



In this issue:

**Summary**

**Errors Identified**

**Recommendations Made**

**Deloitte's View**

**People to Contact**

## GES NewsFlash

# United States – Treasury Report Indicates Need for Improvements to Reduce Erroneous Foreign Earned Income Exclusion Claims

September 8, 2010

### Summary

The Treasury Inspector General for Tax Administration (TIGTA) recently completed and issued a report highlighting its examination of US tax returns filed claiming the foreign earned income exclusion (FEIE). TIGTA reviewed over 230,000 tax returns for 2008 which claimed the FEIE, and found that over 10 percent of the returns filed either incorrectly calculated the exclusion or did not qualify for the exclusion. The report estimates potential lost revenue resulting from these errors at approximately \$450 million over a five year period. As a result of this report, TIGTA provides several recommendations to the IRS to improve the process for examining tax returns claiming the FEIE to ensure accuracy and to increase compliance with the regulations. The implementation of these recommendations will likely result in additional review of returns claiming the foreign earned income exclusion in the future.

### Errors Identified

TIGTA's report identifies two primary areas where taxpayer's returns were incorrect.

The first typical error relates to taxpayers who incorrectly computed the FEIE. Approximately 12,000 returns reflected an exclusion amount greater than the total foreign earned income reported on the return. In addition, approximately 6,000 returns did not accurately transfer the amounts of the FEIE from the Form 2555 to the appropriate line on the Form 1040. Form 2555 is the form used by taxpayers to calculate the FEIE allowed for the current tax year.

The report provides hypothetical examples of these errors. One example included a taxpayer who had \$87,000 of foreign earned income but claimed an exclusion of \$105,000. Another showed a taxpayer who calculated an exclusion of \$85,000 on

Form 2555, but claimed an exclusion on the Form 1040 of \$139,000.

The second typical error relates to taxpayers who did not qualify for the exclusion but claimed it anyway. Included were taxpayers who claimed bona fide residency but had never lived abroad for an entire calendar year and taxpayers who claimed physical presence but their time period reported on the return did not support such a claim. The review included requested data from the US Department of Homeland Security that details time periods of the individuals leaving and entering the U.S.

### Recommendations Made

As a result of this report, TIGTA made several recommendations to the IRS to improve overall compliance. Following are recommendations accepted by the IRS:

- The IRS will review the returns that were identified with errors from this report. Based on this review, the IRS may select some of the returns for examination, or soft letters. Some errors may result in changes in the IRS process.
- The IRS will request programming which will forward both e-filed and paper tax returns to the Error Resolution System for correction if the individual incorrectly computes the FEIE, or if the individual does not appear to qualify for the exclusion. The IRS has procedures in place now to ensure that paper returns are reviewed and plans to implement this recommendation for additional electronic review programming with a target deployment date of January 2012.
- The IRS will establish the International Campus Compliance Unit to address those taxpayers identified as erroneously claiming the FEIE. The IRS has proposed establishing this unit in its Austin, TX facility, with an implementation date scheduled for September 30, 2010.

#### **Deloitte's View**

Since 2009, the IRS has significantly increased its focus on international tax compliance. The IRS determined that much more attention needed to be placed on the increasing levels of compliance risk among global entities, such as multinational corporations, high-wealth individuals, and US citizens living outside the US. With the findings identified in the TIGTA report, we anticipate that the IRS will focus even more attention on international assignees to ensure that they are properly reporting exclusions and credits which lower their US tax liabilities. Care should be taken to ensure that proper attention is given to these claims to ensure accuracy before filing tax returns.

### People to Contact

If you have any questions concerning the issues in this GES NewsFlash, please contact one of the tax professionals as follows:

**Kent Klaus**

Tel: + 1 312-486-2571

**Michael Loskove**

Tel: + 1 312-486-2026

This NewsFlash information is also included in our bi-weekly GES newsletter, *Global InSight*, which you will receive directly if you are on the central distribution list.

If you are not on the central distribution list and received this communication by some other means, you can follow these few simple steps to be added to the central distribution list.

- Go to the [Deloitte Subscriptions Page](#) on Deloitte.com
- Make sure that under Step 1 you select “Tax” and “Global Employer Services”
- Under Step 2, select “Global Insight”
- Under Step 3, fill out your contact information and click “Save my profile”

Be sure to visit us at our Web site: [www.deloitte.com/tax](http://www.deloitte.com/tax)

If you require information about doing business in a specific country, including individual tax considerations, please log on to [www.deloittetaxguides.com](http://www.deloittetaxguides.com) and select the countries of interest. In addition to detailed guides, there are at-a-glance summaries contained in the Snapshot series section.

**[Back to Top](#)**

---

**[Home](#) | [Security](#) | [Legal](#) | [Privacy](#)**

1633 Broadway  
New York, NY 10019 – 6754  
United States

© 2010 Deloitte Touche Tohmatsu.

Deloitte refers to one or more Deloitte Touche Tohmatsu, a Swiss Verein, and its network of member firms, each of which is a legally separate and independent entity. Please see [www.deloitte.com/about](http://www.deloitte.com/about) for a detailed description of the legal structure of Deloitte Touche Tohmatsu and its member firms.

 **[Deloitte RSS feeds](#)**

---