned. Also, unlike wage data, accounts which pay interest and dividends are often jointly held. It is not clear how this information could be used to accurately reflect income of persons included in a particular household or how it could be provided without the consent of all parties.

For example, household income is a determining factor in whether housing assistance is warranted. Using tax data to verify household income could involve tax information relating to several taxpayers (all household members age 18 or over). Because the tax information of one party generally may not be disclosed to other taxpayers, it is possible that tax information relating to one or more household members could not be discussed freely with other household members, thus complicating how HUD might effectively be able to use Federal tax information.

Finally, the draft report makes several references to HUD's use of contractors in developing its centralized files. The Federal agencies receiving tax information under IRC 6103(1)(7) are not currently authorized to disclose tax information to contractors.

Appendix IV
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Service

- Impact on the Confidentiality of Tax Information: Since 1976, IRC section 6103 has been amended to authorize the disclosure of tax information for several specific benefit programs. As others are added, the cumulative effect is that confidential tax information may no longer be confidential. We are cognizant of the arguments for administrative simplicity and savings if the government utilizes one financial information clearing-house for tax and other data required to be submitted to IRS by individuals, corporations, and financial institutions, but we are concerned about the effect of this policy on the tax system.
- Substantial Cost Savings Should Be Established: The Computer Matching and Privacy Protection Act of 1988 mandates a cost-benefit analysis prior to approval of any computer match involving a Federal benefit program. The intent of this law is not to prohibit all inter-agency computer matching programs, but to guarantee that any abridgement of our citizens' rights to privacy is warranted by specific and significant savings to the government.

In enacting IRC 6103 in 1976, Congress specifically weighed and balanced the needs of other government agencies for information against the taxpayer's privacy interests and the impact that such disclosures would have on voluntary compliance. The statutory result was a sharp curtailment of disclosures to other agencies. Additionally, congressional intent behind section 6103 is that taxpayers have a right to expect their tax information will remain confidential.

Just as we are concerned that the cumulative impact of amendments authorizing additional non-tax agencies access to tax data may adversely affect voluntary compliance, we are also concerned about the increased risk of unauthorized disclosures, particularly in a case such as this, where approximately 4.6 million taxpayers may be affected.

We hope these comments will receive careful consideration in finalizing your draft report and its recommendations.

Best regards.

Sincerely,


Shirley D. Peterson

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Related GAO Products

Veterans' Benefits: Millions in Savings Possible From VA's Matching Program With IRS and SSA (GAO/HRD-92-37, Dec. 23, 1991).

Veterans' Pensions: Verifying Income With Tax Data Can Identify Significant Payment Problems (GAO/HRD-88-24, Mar. 16, 1988).

Veterans Benefits: Improving the Integrity of VA's Unemployability Compensation Program (GAO/HRD-87-62, Sept. 21, 1987).

Welfare Eligibility: Deficit Reduction Act Income Verification Issues (GAO/HRD-87-79FS, May 26, 1987).

Social Security: Pension Data Useful for Detecting Supplemental Security Payment Errors (GAO/HRD-86-32, Mar. 12, 1986).

A Central Wage File for Use by Federal Agencies: Benefits and Concerns (GAO/HRD-85-31, May 21, 1985).

Eligibility Verification and Privacy in Federal Benefit Programs: A Delicate Balance (GAO/HRD-85-22, Mar. 1, 1985).

GAO Observations on the Use of Tax Return Information for Verification in Entitlement Programs (GAO/HRD-84-72, June 5, 1984).

Legislative and Administrative Changes to Improve Verification of Welfare Recipients' Income and Assets Could Save Hundreds of Millions (GAO/HRD-82-9, Jan. 14, 1982).