

**INTERNAL REVENUE SERVICE OPERATIONS  
AND THE 2011 TAX RETURN FILING SEASON**

---

**HEARING**  
BEFORE THE  
SUBCOMMITTEE ON OVERSIGHT  
OF THE  
COMMITTEE ON WAYS AND MEANS  
U.S. HOUSE OF REPRESENTATIVES  
ONE HUNDRED TWELFTH CONGRESS  
FIRST SESSION

MARCH 31, 2011

**Serial No. 112-OS2**

Printed for the use of the Committee on Ways and Means



U.S. GOVERNMENT PRINTING OFFICE

70-878

WASHINGTON : 2011

---

For sale by the Superintendent of Documents, U.S. Government Printing Office  
Internet: [bookstore.gpo.gov](http://bookstore.gpo.gov) Phone: toll free (866) 512-1800; DC area (202) 512-1800  
Fax: (202) 512-2104 Mail: Stop IDCC, Washington, DC 20402-0001

**COMMITTEE ON WAYS AND MEANS  
OVERSIGHT SUBCOMMITTEE**

CHARLES W. BOUSTANY, JR., Louisiana, *Chairman*

DIANE BLACK, Tennessee

JIM GERLACH, Pennsylvania

VERN BUCHANAN, Florida

AARON SCHOCK, Illinois

LYNN JENKINS, Kansas

KENNY MARCHANT, New York

JOHN LEWIS, Georgia

XAVIER BECERRA, California

RON KIND, Wisconsin

JIM MCDERMOTT, Washington

JON TRAUB, *Staff Director*

JANICE MAYS, *Minority Staff Director*

## CONTENTS

---

	Page
Advisory of March 31, 2011, announcing the hearing .....	2
WITNESSES	
The Honorable Douglas Shulman, Commissioner, Internal Revenue Service ....	50
SUBMISSIONS FOR THE RECORD	
Chairman Boustany .....	91
Rep. Diane Black .....	95
Rep. Jim Gerlach .....	98
Rep. John Lewis .....	99
Colleen M. Kelley, National President National Treasury Employees Union ....	101





# **INTERNAL REVENUE SERVICE OPERATIONS AND THE 2011 TAX RETURN FILING SEASON**

---

**THURSDAY, MARCH 31, 2011**

U.S. HOUSE OF REPRESENTATIVES,  
COMMITTEE ON WAYS AND MEANS,  
SUBCOMMITTEE ON OVERSIGHT,  
*Washington, DC.*

The subcommittee met, pursuant to notice, at 10:02 a.m., in Room 1100, Longworth House Office Building, the Honorable Charles Boustany [chairman of the subcommittee] presiding.  
[The advisory of the hearing follows:]

# HEARING ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

## Boustany Announces Hearing on Internal Revenue Service Operations and the 2011 Tax Return Filing Season

March 24, 2011

Congressman Charles W. Boustany, Jr., MD, (R-LA), Chairman of the Subcommittee on Oversight of the Committee on Ways and Means, today announced that the Subcommittee will hold a hearing on the Internal Revenue Service ("IRS") and the 2011 Tax Return Filing Season. **The hearing will take place on Thursday, March 31, 2011, in Room 1100 of the Longworth House Office Building, beginning at 10:00 A.M.**

The Commissioner of the Internal Revenue Service, the Honorable Douglas Shulman, will be the only witness at the hearing. Any individual or organization may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

### BACKGROUND:

In fiscal year 2010, the IRS collected \$2.3 trillion in taxes, processed 141 million individual tax returns, and issued \$366 billion in refunds. As the 2011 tax return filing season is underway, the Subcommittee will review IRS performance with a focus on taxpayer service, taxpayer rights, and refund administration.

In conjunction with the review of the current tax return filing season, the Subcommittee will review IRS operations in general. Specifically, the Subcommittee will consider: (1) the protection of taxpayer rights; (2) fairness in examinations and tax administration; and (3) efforts to prevent fraud, waste, and abuse. As part of its consideration of IRS operations, the Subcommittee will also review the Administration's fiscal year 2012 budget proposal for the IRS of \$13.3 billion, an increase of \$1.1 billion over the fiscal year 2010 enacted level.

In announcing the hearing, Chairman Boustany said, **"With so many struggling through a tough economy, it's important we remember that the IRS affects every household and business across the country. The Subcommittee will examine how the IRS is performing this tax season, with an eye toward taxpayer rights and the fair collection of federal taxes. We will also review the Administration's new IRS budget request, an increase of more than 9% from 2010 levels, and the Commissioner's justification for this increase."**

### FOCUS OF THE HEARING:

The hearing will focus on the 2011 tax return filing season, the IRS' budget, and IRS operations generally.

### DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

**Please Note:** Any person(s) and/or organization(s) wishing to submit written comments for the hearing record must follow the appropriate link on the hearing page of the Committee website and complete the informational forms. From the Committee homepage, <http://waysandmeans.house.gov>, select "Hearings." Select the hearing for which you would like to submit, and click on the link entitled, "Click here to provide a submission for the record." Once you have followed the online instructions, submit all requested information. ATTACH your submission as a Word document, in compliance with the formatting requirements listed below, **by the close**

**of business on Wednesday, April 14, 2011.** Finally, please note that due to the change in House mail policy, the U.S. Capitol Police will refuse sealed-package deliveries to all House Office Buildings. For questions, or if you encounter technical problems, please call (202) 225-3625 or (202) 225-5522.

#### **FORMATTING REQUIREMENTS:**

The Committee relies on electronic submissions for printing the official hearing record. As always, submissions will be included in the record according to the discretion of the Committee. The Committee will not alter the content of your submission, but we reserve the right to format it according to our guidelines. Any submission provided to the Committee by a witness, any supplementary materials submitted for the printed record, and any written comments in response to a request for written comments must conform to the guidelines listed below. Any submission or supplementary item not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

1. All submissions and supplementary materials must be provided in Word format and **MUST NOT** exceed a total of 10 pages, including attachments. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.

2. Copies of whole documents submitted as exhibit material will not be accepted for printing. Instead, exhibit material should be referenced and quoted or paraphrased. All exhibit material not meeting these specifications will be maintained in the Committee files for review and use by the Committee.

3. All submissions must include a list of all clients, persons and/or organizations on whose behalf the witness appears. A supplemental sheet must accompany each submission listing the name, company, address, telephone, and fax numbers of each witness.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202-225-1721 or 202-226-3411 TTD/TTY in advance of the event (four business days notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Note: All Committee advisories and news releases are available on the World Wide Web at <http://www.waysandmeans.house.gov/>.

---

Chairman BOUSTANY. The subcommittee will come to order. Good morning. I would like to welcome everyone to today's hearing on the Internal Revenue Service and the 2011 tax return filing season.

Today's conversation about the IRS should begin with a topic too often ignored, and that is the taxpayer. The National Taxpayer Advocate's recent report to Congress provided some alarming facts on what the federal Tax Code has become, and how it affects the average taxpayer.

Every year taxpayers face a Tax Code of growing complexity. For instance, there have been nearly 5,000 changes to the Tax Code in the past 10 years. Between the period of 1975 and 2005, the code tripled in size. As a result of the growing length and complexity of the Tax Code, individual taxpayers and businesses spend an estimated 6.1 billion hours and \$163 billion every single year complying with the tax filing requirements. The cost of compliance for your average individual taxpayer was over \$250 in 2007.

So, as we meet today, we are in the middle of the 2011 tax return filing season. And millions of individuals and businesses are working to meet their annual tax return filing obligations. As of March 18th, IRS had processed over 73 million individual tax re-

turns, and issued nearly 65 million refunds, totaling \$193 billion. With 2.5 weeks to go until the April 18th filing deadline, the subcommittee looks forward to hearing more about the ongoing tax return season and any problems the Agency and tax return filers might be encountering.

The subcommittee would also like to learn more about the efforts the IRS has undertaken to improve the efficient processing of returns and refunds, including its eFiling modernization program.

Charged with administering this growing Tax Code, the IRS must simultaneously respect the rights of taxpayers, provide assistance to the millions of taxpayers who have questions about their taxes, and go after those who cheat the system. And the Agency has to do this against the backdrop of ever-increasing responsibilities to administer social policy programs. The IRS's dual mission to both revenue collector and social policy program administrator diverts IRS resources from its core mission, and can diminish taxpayer service.

Among the biggest contributors to this problem is the new health care law, which gives the IRS a host of new responsibilities, including the indoor tanning tax, new taxes and fees on employers and individuals, and a complex small business tax credit.

For 2011 fiscal year, the IRS has requested nearly \$6 billion, an increase of more than 8 percent from the fiscal year 2011 appropriation. Included in this \$6 billion is a request for nearly a half-a-billion dollars and over 1,200 new employees to implement the health care law's new provisions.

And the cost of the health care law do not end there. IRS's implementation of the health care law is estimated to cost somewhere between \$5 billion and \$10 billion over the next 10 years. So, in addition to the current tax return filing season and the IRS budget request, I hope we can take this opportunity to discuss this dual mission, and whether it is hampering the IRS's ability and core revenue collection responsibilities.

So, with that, I want to welcome Commissioner Shulman today, who is here to testify, and look forward to a fruitful discussion of his agency, its mission, and the ongoing tax return filing season.

Commissioner, I know you were working under very time-constrained circumstances with the passage of the law in December. I know you have scrambled to get things done. And it seems to me at this stage things are going fairly well with the filing season, so we look forward to your comments.

Before I yield to Ranking Member Lewis, I ask unanimous consent that all Members' written statements be included in the record.

[No response.]

Chairman BOUSTANY. Without objection, so ordered. I also ask unanimous consent that the GAO's interim report on the 2011 tax filing season, which is being released today, also be included in the record.

[No response.]

Chairman BOUSTANY. Without objection, so ordered.

[The information follows: GAO's Interim Report, 2011]

---

**GAO**

United States Government Accountability Office

Report to Congressional Requesters

---

March 2011

## 2011 TAX FILING

IRS Dealt with  
Challenges to Date but  
Needs Additional  
Authority to Verify  
Compliance



---

GAO-11-481

---

## Contents

<b>Letter</b>		1
	Scope and Methodology	2
	Background	3
	Interim Filing Season Results	4
	Conclusion	5
	Matter for Congressional Consideration	6
	Agency Comments and Our Evaluation	6
<b>Appendix I</b>	<b>Updated Slides from the March 23 and March 24, 2011, Congressional Briefings</b>	8
<b>Appendix II</b>	<b>IRS's Existing Math Error Authority</b>	37
<b>Appendix III</b>	<b>Descriptions of IRS Volunteer Income Tax Assistance/Tax Centers for the Elderly and Treasury Programs to Offer Tax Refunds on Debit Cards</b>	38
<b>Appendix IV</b>	<b>GAO Contact and Staff Acknowledgments</b>	41
<b>Tables</b>		
	Table 1: IRS's 13 Existing MEAs	37
	Table 2: Tax Refunds Offered on Debit Cards at IRS VITA and TCE Sites	38
	Table 3: Treasury Pilot Debit Card Program Offers	39

---

**Abbreviations**

CADE	Customer Account Data Engine
E-file	Electronic filing
EITC	Earned Income Tax Credit
FDIC	Federal Deposit Insurance Corporation
IRS	Internal Revenue Service
IVR	Interactive voice response
MEA	math error authority
MeF	Modernized e-File
SMS	Short messaging service
TCE	Tax Center for the Elderly
TIN	Taxpayer identification number
Treasury	Department of the Treasury
VITA	Volunteer Income Tax Assistance

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.



United States Government Accountability Office  
Washington, DC 20548

March 29, 2011

The Honorable Max Baucus  
Chairman  
Committee on Finance  
United States Senate

The Honorable Charles E. Grassley  
Ranking Member  
Committee on the Judiciary  
United States Senate

The Honorable Charles W. Boustany, Jr.  
Chairman  
The Honorable John Lewis  
Ranking Member  
Subcommittee on Oversight  
Committee on Ways and Means  
House of Representatives

Every tax filing season is a large-scale undertaking during which the Internal Revenue Service (IRS) interacts with taxpayers by processing returns, issuing refunds, answering telephone calls, and providing other services, both face-to-face and on its Web site. As part of processing returns and before refunds are issued, IRS uses its statutory authority to automatically correct errors. This allows IRS to avoid costly and burdensome audits and taxpayers to be made aware of additional taxes owed before being required to pay interest and penalties. For the 2011 filing season, IRS is administering a number of complex tax law changes, including the Residential Energy Property Tax Credit and provisions enacted in December 2010 as part of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (commonly known as the tax extenders).<sup>1</sup>

Other changes for the 2011 filing season include paid preparer regulations and expanded efforts to provide refunds on debit cards. In 2011, for the first time, paid preparers must register with IRS. In the future, certain paid preparers will be subject to competency tests and continuing education

<sup>1</sup>L.R.C. § 25C and Pub. L. No. 111-312, respectively.



---

requirements to be allowed to prepare tax returns.<sup>2</sup> This year IRS is offering refunds on debit cards to taxpayers at almost all of its roughly 12,000 Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) sites. Also, the Department of the Treasury (Treasury) is pilot testing whether offering refunds on debit cards on a larger scale would be feasible.

As part of our ongoing assessment of IRS's 2011 filing season being conducted at your request, on March 23 and 24, 2011, we briefed the offices of the Senate Committee on Finance and the Subcommittee on Oversight, House Committee on Ways and Means, respectively, on IRS's performance to date. This report includes updated materials presented at the briefing in appendix I.

Based on discussions with your offices, our objective was to provide an interim assessment of IRS's performance during the 2011 filing season, including its efforts to streamline returns processing, conduct pre-refund compliance checks, improve taxpayer service, and issue refunds on debit cards.

---

## Scope and Methodology

To accomplish our objective, we

- obtained and analyzed data from IRS related to processing returns, telephone service, Web site performance, and debit card refund offers;
- reviewed documentation to identify areas where additional statutory authority to conduct automated pre-refund compliance checks would benefit taxpayers or IRS;
- obtained and analyzed Treasury data on its 2011 debit card initiative and plans to evaluate it and also interviewed Treasury officials;
- interviewed representatives of tax preparation and tax software firms about challenges IRS faced during the 2011 filing season;
- interviewed IRS officials on various aspects of filing season performance, including ongoing efforts to provide refunds on debit cards at VITA and TCE sites and efforts to evaluate the program; and
- interviewed Treasury Inspector General for Tax Administration officials about IRS's 2011 filing season.

We interviewed IRS and Treasury officials and determined that the data presented in our briefing were sufficiently reliable for our purposes. We

---

<sup>2</sup>We plan to issue a report on paid preparer regulations in March 2011.

---

conducted this performance audit in March 2011 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

---

## Background

IRS is making major changes to how it processes individual income tax returns. IRS initiated its current Customer Account Data Engine (CADE) in 1999 to provide a modernized system for processing tax returns, which proved to be more complicated than IRS expected. As a result, IRS created a new strategy referred to as CADE 2, which it expects to deliver in three phases—one in 2012, one in 2014, and one at a yet to be determined date. IRS is finalizing plans to deliver the first phase of CADE 2 for the 2012 filing season, and, if effectively implemented, IRS expects it should provide many benefits, including providing faster refunds and IRS with more timely account information. IRS's Modernized E-file (MeF) system is expected to replace the legacy electronic filing (e-file) system, which IRS is scheduled to retire in October 2012. MeF provides taxpayers with a faster acknowledgment that their returns have been accepted and better information on why electronically filed returns are rejected.

In the past, Congress has granted IRS statutory authority, called math error authority (MEA), to correct calculation errors and check for obvious noncompliance, such as claims above income and credit limits. In some cases, MEA allows IRS to use prior year tax return information to verify compliance before issuing refunds. These automated and relatively low-cost compliance checks (compared to audits) can prevent erroneous refunds and avert the need to try to recover such payments. Congress must grant IRS specific authority to use MEA for purposes beyond computational errors. For example, in 2009, Congress gave IRS MEA following our suggestion that IRS should be authorized to determine whether taxpayers claimed the First-Time Homebuyer Credit more than once.<sup>3</sup> For more discussion of IRS's and taxpayers' responsibilities and

---

<sup>3</sup>Congress enacted the First-Time Homebuyer Credit to assist the struggling housing market and help taxpayers purchase their first homes. GAO, *Tax Administration: Opportunities Exist for IRS to Enhance Taxpayer Service and Improve Enforcement for the 2010 Filing Season*, GAO-09-1026 (Washington, D.C.: Sept. 23, 2009).

rights under MEA, see our 2010 report.<sup>4</sup> IRS's 13 existing MEAs are described in appendix II.

Since 2009, IRS has worked with partner organizations at VITA and TCE sites to encourage taxpayers not requesting a direct deposit of their refund to opt to receive it on a debit card sponsored by a participating financial institution. Separately, in 2011, Treasury launched a pilot program which offers low-income taxpayers tax refunds on debit cards. Although targeting the same demographic group, the VITA site offer is made in person and the Treasury offer is made through the mail. Both the IRS and Treasury initiatives are intended to reduce the cost of delivering refunds to taxpayers, provide faster refunds compared to paper checks, reduce transaction costs, and provide individuals who might not otherwise have access with an ongoing financial account to obtain banking services.<sup>5</sup>

## Interim Filing Season Results

- As of March 18, 2011, IRS had processed about 73 million returns and issued about 65 million refunds totaling close to \$193 billion.
- The percentage of e-filed returns continues to grow, which remains important because it significantly reduces IRS's costs and speeds refunds. For fiscal year 2009, IRS reported that it costs 19 cents to process an e-filed return compared to \$3.29 for a paper return.
- Late tax law changes in 2010 resulted in IRS not being able to accept certain returns until mid-February 2011 because of the time it took to complete programming changes. According to officials from IRS's Business Modernization Office, when CADE 2 and MeF are fully implemented, IRS will be able to reprogram its computers more efficiently.
- IRS's inability to accept certain returns until mid-February also affected paid preparers and tax preparation software providers. Representatives from those groups told us that some taxpayers believed that the delay applied to all tax returns and delayed filing as a result, effectively condensing the filing season. According to IRS data,

<sup>4</sup>GAO, *Recovery Act: IRS Quickly Implemented Tax Provisions, but Reporting and Enforcement Improvements Are Needed*, GAO-10-349 (Washington, D.C.: Feb. 10, 2010). In this report, we suggested that Congress should provide IRS with broader MEA.

<sup>5</sup>We previously recommended that IRS examine the feasibility of offering refunds on debit cards. See, GAO, *2009 Tax Filing Season: IRS Met Many 2009 Goals, but Telephone Service Remained Low, and Taxpayer Service and Enforcement Could Be Improved*, GAO-10-225 (Washington, D.C.: Dec. 10, 2009), and *Tax Administration: Most Filing Season Services Continue to Improve, but Opportunities Exist for Additional Savings*, GAO-07-27 (Washington, D.C.: Nov. 15, 2006).

---

IRS received about 21 percent fewer returns through mid-February 2011 compared to mid-February 2010. Those same representatives also expressed some concerns about the new paid preparer registration process.<sup>6</sup>

- IRS has rejected about 13 percent of e-filed returns for reasons such as incorrect personal identification numbers. According to IRS officials, when returns are rejected through MeF, taxpayers receive better information on why returns are rejected and MeF allows taxpayers to submit additional documentation electronically, both of which reduce IRS's costs.
- IRS lacks MEA to review prior year tax returns to verify compliance with lifetime limits on amounts that can be claimed. For example, IRS does not have MEA to verify that the Residential Energy Credits claimed for 2009 and 2010 do not exceed the lifetime credit limit of \$1,500. According to IRS officials, evidence exists that some taxpayers may be claiming Residential Energy Credits beyond the limit. Without MEA, IRS must ensure compliance through audits, which are time consuming for taxpayers and too costly to conduct in large numbers.
- Total telephone call volume increased by nearly 13 percent compared to volume during the same time period last year. Wait times to speak to an assistor averaged about 10 minutes, slightly longer than last year.
- The number of visits to IRS's Web site has increased by about 9 percent compared to visits during the same time period last year.
- It is too early to tell the extent to which the various debit card offers are being accepted by taxpayers. Both IRS and Treasury officials said they will evaluate their programs after the filing season.<sup>7</sup>

---

## Conclusion

IRS has had to deal with several challenges this filing season, including late tax law changes and an increase in the volume of telephone calls. IRS's inability to accept certain returns until mid-February highlights the importance of fully implementing new systems to modernize returns processing, particularly CADE 2 and MeF. According to IRS officials, these systems should allow IRS to more easily accommodate tax law changes and issue refunds faster.

---

<sup>6</sup>Our forthcoming report on paid preparer regulations will discuss IRS's efforts to implement the program.

<sup>7</sup>IRS designed the evaluation based in part on a recommendation we made in 2010 for IRS to include the full range of stakeholders in its analysis of the debit card program. See GAO, *2010 Tax Filing Season: IRS's Performance Improved in Some Key Areas, but Efficiency Gains Are Possible in Others*, GAO-11-111 (Washington, D.C.: Dec. 16, 2010).

---

	<p>Additional MEA to verify compliance with lifetime limits on credits and deductions has advantages, compared to audits, for both taxpayers and IRS. For example, taxpayer errors can be caught and corrected before they result in penalties. This, in turn, would allow IRS to use its expensive auditors' time on more significant compliance problems.</p>
<b>Matter for Congressional Consideration</b>	<p>To ensure that IRS can adequately enforce certain tax provisions, Congress should provide IRS with MEA to use tax return information from previous years to ensure that taxpayers do not improperly claim credits or deductions in excess of lifetime limits where applicable.</p>
<b>Agency Comments and Our Evaluation</b>	<p>IRS officials provided us with technical comments on this report, which we incorporated as appropriate.</p> <p>As agreed with your offices, unless you publicly announce the contents of this report earlier, we plan no further distribution until 2 days from the report date. At that time, we will send copies of this report to the Chairmen and Ranking Members of other Senate and House committees and subcommittees that have appropriation, authorization, and oversight responsibilities for IRS. We will also send copies to the Commissioner of Internal Revenue, the Secretary of the Treasury, the Chairman of the IRS Oversight Board, and the Director of the Office of Management and Budget.</p> <p>The report also is available at no charge on the GAO Web site at <a href="http://www.gao.gov">http://www.gao.gov</a>. If you or your staff have any questions or wish to</p>

---

discuss the material in this report further, please contact me at (202) 512-9110 or at [whitej@gao.gov](mailto:whitej@gao.gov). Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. Major contributors to this report are listed in appendix IV.


A handwritten signature in black ink that reads "James R. White". The signature is written in a cursive, flowing style.

James R. White  
Director, Tax Issues  
Strategic Issues

---

**Appendix I: Updated Slides from the  
March 23 and March 24, 2011, Congressional  
Briefings**

---



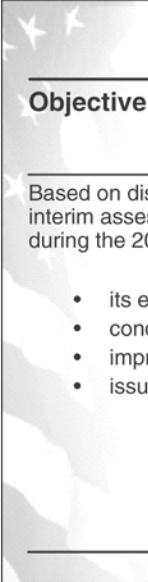

---

**2011 Tax Filing:  
IRS Dealt with Challenges to Date but Needs Additional  
Authority to Verify Compliance**

**Senate Committee on Finance and Subcommittee on  
Oversight, House Committee on Ways and Means,  
March 23 and 24, 2011**

---

---



---

## Objective

---


Based on discussions with your offices, our objective was to provide an interim assessment of the Internal Revenue Service's (IRS) performance during the 2011 filing season, including:

- its efforts to streamline returns processing;
- conduct pre-refund compliance checks;
- improve taxpayer service; and
- issue refunds on debit cards.

---

Page 2






## Results in Brief

- To date, for the 2011 tax filing season:
  - IRS processed about 73 million returns and issued about 65 million refunds and the percentage of taxpayers filing electronically continues to grow, which is important because it reduces IRS's costs.
  - IRS's inability to process certain returns until mid-February highlights the need for IRS to complete new systems.
  - IRS lacks statutory authority to review prior year tax returns for provisions with lifetime limits on the amount that can be claimed.
  - Total call volume increased by about 13 percent and the average wait time to reach a live assistor was about 10 minutes.
  - The number of visits to IRS's Web site has increased by about 9 percent.
  - It is too early to tell the extent to which debit card offers are being accepted by taxpayers. Both IRS and Treasury officials said they will evaluate their programs this year.

Page 3



## Scope and Methodology

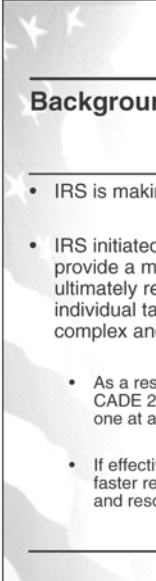

---

- To accomplish our objective, we
  - obtained and analyzed data from IRS related to processing returns, telephone service, Web site performance, and debit card offers;
  - reviewed debit card refund offers;
  - reviewed documentation to identify areas where additional statutory authority to conduct automated pre-refund compliance checks would benefit taxpayers or IRS;
  - obtained and analyzed Department of the Treasury (Treasury) data on its 2011 debit card initiative and plans to evaluate it and also interviewed Treasury officials;
  - interviewed representatives of tax preparation and tax software firms about challenges IRS faced during the 2011 filing season;
  - interviewed IRS officials on various aspects of filing season performance, including ongoing efforts to provide refunds on debit cards at Volunteer Income Tax Assistance (VITA) and Tax Center for the Elderly (TCE) sites and efforts to evaluate the program; and
  - interviewed Treasury Inspector General for Tax Administration (TIGTA) officials about IRS's 2011 filing season.
- As part of our ongoing work on IRS's 2011 filing season performance, we conducted this performance audit in March 2011 in accordance with generally accepted government auditing standards. We interviewed IRS and Treasury officials and determined that the data presented in this briefing were sufficiently reliable for our purposes.

---

Page 4

---



---

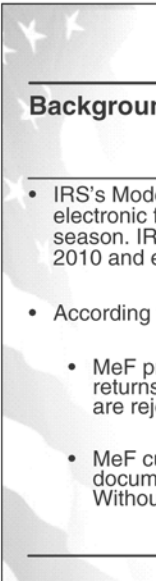

## Background

- IRS is making major changes to how it processes individual income tax returns.
- IRS initiated its current Customer Account Data Engine (CADE) in 1999 to provide a modernized system for processing tax returns, with the intention of ultimately replacing the Individual Master File (IMF), the authoritative source for individual taxpayer accounts. However, developing the system was more complex and taking longer than IRS expected.
  - As a result, IRS created a new strategy to replace the current CADE, referred to as CADE 2, which it expects to deliver in three phases—one in 2012, one in 2014, and one at a yet to be determined date.
  - If effectively implemented, CADE 2 should provide many benefits, including providing faster refunds and IRS with access to more timely account data for use in compliance and resolution of taxpayer questions or issues.

---

Page 5

---



---

### Background, Cont'd


---

- IRS's Modernized E-file (MeF) system is expected to replace the legacy electronic filing (e-file) system and be fully operational for the 2012 filing season. IRS began accepting some individual tax returns on MeF in 2010 and expects to retire the legacy e-file system in October 2012.
- According to IRS officials:
  - MeF provides taxpayers with a faster acknowledgment that their returns have been accepted and better information on why returns are rejected.
  - MeF currently provides IRS with the ability to accept additional documentation electronically through portable document files. Without MeF, IRS must accept certain returns on paper.

---

Page 6

---



---


### Background, Cont'd

---

- Taxpayers and IRS rely heavily on paid preparers and tax preparation software providers. About 90 percent of returns are prepared by individual taxpayers or paid preparers using tax preparation software. Additionally, in 2010, over 70 percent of taxpayers electronically filed their tax returns, which has benefits for IRS.
- In 2011, paid preparers must register with IRS, and in the future, certain paid preparers will be subject to competency tests and continuing education requirements to be allowed to prepare tax returns.
  - We plan to issue a report on paid preparer regulations at the end of March 2011.

---


Page 7



### Background, Cont'd

- Complex tax law changes enacted in December 2010 as part of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010—commonly referred to as the tax extenders ( Pub. L. No. 111-312)—caused IRS to be unable to process returns until February 14, 2011, for taxpayers
  - filing a Schedule A, because of the extension of the state and local general sales tax deduction;
  - claiming the higher education tuition and fees deduction on Form 8917; or
  - claiming the educator expense deduction, for K-12 educators with out-of-pocket classroom expenses.
- In addition, IRS is administering the Residential Energy Property Credit (I.R.C. § 25C). This credit allows taxpayers to receive 30 percent of the cost of improvements with a maximum lifetime credit limit of \$1,500 for the combined 2009 and 2010 tax years (Pub. L. No. 111-5, § 1121).
  - In 2011, the limit drops to 10 percent of the cost of improvements with a \$500 credit limit (Pub. L. No. 111-312, § 710).

Page 8




## Background, Cont'd

- As part of its pre-refund compliance checks, Congress has granted IRS 13 specific math error authorities (MEA). MEA allows IRS to correct calculation errors and check for obvious noncompliance, such as claims above income and credit limits. Congress
  - must grant MEA to IRS for purposes beyond correcting computational errors.
  - has granted MEA to use information from prior year returns to determine compliance. This was the case following our Matter for Congressional Consideration on the First-Time Homebuyer Credit.<sup>1</sup> IRS's existing MEA is described in appendix II of our report
- When IRS has MEA, it does not have to provide the taxpayer with a statutory notice of deficiency to correct a return.
- Correcting errors before issuing refunds allows IRS to avoid costly and burdensome audits and taxpayers may receive larger refunds or be made aware of additional taxes owed before they are required to pay interest and penalties.
- We previously suggested that Congress should provide IRS with broader MEA.<sup>2</sup> Congress has yet to provide IRS with this authority.

<sup>1</sup> GAO, *Tax Administration: Opportunities Exist for IRS to Enhance Taxpayer Service and Improve Enforcement for the 2010 Filing Season*, GAO-09-1026 (Washington, D.C.: Sept. 23, 2009).

<sup>2</sup> GAO, *Recovery Act: IRS Quickly Implemented Tax Provisions, but Reporting and Enforcement Improvements Are Needed*, GAO-10-349 (Washington, D.C.: Feb. 10, 2010).

Page 9




### Background, Cont'd

- Since 2009, a small number of VITA sites have encouraged taxpayers not requesting a direct deposit to opt for a debit card sponsored by a participating financial institution.
  - In 2010, IRS partnered with three large financial institutions to offer debit cards at 20 VITA sites. However, only about 3 percent of eligible taxpayers elected to receive the cards, down from 8 percent of eligible taxpayers in 2009.<sup>3</sup>
  - Taxpayers may sign up for the card at a participating VITA site.
- In 2011, Treasury launched a pilot program that offers low-income taxpayers and taxpayers without bank accounts debit cards to receive their refunds at a low cost.
  - Treasury informed taxpayers of this program through targeted mailings.

<sup>3</sup>GAO, 2010 Tax Filing Season: IRS's Performance Improved in Some Key Areas, but Efficiency Gains Are Possible in Others, GAO-11-111 (Washington, D.C.: Dec. 16, 2010).

Page 10



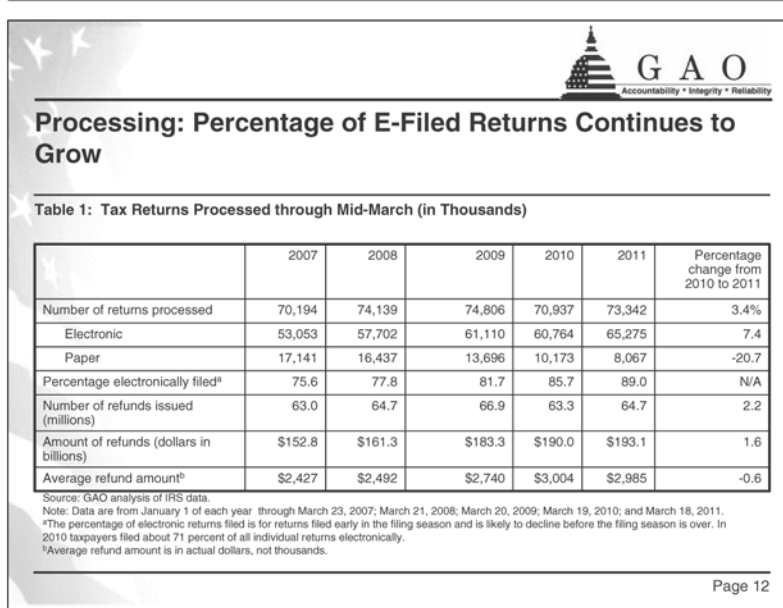


### Background, Cont'd

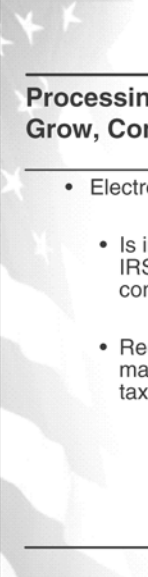

- These debit card initiatives are intended to
  - reduce the cost of delivering refunds to taxpayers, provide faster refunds compared to paper checks, and reduce transaction costs and
  - provide banking services to individuals who might not otherwise have access to an ongoing financial account.
- We previously recommended that IRS examine the feasibility of offering refunds on debit cards.<sup>4</sup> IRS stated that they were exploring a range of options to deliver refunds to unbanked taxpayers, including providing refunds on debit cards.

<sup>4</sup>GAO, 2009 Tax Filing Season: IRS Met Many 2009 Goals, but Telephone Access Remained Low, and Taxpayer Service and Enforcement Could Be Improved, GAO-10-225 (Washington, D.C.: Dec. 10, 2009), and Tax Administration: Most Filing Season Services Continue to Improve, but Opportunities Exist for Additional Savings, GAO-07-27 (Washington, D.C.: Nov. 15, 2006).

Page 11



---



---


### Processing: Percentage of E-Filed Returns Continues to Grow, Cont'd

---

- Electronic filing:
  - Is important because it reduces IRS's costs. For fiscal year 2009, IRS reported that it cost 19 cents to process an e-filed return compared to \$3.29 for a paper return.
  - Reduces errors because it eliminates the need for IRS to manually transcribe information from returns and it allows taxpayers to receive refunds faster.

---


Page 13



**Processing: IRS's Inability to Process Certain Returns until Mid-February Highlights the Need for IRS to Complete New Systems**

- According to officials from IRS's Business Modernization Office, when CADE 2 and MeF are fully implemented, IRS will be able to reprogram its computers more efficiently following tax law changes.
- As of March 18, 2011, over 24 million returns have been processed using the current CADE.
- In 2011, IRS expects to process approximately 42 million returns using the current CADE, about the same as last year.
- IRS plans to retire the current CADE later this year and all taxpayer accounts will be shifted to accelerated processing on the IMF next year and then to CADE 2. Accelerated processing on the IMF will also result in faster refunds to all taxpayers.


Page 14



**Processing: IRS's Inability to Process Certain Returns Until Mid-February Highlights the Need for IRS to Complete New Systems, Cont'd.**

- IRS data show that through March 27, 2011, MeF had accepted about 4.8 million individual returns (on Form 1040), up from about 281,000 returns at the same time last year.
- Last year we noted that IRS-authorized e-file providers did not use MeF as much as IRS anticipated because of issues with the system's stability.
- According to industry experts, the MeF system is much more stable this filing season and IRS is continuing to promote its use.
- IRS plans to fully retire the legacy e-file system in October 2012 and use MeF to accept all individual tax returns after that.


Page 15



**Processing: IRS's Inability to Accept Certain Returns until Mid-February Also Affected Paid Preparers and Tax Preparation Software Providers**

- According to industry experts representing paid preparers and tax preparation software firms we interviewed:
  - Some taxpayers believed that the delay applied to all tax returns and not a limited number of tax returns and delayed filing as a result;
  - Delays result in tax professionals preparing and transmitting to IRS a larger volume of returns in a shorter period of time, effectively condensing the filing season. According to IRS data, IRS received about 21 percent fewer returns through mid-February 2011 compared to mid-February 2010.
  - The implementation of new paid preparer regulations caused some concerns, but did not indicate that the new rules have had a significant effect on return preparation during the 2011 filing season.
- Our forthcoming report on paid preparer regulations will discuss IRS's efforts to implement the program.

Page 16




### Processing: Reducing Rejected Electronic Returns Could Result in Cost Savings

- IRS automatically rejects a return and sends it back to the taxpayer when basic information provided by the taxpayer, such as verification of identity with a personal identification number (PIN) or address, does not match IRS records.
- As of March 21, 2011, IRS had a rejection rate of 13 percent for electronically filed returns.
  - According to IRS data, the most common reasons for rejection were (1) incorrect PIN information provided, (2) a dependent's Social Security number not matching the IMF, and (3) incorrect information for taxpayers claiming the Earned Income Tax Credit.<sup>5</sup>
- MeF provides better information to taxpayers on why returns are rejected and allows taxpayers to submit additional documentation electronically, both of which, according to IRS, reduce IRS's costs.
- Taxpayers with rejected returns frequently call IRS to learn why and may refile on paper rather than electronically. It costs IRS about \$25 for an IRS assistor to answer a call and about \$3.10 extra to process a paper return.

<sup>5</sup>The Earned Income Tax Credit is a refundable tax credit for moderate and low-income working individuals and families. For refundable credits, taxpayers receive payments even when there is no tax liability.

Page 17

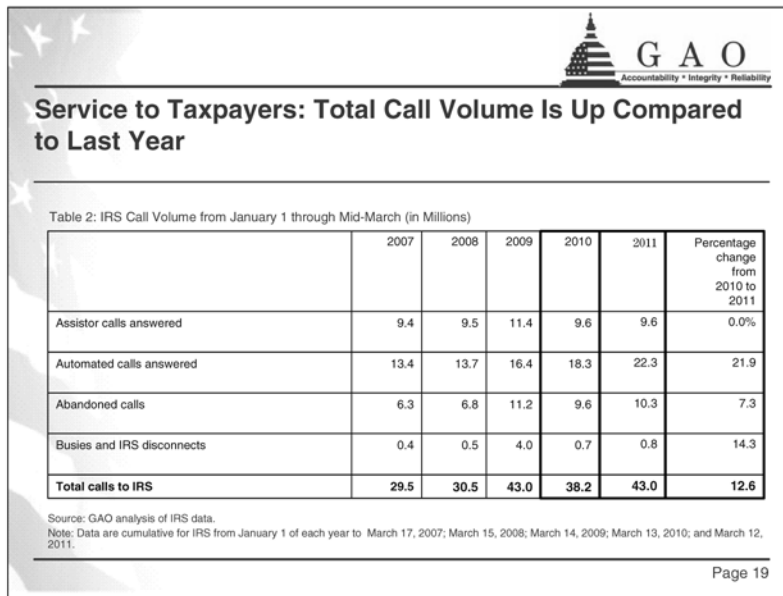


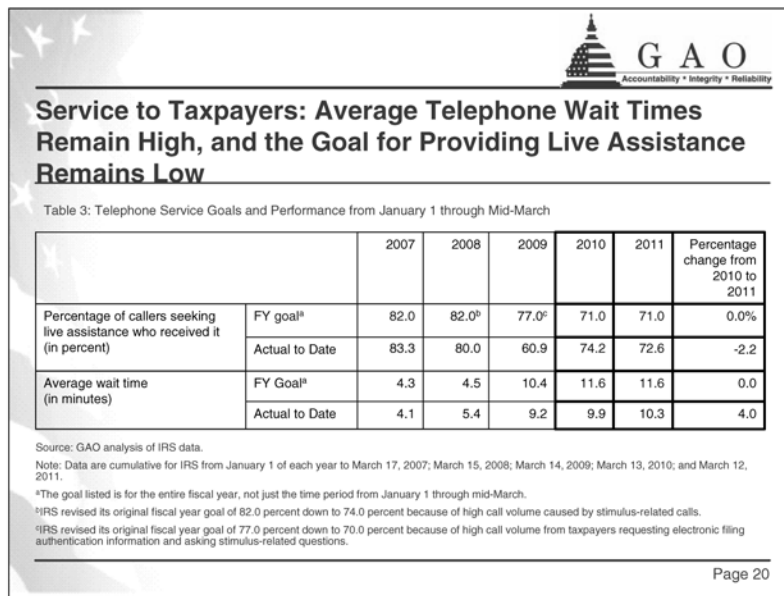
### Pre-Refund Compliance Checks: IRS Lacks MEA to Use Prior Year Information


- IRS lacks MEA to review prior year tax returns for provisions with lifetime limits on the amount that can be claimed.
  - For example, IRS does not have MEA that would allow it to review the 2009 return to see if the total amount of Residential Energy Credits claimed for 2009 and 2010 exceeds the \$1,500 lifetime limit.
  - According to IRS officials, preliminary analysis conducted by TIGTA indicates that some taxpayers may be claiming more Residential Energy Credits than they are entitled to claim.
- Without MEA, IRS must ensure compliance through audits, which are time consuming for taxpayers and costly for IRS. Resource constraints also limit the number of audits IRS can complete in a given year.

Page 18





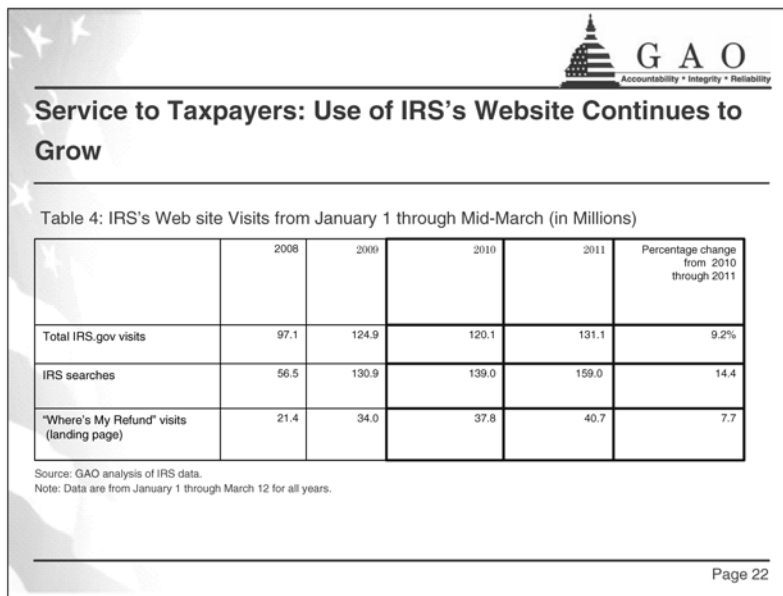





### **Service to Taxpayers: IRS Has Requested Additional Funding to Improve Its Level of Telephone Service**

- IRS sets its annual goal for telephone level of service—the percentage of taxpayers seeking live assistance who actually receive it—based on anticipated call volume and available resources.
- IRS has requested additional funds to increase the goal for level of service to 80 percent in fiscal year 2012.
- The level of service goal for fiscal year 2011 remains 71 percent, the same as in fiscal year 2010. IRS has asked for an additional \$20.9 million to raise this goal to 75 percent, but has not received this funding under the current continuing budget resolution.
- In its fiscal year 2012 budget request, IRS asked for an additional \$30 million (on top of the \$20.9 million requested in 2011) to raise the level of telephone service to 80 percent.

Page 21






### Service to Taxpayers: IRS Has Requested Funding to Expand Its E-Services

- IRS is taking steps to improve its Web site, including planning to invest \$320 million over 10 years to introduce a new Web site by the 2013 filing season.
- For the fiscal year 2011 budget, IRS asked for \$25 million to upgrade its public user portal, which will allow for the installation of additional e-services, but has not received this funding under the current continuing budget resolution.
- For the fiscal year 2012 budget, IRS requested \$25 million to replace both the employee and registered user portal (on top of the \$25 million requested in 2011). IRS requested an additional \$8 million to create an e-service, called E-Notices.
- This service would allow taxpayers who have entered into installment agreements to opt for monthly electronic payment reminders.


Page 23



### Issuing Refunds on Debit Cards: IRS Partners with Financial Institutions to Offer Debit Cards at VITA Sites

- For 2011 IRS is partnering with J.P. Morgan Chase, PNC Bank, U.S. Bank, and Western Union (PNC and U.S. Bank also participated last year) to offer refunds on debit cards and debit cards are available to taxpayers at almost all of IRS's roughly 12,000 volunteer sites across the country. Additionally, IRS partner organizations work with financial institutions locally to provide debit cards to taxpayers.
  - Debit cards from Western Union are available through the software program used to prepare returns at nearly all VITA sites. This card includes a \$1.95 fee per ATM withdrawal and may only be used in the United States.
  - The other three partnering financial institutions offer debit cards at a limited number of VITA sites (18 sites, 154 sites, and 45 sites, respectively).
- All four options include no monthly or activation fee.
- All of the debit cards except the Western Union card include free in-network ATM withdrawals. Except for Western Union, each bank has ATMs in a limited number of states.


Page 24



### Issuing Refunds on Debit Cards: Treasury's 2011 Pilot Program Involves Testing Different Debit Card Offers

- In January 2011, Treasury mailed offers to about 808,000 taxpayers who likely make less than \$35,000 per year, and are unlikely to have bank accounts.
  - Treasury offered eight different options to different groups of taxpayers, randomly assigning which taxpayers received which offer, to test how taxpayers respond to the different offers. Program invitees may only enroll in the option they received with their offer and may not choose among offers.
  - The offers vary by monthly fee (\$4.95 or none) and whether the card includes access to a savings account. The offers also differ based on the message used to promote the card (convenience versus safety).
- All cards are provided on a Visa debit card by a contractor selected by Treasury. Card options include no acquisition fee, free in-network ATM withdrawals, and \$2.50 out-of-network ATM withdrawals.
  - According to Treasury officials, if Treasury expands the program next year they will hold a competitive bidding process to select the contractor.
- Appendix III of our report provides a more detailed comparison of the Treasury and IRS programs

Page 25




### Issuing Refunds on Debit Cards: Both IRS and Treasury Are Conducting Program Evaluations

- It is too early to tell what the take-up rate for the IRS program will be this year or whether any of the debit card options in the Treasury program will be widely used. Both IRS and Treasury plan to evaluate their programs after the filing season.
- IRS will apply social marketing principles and techniques to promote and increase the use of prepaid cards by different target groups.<sup>6</sup>
  - IRS will engage a range of stakeholders and partners to issue a program evaluation report by August 2011.
  - IRS designed its evaluation based, in part, on a recommendation we made in 2010 for IRS to include the taxpayers, volunteer site partners, and other stakeholders in its analysis of the debit card program.<sup>7</sup>

<sup>6</sup>Social marketing emphasizes listening to the needs and desires of the target audience to develop a program to benefit them.  
<sup>7</sup>GAO-11-111.

Page 26





---


### **Issuing Refunds on Debit Cards: Both IRS and Treasury Are Conducting Program Evaluations, Cont'd**

---

- Treasury contracted with the Urban Institute, a research organization, to evaluate its debit card program. The study will compare taxpayers' responsiveness to the eight different offers and evaluate the design and execution of the program.
- The study should be publicly released later this year, and, according to Treasury officials, will be used as one of the factors in the decision regarding the future of its debit card program.

---

Page 27



---

## Conclusion

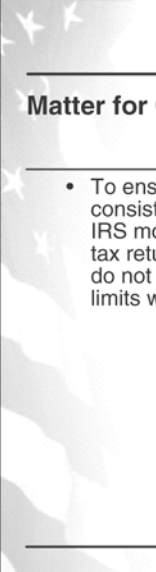

---

- IRS has had to deal with several challenges this filing season, including late tax law changes and an increase in the volume of telephone calls. IRS's inability to accept certain returns until mid-February highlights the importance of fully implementing new systems to modernize returns processing, particularly CADE 2 and MeF. According to IRS officials, these systems should allow IRS to more easily accommodate tax law changes and issue refunds faster.
- Additional MEA to verify compliance with lifetime limits on credits and deductions has advantages, compared to audits, for both taxpayers and IRS. For example, taxpayer errors can be caught and corrected before they result in penalties. This, in turn, would allow IRS to use its expensive auditors' time on more significant compliance problems.

---

Page 28

---



---

### Matter for Congressional Consideration

---

- To ensure IRS can adequately enforce certain tax provisions and consistent with our previous suggestion that Congress grant MEA to IRS more broadly, Congress should provide IRS with MEA to use tax return information from previous years to ensure that taxpayers do not improperly claim credits or deductions in excess of lifetime limits where applicable.

---

Page 29

## Appendix II: IRS's Existing Math Error Authority

Table 1 summarizes the Internal Revenue Service's (IRS) existing math error authority (MEA).

**Table 1: IRS's 13 Existing MEAs**

No.	Description
1	An error in addition, subtraction, multiplication, or division shown on any return.
2	An incorrect use of any table provided by IRS with respect to any return if other information in the return makes the incorrect use apparent.
3	An entry on a return of an item that is inconsistent with another entry of the same or different item on that return.
4	An omission of information that is required to be supplied on the return to substantiate an entry on that return.
5	An entry on a return of a deduction or credit in an amount that exceeds the statutory limit for that deduction or credit, if that limit is expressed as a specific monetary amount or as a percentage, ratio, or fraction, and if the component items of that limit appear on the return.
6	A correct Taxpayer Identification Number (TIN) not provided on the return as required for the following provisions: <ul style="list-style-type: none"> <li>• Earned Income Tax Credit (EITC);</li> <li>• child and dependent care credit;</li> <li>• personal or dependent exemption;</li> <li>• child tax credit; or</li> <li>• Hope and Lifetime Learning credits.</li> </ul>
7	A return claiming an EITC for net earnings from self-employment, where the self-employment tax imposed by I.R.C. § 1401 on those net earnings has not been paid.
8	An omission of information required for recertification of eligibility for the EITC.
9	An entry on the return of a TIN required for the EITC, the child credit, and the child and dependent care credit, when information associated with that TIN indicates that the child does not meet the age eligibility requirements for those credits.
10	An entry on the return of a claim for the EITC where the Federal Case Registry of Child Support Orders indicates that the taxpayer is the noncustodial parent of that child.
11	A failure to reduce Electronic Stimulus Payment credit on a return related to the Economic Stimulus Act of 2008 by amounts previously advanced.
12	A failure to reduce the Making Work Pay credit by the amount of any payment received as a result of tax abatement resulting from the combat-related deaths of members of the Armed Forces, deaths of astronauts, and deaths of victims of certain terrorist attacks, or by the amount of any credit allowed under the American Recovery and Reinvestment Act of 2009, or a failure to submit a proper Social Security number with the claim.
13	A claim for the First Time Homebuyer Credit where the taxpayer has not included the required settlement statement; or where other information indicates that the taxpayer is under 18 years of age, or where information from the past 2 years of returns indicates ineligibility for the credit. Additionally, IRS may correct the return where the taxpayer has failed to include the increased tax required under the recapture provision for the credit, when applicable.

Source: GAO analysis.

## Appendix III: Descriptions of IRS Volunteer Income Tax Assistance/Tax Centers for the Elderly and Treasury Programs to Offer Tax Refunds on Debit Cards

Table 2 provides further details on the debit cards being offered at Volunteer Income Tax Assistance (VITA) and Tax Center for the Elderly (TCE) sites.

**Table 2: Tax Refunds Offered on Debit Cards at IRS VITA and TCE Sites**

	J.P. Morgan Chase	PNC Bank	U.S. Bank	Western Union
Type of card	Visa	Visa	Visa	MasterCard
Card activation	Free	Free	Free	Free
Monthly maintenance	Free	Free	Free	Free
Signature purchase	Free	Free	Free	Free
PIN Purchase	Free	Free	Free	Free
Retailer purchase with cash back option	Free	Free	Free	Free
ATM cash withdrawals	Free at Chase and network	Free at PNC and network	Free at US Bank and network	\$1.95 plus additional ATM fees could be assessed by ATM owner
Bill payment	\$0.75	Free	Free	Free
Live customer service	Free	Free	Two free per month	Free
Overdraft	No fee (\$0.75 per denied transaction for insufficient funds)	No charge	No charge	No charge
Online electronic statements	Free	Free	Free	Free
Payroll direct deposit (employer must have the capabilities for direct deposits)	N/A	Free	Free	Free
Money transfer load	N/A	N/A	N/A	Free
Online/Interactive Voice Response account activity	Free	Free	Free	Free
Short Message Service account notifications (wireless provider could charge a fee)	Free	Free	\$0.15	Free
Card replacement	One free per year. Additional card \$7.50	Free	Free	Free
Cash reloads	N/A	Free at PNC branch	Free at U.S. Bank branch	\$4.95
Teller cash advance	\$10	Free	\$5	Not available
Card consecutive month inactivity fee assessed after	6 months	3 months	3 months	12 months
Relationship building with financial institution	Yes	Yes	Yes	No

Appendix III: Descriptions of IRS Volunteer  
Income Tax Assistance/Tax Centers for the  
Elderly and Treasury Programs to Offer Tax  
Refunds on Debit Cards

	J.P. Morgan Chase	PNC Bank	U.S. Bank	Western Union
Federal Deposit Insurance Corporation protected	Yes	Yes	Yes	Yes
Visa/MasterCard zero liability protected	Yes	Yes	Yes	Yes
Personalized card	Yes	Yes	Yes	Yes
Geographic coverage	Arizona, California, Colorado, Connecticut, Delaware, Florida, Georgia, Idaho, Illinois, Indiana, Kentucky Louisiana, Michigan, Missouri, Nevada, New Jersey, New York, Ohio, Oklahoma, Oregon, South Carolina, Texas, Utah, Washington, West Virginia, and Wisconsin	Delaware, District of Columbia, Florida, Illinois, Indiana, Kentucky, Maryland, Missouri, New York, Ohio, Virginia, West Virginia, and Wisconsin	Arizona, Arkansas, California, Colorado, Florida, Georgia, Idaho, Illinois, Iowa, Kentucky, Minnesota, Missouri, Montana, Nebraska, Nevada, North Dakota, Ohio, Oregon, Pennsylvania, South Dakota, Tennessee, Texas, Utah, Washington, Wisconsin, and Wyoming	USA only

Source: GAO analysis of IRS data.

Table 3 provides additional details on the fee structures offered through Treasury's pilot program.

Table 3: Treasury Pilot Debit Card Program Offers

Service	Fee
Monthly Fee	\$0 or \$4.95 depending on offer (for offers with \$4.95 monthly fee, that charge is waived in any monthly billing cycle in which cardholder loads at least \$1,000 to the Card or makes 30 purchase transactions)
Savings Account	For those participants who are offered a savings feature, there is no charge to open or maintain the account, no minimum balance, and 0.25 percent annual percentage yield (variable rate, subject to change). Fees may apply to withdraw funds if cardholder uses an ATM outside of the MyAccountCard network. There are limitations on the number of transfers in and out of the account per month.
Card acquisition fee	Free
Unlimited ATM cash withdrawals and balance check at 15,000 participating locations nationwide (\$2.50 service fee applies for out-of-network ATM withdrawals)	Free
Transactions at U.S. merchant locations	Free
Purchases online or over the phone	Free
Cash back with purchases	Free
Online bill pay	Free

Appendix III. Descriptions of IRS Volunteer  
Income Tax Assistance/Tax Centers for the  
Elderly and Treasury Programs to Offer Tax  
Refunds on Debit Cards

Service	Fee
Balance inquiries online, by phone, by text and at in-network ATMs (standard text messaging rates may apply from your wireless carrier)	Free
Add money with direct deposit	Free
Lost/stolen card replacement	\$4.95
Second card	\$4.95
Out-of-network ATM cash withdrawals	\$2.50 plus any fee the ATM owner may charge
Teller cash withdrawals	\$2.50
Balance inquiries at out-of-network ATMs	\$0.50
Add money in-person at participating locations	Up to \$4.95
Card use outside of the 50 United States	3 percent of transaction amount

Source: Treasury.

---

## Appendix IV: GAO Contact and Staff Acknowledgments

---

### GAO Contact

James R. White, (202) 512-9110, [whitej@gao.gov](mailto:whitej@gao.gov)

---

### Staff Acknowledgments

In addition to the contact named above, Joanna Stamatiades, Assistant Director; Steven J. Berke; Abbie David; David Fox; Tom Gilbert; Matt Johlle; Inna Livits; Karen O'Connor; and Sabrina Streagle made key contributions to this report.



<b>GAO's Mission</b>	The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.
<b>Obtaining Copies of GAO Reports and Testimony</b>	The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's Web site ( <a href="http://www.gao.gov">www.gao.gov</a> ). Each weekday afternoon, GAO posts on its Web site newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to <a href="http://www.gao.gov">www.gao.gov</a> and select "E-mail Updates."
<b>Order by Phone</b>	<p>The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's Web site, <a href="http://www.gao.gov/ordering.htm">http://www.gao.gov/ordering.htm</a>.</p> <p>Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.</p> <p>Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.</p>
<b>To Report Fraud, Waste, and Abuse in Federal Programs</b>	<p>Contact:</p> <p>Web site: <a href="http://www.gao.gov/fraudnet/fraudnet.htm">www.gao.gov/fraudnet/fraudnet.htm</a>  E-mail: <a href="mailto:fraudnet@gao.gov">fraudnet@gao.gov</a>  Automated answering system: (800) 424-5454 or (202) 512-7470</p>
<b>Congressional Relations</b>	Ralph Dawn, Managing Director, <a href="mailto:dawnr@gao.gov">dawnr@gao.gov</a> , (202) 512-4400 U.S. Government Accountability Office, 441 G Street NW, Room 7125 Washington, DC 20548
<b>Public Affairs</b>	Chuck Young, Managing Director, <a href="mailto:youngc1@gao.gov">youngc1@gao.gov</a> , (202) 512-4800 U.S. Government Accountability Office, 441 G Street NW, Room 7149 Washington, DC 20548



Please Print on Recycled Paper

Chairman BOUSTANY. Now I want to welcome Commissioner Shulman, and I will yield to the ranking member for his opening statement.

Mr. LEWIS. Well, thank you very much, Mr. Chairman. Mr. Chairman, I want to thank you for holding this hearing on the Internal Revenue Service. I am pleased to have the Commissioner before us today. This hearing is timely. I have serious concerns about the Republican plans to cut funding for the agency, and effect that those cuts will have on our taxpayers. The majority's plan to cut \$600 million from the agency budget this year will result in \$4 billion in lost revenue. I do not understand how this helps the deficit.

The plan also harms taxpayers. An estimated three million people will not have their telephone calls answered, and one million people will not receive face-to-face service at an agency center. This makes no sense.

I look forward to discussing the agency's proposed budget for next year. Most of the funds requested for the Affordable Care Act are to assist taxpayers and improve operations, not for enforcement agents, as charged by some.

Finally, I would like to ensure that the Agency has the resources it needs to balance taxpayer services and enforcement. It is important for the agencies to provide services that help elderly, low income, and working class Americans fulfill their tax obligations. It is particularly important that the tax laws are applied fairly to all taxpayers. I look forward to the Commissioner's testimony on how to achieve this balance.

And I welcome you also, Mr. Commissioner. Thank you, Mr. Chairman.

Chairman BOUSTANY. I thank the ranking member. And now I want to welcome IRS commissioner Douglas Shulman.

Commissioner Shulman has served in this position since his appointment in 2008. And, sir, we want to thank you for being here today to testify.

As is customary, you will have the five minutes for your oral statement, to present your testimony, and your full written testimony will be submitted for the record. And I now will yield time to Commissioner Shulman to present your testimony.

Thank you, sir.

#### **STATEMENT OF DOUGLAS SHULMAN, COMMISSIONER, INTERNAL REVENUE SERVICE**

Mr. SHULMAN. Chairman Boustany, Ranking Member Lewis, Members of the Subcommittee, thank you for this opportunity to testify on the filing season, and to provide you with an overview of our proposed 2012 budget.

Despite some of the challenges that the chairman mentioned earlier this year, particularly the late passage of tax law, the 2011 filing season has proceeded smoothly. As of March 19th of this year, we have received more than 75 million individual returns, have issued 65 million refunds, with an average value of refunds of about \$3,000.

Our eFile program continues to grow. This year, so far, our eFile rate is 6.3 percent higher than last year, and last year was 5 percent higher than the year before. We also continue to see people using their home computers and filing continuing to grow. We have received almost 25 million returns from home computers, a 9 percent increase over last year. The reason this is so significant is it is much cheaper for the Federal Government to process an electronically-filed return. It costs about \$.17, as opposed to \$3.66 for a paper return. And people get their refunds much quicker.

We have also seen an increase in self service options. Our web traffic has grown eight percent. Our "Where's My Refund" tool has grown 19 percent. And automated calls answered have increased by about 21 percent.

Regarding our answering phone calls, I am pleased to tell you our level of service, despite a flat budget, remains at 74 percent. And our accuracy remains at 95 percent. And so the phone operation is going well this year.

Let me also note during this filing season we continue to try to adjust core programs to meet evolving needs of taxpayers. And a good example of this is what I call our fresh start program, which is focused on our collection area. We announced that we were expanding our offer in compromise program, making the ability for lien withdrawal easier, making it easier for small businesses to enter an installment plan with us this year, and changing our criteria for filing liens. And you are going to see us continue to evolve our programs as taxpayer needs warrant it.

Let me now turn to the 2012 budget. This budget was crafted during a time of fiscal austerity. For me, that means aggressively pursuing savings where we can find savings, but also investing in strategic priorities that enhance the nation's tax system.

I think the President made clear in the budget that the IRS is vital to the functioning of the government, to keeping our nation strong and our economy strong. Last year, we collected \$2.3 trillion. This translates to every dollar spent on the IRS, about \$200 comes into the Federal Government. I think it is in recognition of the critical role that we play that this 2012 budget makes judicious investments. It also tries to keep the balance between taxpayer service, serving honest Americans, and our enforcement programs, making sure we find people who aren't paying their fair share of taxes.

It also continues our investment in our core account database, which is the cornerstone of our modernization effort. When this is complete in 2012, assuming we get the funding, it is going to mean faster processing of all returns, faster refunds to all Americans, and enhanced data security of our technology systems.

Because of our unique revenue-raising functions, our budget more than pays for itself, and directly contributes to deficit reduction. And I will also note this year's budget, as well as the last several years that I have been here, has significant savings. We have \$190 million of program cuts and savings in the 2012 budget.

Now, I would be remiss in my responsibilities if I didn't make a few comments about H.R. 1. Under the House version of the continuing resolution, the total 2011 funding for the IRS would be \$603 million below the 2010-enacted levels, with potentially devastating effects to the nation's tax system.

If H.R. 1 were to be enacted, the IRS would have to make substantial and immediate cuts to all of its programs, including its enforcement programs. We estimate that this would reduce enforcement revenue this year by \$4 billion. This would increase the deficit by about seven times the magnitude of the proposed reduction in the budget.

In addition, such a conspicuous drop in IRS enforcement activities could have an impact on longer-term voluntary compliance. We would also be forced to dramatically reduce resources to taxpayer services, leading to millions of unanswered phone calls, delayed processing of correspondence, and potentially delayed refunds.

In conclusion, we are in a very challenging environment with difficult choices to make. Despite this year's challenges, the filing season is progressing smoothly. So I look forward to a constructive dialogue today and over the coming weeks and months.

And Mr. Chairman and Ranking Member Lewis, I also just want to very much thank you for the support and constructive dialogue that this committee has had with our agency over the last several years, and continuing this year. That concludes my testimony.

[The prepared statement of Mr. Shulman follows:]

**WRITTEN TESTIMONY  
OF  
DOUGLAS H. SHULMAN  
COMMISSIONER  
INTERNAL REVENUE  
BEFORE  
THE HOUSE WAYS & MEANS  
SUBCOMMITTEE ON OVERSIGHT  
FILING SEASON AND FY 2012 BUDGET REQUEST  
MARCH 31, 2011**

**INTRODUCTION AND SUMMARY**

Chairman Boustany, Ranking Member Lewis and Members of the Subcommittee, thank you for this opportunity to testify on this year's tax filing season and to provide you with a snapshot of our recent successes and an overview of our proposed FY 2012 Budget and what we hope to accomplish with these resources.

***2011 Filing Season***

The 2011 filing season started with difficult challenges for the IRS. As the Subcommittee is aware, substantial tax law changes were enacted in December 2010 that affected tax year 2010 returns. IRS staff worked around the clock over the holidays to make the system changes necessary to open the tax filing season. Although the vast majority of taxpayers could begin filing in January, we had to delay processing of some tax returns for those claiming itemized deductions on Form 1040, Schedule A, as well as deductions for state and local sales tax, higher education tuition and fees and educator expenses. These taxpayers were able to start filing on February 14<sup>th</sup>.

Despite these challenges, there is much of which to be proud this filing season. For example, as of March 19, 2011, the telephone accuracy rates for both customer tax law and account questions stood respectively at 92.2 percent and 95.6 percent.

The IRS E-file program continues to grow. This year the individual E-file rate is trending about 6.3 percentage points higher than last year – a very positive trend.

And in a still challenging economy, it is good news that the average refund is \$2,985 – about the same as last year. This money can help taxpayers pay their bills, make needed purchases and to save. They can purchase up to \$5,000 of Series I U.S. Savings Bonds using their federal tax refund. Taxpayers are increasingly using this option. In this second year of offering these bonds, there has been a 116 percent increase in the number of bonds requested over the same period last year. The dollar amount of the bonds requested has also increased by 13.1 percent.

A more detailed description of the filing season can be found later in the testimony.

*A Record of Success*

Mr. Chairman, the IRS is also proud of its implementation track record over the past few years.

We have run smooth filing seasons for the last several years, despite new tasks being added to our agenda and late passage of legislation.

We have also made good strides in cracking down on international tax evasion. We struck a landmark deal with the government of Switzerland, and for the first time received information on thousands of Americans hiding assets in Swiss bank accounts. As we turned up the pressure on those not paying taxes on overseas assets, we had approximately 15,000 voluntary disclosures from individuals who came in under our special Voluntary Disclosure Program (VDP). Since the special program closed, we received an additional 3,000 voluntary disclosures from individuals with bank accounts from around the world.

Many of these voluntary disclosure cases involve significant amounts of previously unpaid tax.

However, collecting such substantial additional revenue for past misdeeds is not the only important consideration here. Regardless of dollar size, it is important that we are bringing thousands of US taxpayers back into the system so they properly report and pay their taxes for years to come on their offshore accounts.

Last month, the IRS announced a new special voluntary disclosure program designed to help people with undisclosed income from hidden offshore accounts get current with their taxes.

In 2010, the IRS also took a major step towards transparency with Announcement 2010-9 to require business taxpayers to report basic information regarding their uncertain tax positions (UTP) when they filed their tax returns.

This new requirement helps to achieve what most taxpayers and the IRS strive for: certainty, consistent treatment and the efficient use of government and taxpayer resources by focusing on issues and taxpayers that pose the greatest risk of tax noncompliance.

One of the most important initiatives that the IRS has undertaken in recent memory is the return preparer initiative, which is now being implemented. In September 2010, we launched the new online PTIN (Preparer Tax Identification Number) application system. It is up and running with hundreds of thousands of preparers already registered in the system.

More than just an identification number, the PTIN registration process gives the IRS an important and better line of sight into the return preparer community than we have ever

had before. We can leverage that information to help us better communicate, analyze trends, spot anomalies and potentially detect fraud.

The registration process will help us build in several years a publicly-accessible database of preparers who are authorized to prepare returns. This is an extremely important tool for consumers as they will be able to search the database to ensure that their preparer is registered. It will also make it easier to find and track the bad actors out there. They will not be able to pull up stakes and move around anonymously.

The IRS is also very proud of its work in implementing the tax-related provisions of the American Recovery and Reinvestment Act (ARRA) and other economic recovery legislation. We put out billions of dollars to help people buy homes and stabilize the housing market through the First-time Homebuyer Credit, and we added \$400 to \$800 to families' paychecks through the Making Work Pay Credit, just to name two provisions.

The IRS continues to provide taxpayers with quality customer service and different service channels and products. They run the gamut from traditional walk-in sites for those who need to see an IRS representative face-to-face, to toll-free automated and assistor telephone service, to web-based applications and social media. All make it easier for taxpayers to file and pay their taxes.

Finally, the IRS continues to run robust compliance programs. We continue to have appropriate and balanced audit coverage rates across taxpayers and to innovate in our collection programs.

And in our latest effort to help struggling taxpayers, the Internal Revenue Service announced on February 24, 2011 a series of new steps to help people get a fresh start with their tax liabilities.

The goal is to help individuals and small businesses meet their tax obligations, without adding unnecessary burden to taxpayers. Specifically, the IRS set forth new policies and programs to help taxpayers pay back taxes and avoid tax liens.

The announcement centers on the IRS making important changes to its lien filing practices that will lessen the negative impact on taxpayers. The changes include:

- Significantly increasing the dollar threshold when liens are generally issued, resulting in fewer tax liens;
- Making it easier for taxpayers to obtain lien withdrawals after paying a tax bill;
- Withdrawing liens in most cases where a taxpayer enters into a Direct Debit Installment Agreement;
- Creating easier access to Installment Agreements for more struggling small businesses; and
- Expanding a streamlined Offer in Compromise program to cover more taxpayers.

In short, despite a quickly evolving taxpayer base and unprecedented demands on IRS resources, the IRS continues to deliver for the American people.

***Working Smarter and Greater Efficiencies***

The IRS continues to reap the financial benefits of the E-File program, one of the most successful modernization programs in government. Today we receive nearly 100 million tax returns electronically. In the past these returns had to be opened, sorted, and transcribed manually. The efficiency savings have allowed us to reduce our submission processing sites in half. This year we are closing our 5th of the original 10 sites.

The FY 2012 Budget Request includes almost \$190 million in efficiency savings, reductions, and non-recurring activities. While these targets are substantial, I am confident that we will meet them and more, by finding cost-savings in our operations wherever we can.

I have also challenged the IRS leadership and indeed, all IRS employees, to take a hard look at their operations and look for potential savings and efficiencies.

Even in a tough budget environment, I am confident that the IRS will continue to deliver value for the American taxpayer and will emerge as a stronger agency in the years to come.

I am particularly pleased with the progress that we are making in achieving efficiencies in our technology operations. The IRS has embarked on a multi-year effort to streamline and standardize processes that will allow for substantial efficiency gains. For example, the Information Technology Infrastructure Library is a collection of best practices used to aid in the implementation of a lifecycle framework for IT Service Management. In September 2010, an independent third party found that the IRS recently reached Capability Maturity Model (CMM) Level 2 based on established criteria.

Achieving this level allows standardized project management practices across projects. This will improve our agility and quality in delivering software to our business customers and the taxpaying public, as well as reduce the cost of developing and maintaining products, and improve the cost of engineering services.

***FY 2012 Budget Summary***

Mr. Chairman, let me turn to the FY 2012 Budget for the IRS. It was crafted during a time of fiscal austerity and belt tightening for the nation and it is incumbent upon all of us in government to be as efficient as possible and spend taxpayer dollars wisely. That means finding savings where we can, and continuing to invest in strategic priorities that allow us to continuously improve.

Against this backdrop, it is clear that the IRS is vital to the functioning of government and keeping our nation and economy strong. In FY 2010, the IRS collected \$2.345



trillion in gross revenue to fund the federal government, approximately 93 percent of all federal receipts. Moreover, for Calendar Year 2010, we processed nearly 142 million individual income tax returns and issued more than \$366 billion in refunds to taxpayers.

Indeed, it is in recognition of the critical role that the IRS plays in the economy that the FY 2012 Budget includes a judicious investment in the IRS' core service and enforcement programs and initiatives. Enforcement and customer service are not an either/or proposition. Accomplishing our mission requires that we do both well.

The Budget also includes the necessary funding for completing on time the 2012 filing season and the core taxpayer account database. A fully operational customer account database will mean faster processing of returns, expedited refunds for 140 million individual taxpayers and enhanced data security.

The funding in the President's Budget Request will be used to carry out the IRS' strategic and balanced agenda that includes:

- Improved service to taxpayers, including enhancements to the IRS.gov website to meet taxpayer needs and growing demand for more e-services;
- Robust and targeted enforcement programs to address offshore tax evasion and improve tax compliance for corporate and high-income taxpayers;
- Completion of the new taxpayer account database and enhancements to our electronic filing platforms;
- Leveraging the Return Preparer Program to reduce non-compliance;
- Implementation of our Uncertain Tax Position (UTP) reporting requirements;
- Combat errors and fraud for refundable tax credits, such as the Earned Income Tax Credit (EITC);
- Better use of data, such as credit card and securities basis information reporting;
- Implementation of the tax provisions found in major recent legislation, including the Affordable Care Act;
- Workforce development to ensure we have a talented and capable workforce for the foreseeable future; and
- Enhance workplace/physical security for IRS employees.

The IRS will also administer those portions of the American Recovery and Reinvestment Act (ARRA) that were extended into 2011. These include the expanded EITC for families with three or more children, and the American Opportunity tax credit to help pay tuition and other expenses for individuals enrolled in institutions of higher education. In addition, we continue to administer the Health Coverage Tax Credit that was enacted as part of the Trade Adjustment Assistance Reform Act of 2002.

The new enforcement personnel included in the budget will generate more than \$1.3 billion in additional annual enforcement revenue once the new hires reach full potential in FY 2014. The roughly \$6-to-\$1 return on investment (ROI) estimate related to these initiatives does not include the indirect revenue effect of the deterrence value of these investments and other IRS enforcement programs, which is conservatively estimated to be at least three times the direct revenue impact.

As noted in the previous section, the Budget includes almost \$190 million in efficiency savings, reductions and non-recurring activities. While these targets are substantial, I am confident we will meet them and more by finding cost-savings in our operations wherever we can.

## **THE 2011 FILING SEASON & TAXPAYER SERVICE**

Mr. Chairman, although a little more than two weeks remain in the current filing season, it has proceeded smoothly and with few problems, such as the late tax law changes that were quickly identified and remedied.

Providing quality taxpayer service throughout the year, but especially during the filing season, is important if we are to help taxpayers get it right from the start and avoid making unintentional errors. Assisting taxpayers with their questions before they file their returns prevents inadvertent noncompliance and reduces burdensome post-filing notices and other interactions with the IRS.

### ***Submission Processing, Refunds and E-filing***

As of March 19, 2011, the IRS received 75.2 million individual returns. Overall filing is on par with last year although it was down earlier in the filing season, due in large part to the late start of the filing season for some taxpayers due to late tax law changes and inclement weather in many parts of the country.

The IRS E-file program continues to grow. This year the individual E-file rate is trending about 6.3 percentage points higher than last year – a very positive trend. The other side of the coin shows paper returns dropping by 30 percent.

The number of taxpayers e-filing their returns themselves continued to grow this filing season. More than 24.7 million prepared their own e-file return – an almost 9 percent increase over the same time period last year. The overall growth in e-filing translates into a huge savings for the Federal Government.

For FY 2010, it cost only 17 cents to process an e-filed return – a fraction of the \$3.66 it takes to process a paper return. And with e-file, taxpayers get their refund faster, with fewer data processing errors that can lead to problems later in the process.

Indeed, taxpayers filing electronically can get their refunds in less than three weeks upon acknowledgement of receipt by the IRS. Based on the most current Refund Timeliness data, the average time to process a refund for a paper tax return is six weeks upon receipt of the return.

Through March 19, 2011, the IRS issued 64.6 million refunds for a total of \$193 billion, as compared to 63.2 million refunds for a total of \$190 billion over the same time period in 2010. The average dollar refund was \$2,985, about the same as last year. During the same time period, the IRS directly deposited 53.7 million refunds to taxpayers, as compared to 51.3 million last year – a 4.6 percent increase.

Starting last filing season, taxpayers could also purchase up to \$5,000 of Series I U.S. Savings Bonds using their federal tax refund. As of March 19, 2011, there has been a 116 percent increase in the number of bonds requested over the same period last year. The dollar amount of the bonds requested has also increased by 13.1 percent to \$6,169,750.

#### ***Toll-Free Telephone Performance***

High quality toll-free telephone service – both assistor and automated – is an extremely important tool in answering taxpayer questions, helping them navigate an extremely complex tax code and making voluntary compliance easier.

As of March 12, 2011 – the latest data available – IRS telephone assistants answered 9.56 million calls. The IRS also completed 22.2 million automated calls – a 21.6 percent increase over last year's 18.3 million, reflecting a growing taxpayer appetite for quality self-serve options.

Toll-free Assistor Level of Service (an indication of how often taxpayers seeking assistor help can reach such a person) is projected to stand at 73.4 percent through March 19, 2011 compared to last year's 74.4 percent.

Accuracy rates for both customer tax law and account questions remain in the 90-plus percentile with minimal change over last filing season's levels.

#### ***Website Usage and New Media***

IRS.gov continues to be the favorite source of information for millions of taxpayers. As of March 19, 2011, there were over 141 million visits to IRS.gov – an 8 percent increase over the same time period last year. Use of the "Where's My Refund" electronic tracking tool continued to post double-digit yearly gains at 19 percent. IRS.gov/Español offers many of the same services and information in Spanish.

When taxpayers visit the IRS.gov website, they first see a rotating spotlight feature on the front page. The spotlight, which changes every few seconds, highlights important taxpayer and practitioner information, such as Free File, recent tax law changes, and information to help taxpayers in economic distress.

Taxpayers can also use electronic tools, such as the EITC Assistant, to determine if they qualify for the refundable tax credit, or a withholding calculator to help them determine the right amount of tax to withhold from their paychecks. This is especially important given the recent cut in payroll taxes. We also provide new income-tax withholding tables that employers will use during 2011.

The IRS is increasingly communicating with taxpayers who may not get their information from traditional sources, such as newspapers and broadcast and cable news. By employing social and new media, such as YouTube, Twitter and even an iPhone app, we are able to reach these taxpayers with important service and compliance messages. In fact, the three YouTube channels (English, multilingual and ASL) had 667,000 views for the first five months of FY 2011 – a 196 percent increase as compared to the same time frame in FY 2010.

In January 2011, the IRS also unveiled IRS2Go, its first smartphone application that lets taxpayers check on the status of their tax refund and obtain helpful tax information. This new application reflects our commitment to modernizing the IRS and engaging taxpayers where and when they want.

#### *Taxpayer Assistance Centers (TACs)*

The IRS continues to provide in-person service at its 401 TACs. As of March 12, 2011, approximately 1.54 million taxpayers were served – a one percent increase over the previous year. Walk-in service is still popular among elderly taxpayers, those with limited English and computer proficiency, and taxpayers without Internet access. TACs remain a useful filing season resource for taxpayers resolving tax issues and needing help preparing their tax returns.

#### *Open Houses*

Last year, the IRS launched a series of Open House events that gave taxpayers another option to get face-to-face help from the IRS to solve their tax issues. These Saturday events were very successful, serving over 35,000 taxpayers while resolving an overwhelming majority of their concerns the same day.

This year, the IRS will host four more Open Houses to again provide assistance to taxpayers in need of help resolving their federal tax problems. Two were held during the filing season – Saturday, February 26 and Saturday, March 26 – and two will be held after the filing season.

As an added benefit, educational seminars were available at select locations on topics ranging from new tax law for this tax season, to where to go for tax help. Educational brochures were available at all participating Taxpayer Assistance Centers.

Close to 100 Taxpayer Assistance Centers were open for the February and March Open Houses. In addition, Account Management assistance was available through the IRS' toll free lines during each event to provide resolutions to issues and general information about the day's event.

Taxpayers were able to receive the full range of services at each TAC location, including: [free?] tax return preparation if the taxpayer qualified for the EITC or had an income under \$49,000; solutions to tax issues; account inquiries; and answers to tax law, Examination and Appeals questions.

In all, 8,100 taxpayers were served at the February event and 89 percent of cases were resolved the same day.

In addition to IRS help, community organizations partner with the IRS. Volunteer Income Tax Assistance (VITA) programs assist people who earned \$49,000 or less, and Tax Counseling for the Elderly (TCE) programs assist individuals age 60 and over with their 2010 income tax return preparation and electronic filing. Many of these sites have Saturday hours while others offer assistance at various times during the week.

#### ***Limited English Proficiency (LEP)***

Today, the IRS offers language services to LEP taxpayers, thereby affording them the same access to Federal benefits and services as English speakers. We now have more than 2,300 bilingual employees who provide services to LEP taxpayers; a Spanish language web site; and a Multilingual Gateway that provides information in Chinese, Vietnamese, Korean and Russian. A telephone interpreter service is also available in more than 170 languages, and more than 600 tax products have been translated into languages such as Spanish, Chinese, Vietnamese, Russian and Korean.

#### **THE ADMINISTRATION'S FY 2012 BUDGET REQUEST FUNDS KEY PRIORITIES**

The IRS funding level requested for FY 2012 is \$13,283,907,000, which includes \$85,754,000 for maintaining current levels, a decrease of \$22,090,000 from non-recurring activities, a decrease of \$167,867,000 from efficiencies and savings, and a program increase of \$838,836,000 to improve taxpayer service, implement enacted legislation, strengthen enforcement, and continue migration of applications to the new taxpayer account database, CADE 2. By FY 2014, the revenue-producing enforcement investments are projected to increase annual enforcement revenue by more than \$1.3 billion annually.

The Budget Request supports these activities by providing:

- \$114,307,000 to improve taxpayer service and the IRS.gov website;
- \$605,671,000 to implement legislative mandates, handle new information reporting requirements, increase compliance efforts to address offshore tax evasion, focus on corporate and high-wealth returns, increase examination and collection coverage, and enforce tax return preparer compliance; and
- \$118,858,000 to enhance employee security, develop disaster recovery systems capability, and develop the information technology, infrastructure, and systems to implement the various ACA provisions.

#### **BUILDING ON THE FY 2010 ENACTED LEVEL**

The FY 2010 enacted level for the IRS was \$12,146,123,000, supporting an estimated 94,766 FTE.

#### **Maintaining Current Levels**

- ***Adjustment to Reach FY 2011 President's Policy Level +\$401,665,000 / +1,653 FTE*** Adjustment from the FY 2011 Annualized Continuing Resolution Rate to reach the FY 2011 President's Policy Level. The President's Policy Level is equal to the FY 2011 President's Budget Request as adjusted for the proposed pay freeze.
- ***Adjustments Necessary to Maintain Current Levels +\$85,754,000 / 0 FTE*** Funds are requested for inflation adjustments in non-labor expenses such as GSA rent adjustments, postage, supplies and equipment and health benefits and the increase in Federal Employee Retirement System participation. No inflation adjustment is requested for pay in FY 2012.

#### **Base Adjustments**

- ***Technical FTE Adjustments \$0 / +501 FTE*** This adjustment reflects permanent changes made to ensure FTE levels are fully funded in the base budget.

#### **Efficiencies and Savings**

- ***Non-Recur Savings -\$22,090,000 / 0 FTE*** This is the net of reductions of non-recurring, one-time costs associated with the IRS FY 2011 enforcement initiatives (e.g., IT equipment and training).
- ***Increase e-File Savings -\$22,444,000 / -416 FTE*** This decrease is a result of savings from increased electronic filing (e-file). Savings are based on e-file projected growth, modernization, and the completion of the phased implementation of the Worker, Homeowner, and Business Assistance Act of 2009 (Public Law 111-92), which requires all paid tax return preparers who expect to file more than 10 tax returns to file such returns electronically..

- **Reduce IT Infrastructure -\$75,000,000 / 0 FTE** The IRS will reduce the unit costs of infrastructure through use of the Capability Maturity Model (i.e., a process improvement approach that yields efficiencies in software engineering); the Information Technology Infrastructure Library (ITIL) that will allow the IRS to improve the quality of IT services; and the further consolidation of security activities in the Cybersecurity organization to leverage security best practices.
- **Reduce Contracts -\$20,754,000 / 0 FTE** In accordance with Presidential guidance on controlling contracting costs, the IRS will achieve targeted savings through reduced contracting expenses.
- **Reduce Administrative Expenses -\$14,331,000 / -66 FTE** The IRS will reduce administrative expenses, including targeted attrition through hiring freezes.
- **Eliminate Lockbox Fees -\$4,000,000 / 0 FTE** The IRS will eliminate lockbox fees that now will be paid by taxpayers in installment agreements.
- **Reduce Certain Mailings -\$4,000,000 / 0 FTE** The IRS will eliminate printing and mailing of certain forms and publications and reduce the number of inserts in mailings.
- **Reduce Training, Travel and Programs -\$27,338,000 / -41 FTE** The IRS will reduce agency-wide non-technical training, non-case related travel, and the taxpayer communication and education program.

#### **Program Reinvestment**

- **Submission Processing Consolidation (Atlanta) +\$1,486,000 / 0 FTE** Increased use of e-file has led to consolidation of individual return processing sites. A portion of the increased e-File savings will be reinvested to fund the one-time separation costs associated with the September 30, 2011 closure of the Atlanta submission processing site. As the Atlanta consolidation approaches, the IRS will assist employees to find employment either in or outside the organization.

#### **Program Increases**

- **Improve Taxpayer Service +\$81,307,000 / +519 FTE** Funding for this initiative and the \$25.9 million increase from the FY 2011 President's Policy level will provide staffing to address rising demand for services, including a funding increment to deliver an expected 80 percent telephone level of service. This initiative also includes funding to assist taxpayers in understanding new legislative provisions and to make related call center and infrastructure changes to handle anticipated service inquiries, including those related to the ACA.

- ***Expand Online Options through IRS.gov Improvements +\$33,000,000 / +15 FTE*** This initiative will continue the multi-year effort to replace the outdated web portal environment and provide additional online services to taxpayers. The Taxpayer Assistance Blueprint, Phase 2, targeted migration to the electronic channel and services as one of the five areas for improvement of IRS service delivery. IRS will achieve efficiencies by moving high-volume transactions to IRS.gov, improving taxpayer self-service, reducing taxpayer burden, increasing compliance, reducing costs, and improving security. These improvements will position IRS.gov as the preferred delivery channel of choice for taxpayer service.
- ***Increase International Service and Enforcement +\$72,596,000 / +377 FTE*** The IRS will implement reporting, disclosure and withholding requirements and expand coverage of international filings, conduct more in-depth international compliance work, strengthen compliance efforts related to offshore activity and grow the Global High-Wealth compliance group. This initiative will increase examinations of employment tax specialty program audits, individual audits, business audits; and criminal investigation case closures. As part of this overall effort, IRS will also implement changes contained in the Foreign Account Tax Compliance Act (FATCA).
- ***Increase Collection Coverage +\$52,000,000 / +413 FTE*** This initiative will expand work on the collection inventory and improve collection processes to bring taxpayers who fail to pay their tax debt into compliance. This funding will expand the Automated Collection Systems (ACS) program, address the increased workload for the Offers in Compromise (OIC) program due to program improvements and to more taxpayers experiencing economic hardship, and improve efficiency through innovative approaches to inventory selection. The additional staff will resolve an additional 144,300 tax delinquency accounts (TDA) (i.e., balance due accounts where returns were filed, but the taxes have not been paid) and 25,200 tax delinquency investigations (TDI) (i.e., investigations of taxpayers with unfiled returns who have not responded to a notice).
- ***Implement Merchant Card and Basis Reporting +\$35,730,000 / +415 FTE*** This initiative will staff programs to implement information reporting on merchant payment card and third party reimbursements enacted in the Housing and Economic Recovery Act of 2008 (Public Law 110-289) and basis reporting on security sales enacted in the Emergency Economic Stabilization Act of 2008 (Public Law 110-343).
- ***Increase Coverage to Address Tax Law Changes and Other Compliance Issues +\$96,718,000 / +497 FTE*** This initiative addresses compliance issues and new responsibilities arising from recent tax law changes included in major legislation such as ARRA and the ACA. This initiative will fund compliance programs needed for new provisions such as direct-pay bonds, new requirements on tax-exempt hospitals, a new fee on manufacturers and importers of branded prescription drugs, the excise tax on indoor tanning, and will also increase the



number of specialty program (i.e., employment tax, excise tax, and estate and gift tax) audits.

- ***Ensure Accurate Delivery of Tax Credits +\$260,293,000 / +834 FTE*** This initiative recognizes the important role the IRS plays in delivering economic incentives through tax credits by improving the delivery of existing credits through a combination of improved technology tools and increased enforcement staffing. The initiative largely funds the information technology and other systems required to implement the new ACA premium assistance tax credit, which becomes effective in 2014. IRS must build new systems to support eligibility determination based on household income, and modify existing tax processing systems to support reconciliation of advance payments of the credit. The initiative also funds the appropriate compliance resources for the small employer tax credit that came into effect in 2010.
- ***Administer New Statutory Reporting Requirements +\$58,505,000 / +187 FTE*** Recent legislation establishes significant new information reporting and sharing requirements from third parties (such as employers, health insurance providers), and the Health Insurance Exchanges (the “Exchanges”) to administer the premium assistance tax credit, the individual coverage requirement, and the employer responsibility payment. Effective implementation will require significant enhancements to existing information returns systems to handle the additional volumes and new information reporting categories. The ACA also includes provisions that allow the IRS to share tax data with state and federal entities for the purpose of determining eligibility for the advance premium credit. This request also includes resources to ensure secure exchange of information and provides the initial staffing to establish the program to handle the additional inventory of non-filer assessments expected because of the expanded 2012 information reporting requirement for businesses to report all aggregate purchases of services or property greater than \$600.
- ***Leverage Return Preparer Program to Reduce Noncompliance +\$16,600,000 / +108 FTE*** The IRS is increasing tax return preparer oversight to ensure that tax return preparers are competent and to help ensure that the IRS collects the right amount of taxes. This initiative will ensure uniform and high ethical standards of conduct for tax return preparers by enforcing preparer compliance with IRS rules, increasing preparer examinations, and pursuing preparers engaged in fraudulent activities. This initiative is key to the IRS’s tax gap strategy and will increase government revenue.
- ***Address Appeals Workload Growth +\$9,100,000 / +66 FTE*** This initiative will allow the IRS to increase Appeals staffing. Despite improvements in cycle time and increased efficiency in working cases, Appeals continues to experience rising inventories, and because of the nature of Appeals work, the cases must be processed manually. The funding in this initiative will reduce, but not eliminate,

the stress put on the appeals process because of increased caseload. In addition, Appeals settlements generate increased revenues for the federal government.

- ***Implement Uncertain Tax Position Reporting Requirements +\$4,129,000 / +20 FTE*** This initiative will allow the IRS to provide guidance and certainty on UTPs and meet increasing taxpayer demands for this service. This increased workload is expected as a result of changes IRS has proposed for certain large business taxpayers to report information about their uncertain tax positions. It is a critical part of IRS's work to gain greater transparency into large corporate tax returns.
- ***Enhance Security and Disaster Recovery Systems Capability +\$12,000,000 / +5 FTE*** This initiative is part of a multi-year improvement strategy to support the continued deployment of critical disaster recovery capabilities. It supports two critical business processes: Processing Remittances and Processing Tax Returns by reducing the recovery time dramatically for the critical applications supporting these processes.
- ***Update Integrated Financial System (IFS) +\$27,500,000 / +5 FTE*** This initiative provides funds to complete the first phase of an initiative to update IFS. This request will ensure IRS compliance with future federal accounting requirements and allow implementation of standard interfaces and communication with other federal systems. The IRS current financial system is more than ten years old and SAP software no longer provides updates or changes to accommodate new legislative or other federal accounting requirements. Without a system that will allow implementation of new federal accounting requirements, IRS compliance with federal financial management standards could be jeopardized.
- ***Leveraging Data to Improve Compliance +\$1,400,000 / +5 FTE*** The IRS is focused on using a data-driven approach to continually innovate and improve its programs. This investment will capitalize on the significant increase in data reported to the IRS, with the goal of using research to find ways to improve tax administration and/or increase compliance. Funding will increase compliance through leveraging such data and/or evaluating the effectiveness of tax-related programs.
- ***Enhance Physical Security for Federal Employees +\$15,481,000 / +10 FTE*** The February 2010 attack against the IRS in Austin, Texas killed one IRS employee and injured several others. This initiative will provide investments needed to update and/or upgrade the physical security of IRS facilities. The investments will enhance the overall security of IRS employees in the workplace, while maintaining open access for the taxpayers that they serve.
- ***Implement Individual Coverage Requirement and Employer Responsibility Payments +\$62,477,000 / +65 FTE*** This initiative will fund the development of the information technology, infrastructure, and systems to implement the ACA

provision that establishes shared responsibility payments for both individuals and employers. Beginning in 2014, the ACA requires individuals who are able to afford health insurance to obtain minimum essential coverage or pay a penalty, and large employers – those with 50 or more full-time employees – to make a shared responsibility payment if they do not provide affordable coverage to their employees, and at least one of their employees benefits from the premium assistance tax credit.

#### ENFORCEMENT PROGRAM

The FY 2012 President's Budget Request is \$5,966,619,000 in direct appropriations and an estimated \$75,902,000 from reimbursable programs for a total operating level of \$6,042,521,000. The total direct appropriations level includes an additional appropriation for tax enforcement and compliance activities, by which funding is requested through a program integrity allocation adjustment totaling \$1,257,000,000, of which \$936,000,000 will be funded from the Enforcement account. The proposed allocation adjustment would increase the Financial Services Committee's 302(b) level by the amount of the allocation adjustment. Congress used such an allocation adjustment mechanism to fund IRS enforcement initiatives in both FY 2009 and FY 2010 and the Administration proposed an adjustment of \$1,115,000,000 for FY 2011. This appropriation funds the following budget activities:

- **Investigations (\$678,849,000 from direct appropriations and an estimated \$66,567,000 from reimbursable programs)** This budget activity funds the criminal investigations programs that uncover criminal violations of the internal revenue tax laws and other financial crimes; enforces criminal statutes relating to these violations; and recommends prosecution as warranted. These programs identify and document the movement of both legal and illegal sources of income to identify and document cases of suspected intent to defraud. It provides resources for international investigations involving U.S. citizens residing abroad, non-resident aliens and expatriates and includes investigation and prosecution of tax and money-laundering violations associated with narcotics organizations.
- **Exam and Collections (\$5,103,420,000 from direct appropriations and an estimated \$8,761,000 from reimbursable programs)** This budget activity funds programs that enforce the tax laws and increase compliance through examination and collection programs that ensure proper payment and tax reporting. It also includes programs such as specialty program examinations (employment tax, excise tax and estate and gift exams), international collections and international examinations. The budget activity also supports appeals and litigation activities associated with exam and collection.
- **Regulatory (\$184,350,000 from direct appropriations and an estimated \$574,000 from reimbursable programs)** This budget activity funds the development and printing of published IRS guidance materials; interpretation of tax laws; advice on general legal servicing, ruling and agreements; enforcement of

regulatory rules, laws, and approved business practices; and supporting taxpayers in the areas of pre-filing agreements, determination letters, and advance pricing agreements. The Return Preparer Strategy initiative is funded within this activity in addition to the Office of Professional Responsibility which is responsible for identifying, communicating, and enforcing the Treasury Circular 230 standards of competence, integrity, and conduct of professionals representing taxpayers before the IRS.

#### **TAXPAYER SERVICE**

The FY 2012 President's Budget Request is \$2,345,133,000 in direct appropriations, an estimated \$22,924,000 from reimbursable programs, and an estimated \$130,962,000 from user fees, for a total operating level of \$2,499,019,000. This appropriation funds the following budget activities:

- **Pre-Filing Taxpayer Assistance and Education (\$701,035,000 from direct appropriations and an estimated \$863,000 from reimbursable programs)**  
This budget activity funds services to assist with tax return preparation, including tax law interpretation, publication, production, and advocate services. In addition, funding for these programs continues to emphasize taxpayer education, outreach, increased volunteer support time and locations, and enhancing pre-filing taxpayer support through electronic media.
- **Filing and Account Services (\$1,644,098,000 from direct appropriations, an estimated \$22,061,000 from reimbursable programs, and an estimated \$130,962,000 from user fees)** This budget activity funds programs that provide filing and account services to taxpayers, process paper and electronically-submitted tax returns, issue refunds, and maintain taxpayer accounts. The IRS continues to make progress in decreasing paper returns and increasing the use of electronic filing and payment methods.

#### **BUSINESS SYSTEMS MODERNIZATION**

The FY 2012 President's Budget Request is \$333,600,000 in direct appropriations. This appropriation funds the following budget activity:

- **Business Systems Modernization (\$333,600,000 from direct appropriations)**  
This budget activity funds the planning and capital asset acquisition of information technology (IT) to continue the modernization of IT systems, including labor and related contractual costs. The completion of the core database is the cornerstone of modernization and is a prerequisite to developing the next generation of IRS service and enforcement initiatives. The integration strategy includes a particular focus on enhanced information technology security practices and robust accounting and financial management controls. This activity also funds the ongoing development of the Modernized e-File platform for filing tax returns electronically.

### OPERATIONS SUPPORT

The FY 2012 President's Budget Request is \$4,620,526,000 in direct appropriations, an estimated \$39,446,000 from reimbursable programs, and an estimated \$73,466,000 from user fees, for a total operating level of \$4,733,438,000. The total direct appropriations level includes an additional appropriation for tax enforcement and compliance activities by which funding is requested through a program integrity allocation adjustment totaling \$1,257,000,000, of which \$312,000,000 will be funded from the Operations Support Account. The proposed allocation adjustment would increase the Financial Services Committee's 302(b) level by the amount of the allocation adjustment. Congress used such an allocation adjustment mechanism to fund IRS enforcement initiatives in both FY 2009 and FY 2010 and the Administration proposed an adjustment of \$1,115,000,000 for FY 2011. This appropriation funds the following budget activities:

- **Infrastructure (\$986,045,000 from direct appropriations, an estimated \$516,000 from reimbursable programs, and an estimated \$22,095,000 from user fees)** This budget activity funds administrative services related to space and housing, rent and space alterations, building services, maintenance, guard services, and non-IT equipment.
- **Shared Services and Support (\$1,313,050,000 from direct appropriations and an estimated \$20,577,000 from reimbursable programs)** This budget activity funds policy management, IRS-wide support for research, strategic planning, communications and liaison, finance, human resources, and equal employment opportunity and diversity services and programs. It also funds printing and postage, business systems planning, security, corporate training, legal services, procurement, and specific employee benefits programs.
- **Information Services (\$2,321,431,000 from direct appropriations, an estimated \$18,353,000 from reimbursable programs, and an estimated \$51,371,000 from user fees)** This budget activity funds staffing, equipment, and related costs to manage, maintain and operate the information systems critical to the support of tax administration programs. This includes the design and operation of security controls and disaster recovery planning. This budget activity also funds the development and maintenance of the millions of lines of programming code that support all aspects and phases of tax processing and the operation and administration of the mainframes, servers, personal computers, networks, and a variety of management information systems.

### Health Coverage Tax Credit (HCTC) Administration

The FY 2012 President's Budget request is \$18,029,000 in direct appropriations. This appropriation funds the following budget activity:

- **HTCA (\$18,029,000 from direct appropriations)** This budget activity funds costs to administer a refundable tax credit for health insurance to qualified individuals, which was enacted as part of the Trade Adjustment Assistance Reform Act of 2002.

### **AFFORDABLE CARE ACT**

The IRS will need to implement and administer the tax provisions of the Affordable Care Act (ACA) (Public Law 111-148) in 2012. IRS seeks to be helpful to families and businesses that will benefit from the ACA. In fact, some benefits have already begun. For example, upon enactment of the ACA, the IRS immediately began to make sure that small employers were aware of a significant new tax credit to help them provide health coverage to their workers.

Because the tax credit was enacted mid-year, and was effective immediately, the IRS conducted a significant outreach campaign to small businesses. In addition to mailing postcards to millions of employers alerting them to the new credit, the IRS held or attended more than 1,000 outreach events targeted at small businesses, and the tax practitioners who serve them.

Working with the Department of Health and Human Services, we also administered a program to provide \$1 billion in tax credits and grants to qualifying therapeutic discovery projects.

In addition, we have implemented or have begun to implement changes that expanded the tax credit for adoptive parents, a new exclusion for loan forgiveness programs for certain health professionals, and a new excise tax on indoor tanning services.

We are also working diligently to implement the tax law components of the changes made to the health insurance marketplace that will begin in 2014. Let me put these efforts in context by describing the activities that we are undertaking to plan for these upcoming changes.

The IRS also has significant information technology development work that must be completed in order to administer these provisions. The vast majority of the resources that IRS will require between now and 2014 will be dedicated to technology and the associated business process design required to effectively administer these new provisions.

### ***Exchanges and Medicaid Health Coverage***

Individuals seeking subsidized coverage will interact with the IRS at a few discrete points in the process:

1. Obtaining coverage through exchanges and/or Medicaid

The ACA outlines eligibility rules for the premium assistance tax credit, as well as Medicaid. In both cases, the household income as reported to the IRS by approximately 140 million taxpayers on the 2012 tax returns will be relevant to eligibility determination. The IRS will alter its systems to take account of the new concept of household income, and is planning to provide significant educational tools to help individuals understand what household income represents. Furthermore, planning is underway to determine the best way to provide this information to taxpayers via the Web, telephone, and other channels.

2. Receiving advance premium tax credits

Individuals who are determined to be eligible for the premium assistance tax credit can receive the benefit through advance monthly payments that are made directly to the plan provider. Working with the Treasury Financial Management Service, which will be making the advanced payments, the IRS will develop new systems for the administration of the tax credit. In addition, the IRS will work with the exchanges as appropriate to insure there is significant outreach and education to make taxpayers who are receiving the advance payments aware of the importance of reporting mid-year changes in circumstance that could affect their eligibility for, or the amount of the credit.

3. Reconciling the premium assistance tax credit with advance payments made through the year

The ACA provides that individuals will reconcile the amount of advance payments of the premium credit with the actual amount as computed on the tax return. In other words, advance payments made throughout 2014 will be reconciled with individuals' tax returns that are filed in the spring of 2015. To the extent that the ultimate credit amount is larger than the sum of the advance payments, the additional amount will be added to the taxpayer's refund. If the ultimate credit amount is lower than the sum of the advance credit, the taxpayer will owe additional tax on the return. The amount owed may be capped, subject to the schedule outlined in the Medicare and Medicaid Extenders Act of 2010.

***Individual Coverage Requirement***

The IRS will also be responsible for administering the requirement that individuals who can afford health coverage either obtain it, or make a payment to the IRS. While implementation of this requirement does not come into effect until 2014, and will appear on the 2014 tax forms that will be filed in the spring of 2015, we have nonetheless received a number of questions about how this provision will be implemented.

First, we anticipate providing significant outreach and education on this provision. This will come directly from IRS and in partnership with state and federal agencies,

employers, tax return preparers, and others. Our experience in administering new tax laws suggests that the vast majority of individuals will successfully incorporate this provision into their tax year 2014 returns, filed in 2015.

The forms will provide instructions on how individuals can determine if they met the coverage requirement, and if not, how to compute the payment and include it in that year's tax liability. We also plan to work closely with the tax return preparation industry to ensure that the professionals who advise taxpayers are fully informed about this provision. Today, approximately 60 percent of taxpayers use a return preparer; another 25 percent use software to prepare their own returns.

#### ***Employer Provisions***

Finally, the IRS will administer the employer responsibility payment for large employers who do not offer affordable coverage, and have at least one employee who receives subsidized coverage through the exchange. This provision closely intersects with the rest of the exchange provisions, and we are working closely with the Department of Health and Human Services and the Department of Labor to reach out to the employer community; understand what questions and issues they foresee; and incorporate the feedback that we get into the upfront program design and regulatory guidance.

#### ***Tax Law Changes***

The IRS is also working diligently to implement other tax law changes that come into effect over the next several years. Earlier in my testimony, I mentioned several that we are already implementing, and would be happy to answer any questions that you have on those, or the provisions coming into effect in the months and years ahead.

#### **CONCLUSION**

In conclusion, let me thank the subcommittee again for this opportunity to discuss the 2011 filing season and IRS Budget Request for FY 2012. Both reflect the progress and improvements the IRS continues to make – even in a difficult budget environment.

I believe the FY 2012 Budget is fiscally prudent and makes wise investments in strategic priorities in enforcement, service, and business modernization. It will help ensure that the IRS will continue its vital role in keeping our nation and economy healthy and strong.

---

Chairman BOUSTANY. Thank you, Commissioner. I mentioned to you before the hearing I appreciated your written testimony and some of the breakdowns that you gave us. And the information was very, very helpful.



As I mentioned in my opening statement, too often we all forget the enormous price in both time and dollars that the individual taxpayer has to pay to comply with the tax filing requirement. And, of course, Americans spend a vast amount of time and resources every year to file their tax returns. The Tax Code clearly is growing in complexity, and this shifts enormous cost to the taxpayer, but also makes honest compliance more difficult. The complexities have added significant burdens to the IRS.

And just a simple question. Is it your opinion that the Tax Code is too complex?

Mr. SHULMAN. Yes.

Chairman BOUSTANY. We are going to be going through tax reform, and this is certainly going to take time. It is going to be a deliberative process. And so, I think as we go through that process, clearly with a mind on how to simplify things for the taxpayer, we also need to keep in mind the burdens that it places on your agency as well. And I would just like to hear you expound a little more on that aspect of the complexity.

Mr. SHULMAN. Sure. So my short answer, yes, is what I believe. The Tax Code is incredibly complex, and unfortunately has been going in the wrong direction over the last decade.

As I mentioned in my remarks, the vast majority of my employees' time and resources is spent trying to serve the American people and help them wade through tax complexity, and get their refunds quickly. We have a pretty unique view into what it feels like to be a taxpayer, wrestling with the Tax Code. We would be happy to engage in whatever dialogue people would like, just about simplicity.

We also can see where there is either honest mistakes made, and—because of the complexity, a lot of non-compliance is honest mistakes by taxpayers, just getting tripped up with the code. We also see where we have issues in areas of controversy. A lot of places where we have controversy is where there is complexity, because there is vagaries in the law we then need to, with the Treasury Department, promulgate guidance.

And so, anything you can do to simplify the code certainly helps our agency, because we spend a lot of time answering questions, providing service, correcting mistakes, and then having enforcement actions around the complex areas of the law. My belief is it would certainly help taxpayers.

Chairman BOUSTANY. And I think you bring an important perspective to this, because I know in our conversations in the past, you have started businesses, you came from the business world and had to deal with the Tax Code from the perspective of a business owner. And now, your position heading the agency, the Internal Revenue Service.

And I think you told me in the past that you get assistance when you file. Is that true?

Mr. SHULMAN. I traditionally have, yes.

Chairman BOUSTANY. Yes. And so, when the IRS commissioner himself is requiring, you know, professional assistance to deal with the Tax Code, I think that is a statement in and of itself, as many of us who serve in Congress probably also—I know I get profes-

sional help with mine. So, again, it is just an indicator of the complexity of the code.

The new health care law, of course, it is no news that it has added enormous new duties and responsibilities. I mentioned an indoor tanning tax, new Medicare Part D rebates, new taxes on drug makers, insurance subsidies, employer penalties, and of course, the individual mandate.

The 2012 budget proposal request, nearly half-a-billion dollars in new funding, and I think we've seen the figure of 1,200 new employees to implement the law for next year. And much of this in the law isn't implemented until later in the decade. So I think CBO estimates that the 10-year cost for the IRS is going to be somewhere in the \$5 billion to \$10 billion range. And do you agree with that, as a result of the Affordable Care Act? Is that—

Mr. SHULMAN. Yes.

Chairman BOUSTANY. Do you agree with—

Mr. SHULMAN. I think the CBO estimates are—

Chairman BOUSTANY. Okay.

Mr. SHULMAN [continuing]. In the general direction.

Chairman BOUSTANY. Yes. And for 2012 do you have any indication—I think we have seen mention of tens of millions of dollars for infrastructure related to the Affordable Care Act, and I guess, related staff. Do you have a sense of what kind of staffing request or build-out you will need for the 2012 budget?

Mr. SHULMAN. Yes, the 2012 budget submitted is the 1,200 people. Just a few comments about that. I want to make very clear that the IRS's role in the Affordable Care Act is to implement the Tax Code provisions in the act, the movement of money. It is really HHS's responsibility to be involved in the health policy issues.

The vast majority of our request—82 percent—is really around technology and infrastructure to build systems to match household incomes—because right now we have AGI by individuals and couples—and build the interfaces with insurance companies and the state exchanges to administer the refundable credit portion of that. That is the vast majority of the request.

Chairman BOUSTANY. That is the big part. Have you—do you have an estimate of how many full-time employees you're going to need to bring in for the implementation in 2012?

Mr. SHULMAN. So 2012 is the 1,200.

Chairman BOUSTANY. That is the 1,200.

Mr. SHULMAN. Yes.

Chairman BOUSTANY. Okay. For clarification. Okay, thank you. I now yield time to the ranking member.

Mr. LEWIS. Thank you, Mr. Chairman. Mr. Commissioner, again I want to thank you for being here, and I want to thank you for your years of service.

I noticed that you have a number of open houses this filing season. I would like to know who attended these open houses, and what problems are they facing?

Mr. SHULMAN. About two years ago, as we continued to innovate around service—and two years ago we were still deep in the nation's worst recession—I really sat down with my senior team and said, what can we do to help taxpayers? How can we go the extra mile to help resolve issues?

Last year we actually held 1,000 open houses around the country. And they were Saturdays, trying to create another service option so working people who had the weekend off could do this. It was mainly targeted at individual taxpayers, as well as small businesses, who had an outstanding issue with the IRS and wanted to resolve it.

A lot of people, if they get behind on their tax, don't understand they can come in, and get on an installment plan. If they really can't pay and their circumstances have changed, we can put them in currently not collectible status and leave them alone for a year. And we can also compromise their debt, if there is no prospect of paying.

So, we—and what we did is we made these available, and we had everyone from revenue agents, customer service reps, appeals officers who could settle, so everyone was there that they could settle their issues.

This year we are repeating it, based on lessons of last year. I think the main issues—and I can get back to you with a specific breakdown—is we're trying to target people who have an outstanding debt, or are wrapped up with us in some way, either need to get on an installment plan, need to pay, want to get a lien released, or have simple tax law questions.

We will service anyone from across the board, but we are really trying to focus on people who got caught up in the economic downturn, whose circumstances have changed. We can answer questions and really resolve any situations, once and for all.

Mr. LEWIS. Has the agency been a little more liberal during these difficult economic times with taxpayers?

Mr. SHULMAN. The way I would describe it is we always have the ability to be reasonable with folks, and compromise the debt, et cetera. I encourage anyone on the subcommittee to come visit IRS facilities. If you walk around, despite the popular image of the IRS in people's head, if you walk around and meet any of our employees, they say "I am serving the American people."

Again, a year-and-a-half ago we did the open houses. I also announced expedited lien release for people who are refinancing houses. As I mentioned, this year we increased from \$25,000 of tax debt, where a small business could automatically get on an installment plan without any questions asked to \$50,000 this year. We basically said we won't file a lien with someone if they create direct deposits with us this year. People who felt that their credit scores were being hurt because a lien wasn't withdrawn after they paid their debt, but rather was released, we made it so they can automatically get it withdrawn.

And so, absolutely I think my answer is in these tough economic times I have pushed the agency hard, and the agency has responded very well, to get creative, to try to make sure we help out taxpayers where we can, while also trying to make sure those who can afford to pay, pay their tax bill.

Mr. LEWIS. Mr. Commissioner, are those that claim the earned income tax credit more likely to be audited than the general population?

Mr. SHULMAN. Yes, they are. With any large refundable tax credit there is always the temptation for fraud. It is also a very

complex credit, as I was discussing with the chairman. And so I think there is a whole set of honest mistakes that happen in claiming that.

We basically have a two percent audit rate of earned income tax credit. We have a one percent audit rate for the rest of the individual taxpayer population. And about 36 percent of our audits last year were targeted at the earned income tax credit.

What we try to do with that program, like any of our programs, is have balance. We do a lot of outreach and education—we've done it with a lot of Members of Congress—to make sure people who are eligible take advantage of the credit. And then we have very rigorous enforcement programs to make sure people who aren't eligible—we try to stop them from getting the credit.

Mr. LEWIS. Thank you, Mr. Commissioner. Thank you, Mr. Chairman.

Chairman BOUSTANY. I thank the ranking member. The chair now recognizes Mr. Gerlach for five minutes.

Mr. GERLACH. Thank you, Mr. Chairman. Thank you, Commissioner, for being here.

Can I follow up on just some of that last commentary you made on auditing? Does—the auditing work that the IRS does, does that fall under the enforcement part of your budget request, for this year, \$5.9 billion that you're requesting for "enforcement?" Would auditing of individuals and businesses fall under that category?

Mr. SHULMAN. Yes, it would.

Mr. GERLACH. Okay. And did I hear you correctly just a moment ago that, on average, you audit individuals—about one percent of the individuals that file with the IRS per year?

Mr. SHULMAN. That has been a traditional rate, spread out across all individuals. It varies by income category, it varies by, as I said, earned income tax credits, a particular interest of ours.

Mr. GERLACH. And what percent of business filers do you audit per year?

Mr. SHULMAN. It depends on the level of income, and also, the volume of filers that come in. Some quick statistics, businesses that have assets below 10 million last year, it was about .94 percent. So just under one—

Mr. GERLACH. Just under one?

Mr. SHULMAN. Just under one percent. And then it goes up. Businesses that have over \$250 million of assets have about a 23 percent audit coverage rate. And then the largest corporations in the country generally have auditors on site and have lots of ongoing interactions with us.

Mr. GERLACH. So are the audits—for the business audit, are they kicked off based upon random selection, or based upon red flags that come up from the prior filings, or the periodic filings? What kicks in an audit for particularly a small business owner?

Mr. SHULMAN. Yes. Our audit criteria is based on a number of factors. We have been, as an agency—and I have been very focused on—risk-based audits as the most important to us. So it can be—we have certain geographic coverage. We have certain risk factors and parameters around data that comes in on returns.

And we also have certain areas—certain businesses which are more risky, from a compliance standpoint. Cash businesses, obviously, have different compliance issues than other—

Mr. GERLACH. And what is the average length of an audit? How much time does your auditor spend in that business?

And how do you juxtapose that against the amount of time, therefore, the business has to participate and cooperate with those auditors, in terms of the time they are then taking their employees away from their business duties to them comply with the audit requests that the auditors are making?

What is the ratio of time you are spending in the businesses auditing them, and what is the amount of time they are putting in to cooperate and participate and try to satisfy the auditor's request?

Mr. SHULMAN. I can get back to you with that. I don't have the ratio off the top of my head.

Mr. GERLACH. Okay. But I guess what I am getting at is what is the loss of productivity and profitability of these businesses that are taking time to comply with your request, and have you ever calculated what the impact of the auditing process is on profitability and productivity of the businesses that you are involved in?

Mr. SHULMAN. Yes, we look at burden and calculate burden quite a bit. And let me just share with you my approach, and my philosophy—

Mr. GERLACH. Yes, yes.

Mr. SHULMAN [continuing]. About this. We try to do is do our job of making sure there is compliance with the law, do a lot of outreach and education—we've got extensive programs around small businesses, and making sure we help them comply with the law—and try to do our job in the least burdensome manner possible. Obviously, nobody likes to have an audit.

Mr. GERLACH. Yes.

Mr. SHULMAN. And it's going to take some time when someone does an audit.

We have tried to move more and more, as I mentioned, to targeting our audits to places where there is potential non-compliance, and leaving taxpayers who have traditionally been compliant alone. We have also tried to get better and better at using data, so that when data comes in, we analyze the data, and when we go in we spend less time.

Mr. GERLACH. What—of those that are audited on the business side—and I would be interested on the individual side, as well—but on the business side, staying with that, how many are found to be in non-compliance, or to have violated the code, based upon that audit?

What percentage of those in the total auditing—audited group there, how many do you find have violated the law and need to either pay penalties or interest or a combination?

Mr. SHULMAN. We measure something called the no-change rate, which is what percentage of people do we audit, and there has been no adjustment made. I will get you the numbers. One of the measures is—are we doing risk-based audits appropriately? If we are auditing and there is not much of a no-change rate, then it means we might be picking the wrong folks.

If—the no-change rates have been moving up, that means our analytical group has gotten better at risk-based audits. But we've got to be real careful.

Mr. GERLACH. Is it 50 percent of those businesses audited?

Mr. SHULMAN. Yes—it is more than 50 percent.

Mr. GERLACH. Are in violation in some way, shape, or form—

Mr. SHULMAN. Yes, have a change in the audit.

Mr. GERLACH. Okay.

Mr. SHULMAN. But just one comment I want to make is I am always very cognizant—and there is a whole bunch of things in the law about how we measure our performance. While we want to go in places that have higher non-compliance in the enforcement arena, I also don't want to set perverse incentives for my people to make changes where they won't happen. We are always trying to get that balance right and have that dialogue.

Mr. GERLACH. Thank you. Appreciate it.

Mr. SHULMAN. Thank you.

Chairman BOUSTANY. I thank the gentleman. Mr. Becerra, you are recognized for five minutes.

Mr. BECERRA. Thank you, Mr. Chairman, and thank you for holding this hearing. Commissioner, great to see you again. Thank you for the work you are doing.

By the way, thank you for the work that you have done in trying to get agents who try to put out their services as preparers of tax returns for the American public, having them become registered agents, so that we have a way to track their record of service.

Because too often I know I have had people come to my office saying, "I got swindled by a guy who said he's going to prepare my taxes, did a terrible job, now I'm being audited, I had to pay a big amount of money, causing big headaches," so thank you very much for helping us go down the road of making the realm of tax preparers a professional service.

And I know my own tax preparer has said to me, "Great work that the IRS did in trying to help the rest of the guys out there do what many of us have done for years, and that is provide a professional service that we are willing to have audited at any time."

So thank you for that. I know you are saving the American public a great deal of money, and probably increasing their tax refunds, because they are calculating them correctly.

You mentioned something very troubling. The budget bill that was passed by this House, H.R. 1, by the Republican majority a few weeks back, would cut \$600 million out of your budget, which you said would cost us in revenues, because of lower tax collections—proper and legitimate tax collections—some \$4 billion. So, by almost a factor of seven, we would be increasing the size of the deficit by instituting a cut that would not allow you to go out and do your collection services appropriately. And it might also undermine the voluntary system that we have for tax payment by American taxpayers.

Does that mean that you would actually have to reduce the number of personnel that are actually working to help process forms? What actually goes into this \$600 million cut that makes it difficult for the U.S. Treasury to collect the money that is owed to it, and therefore, makes other taxpayers have to pay more, because they

will have to make up for the \$4 billion lost by those who owe the money?

Mr. SHULMAN. First of all, I am hopeful—at least from my proprietary perspective, as the IRS Commissioner—that we don't have those cuts. And I know that all Members of Congress and the administration are now working to try to get a budget deal done.

The cuts would be just big, big cuts that would have to be jammed into a six-month window. We would have to have across-the-board cuts. We would either have to have long furloughs or RIFs, and we would be taking people basically away from every function. So we would be taking people away from collection, we would take them away from exam, we would take them away from automatic screening. We would be taking them from customer service, we would be taking them from outreach. We would be taking them out of our technology operation.

My responsibility—as, obviously, Congress's responsibility to give us whatever budget, my responsibility is to tell you what would happen. This would be our estimate, \$4 billion less revenue, phone calls not answered, returns backed up and not processed.

Mr. BECERRA. Yes. And so there was no direction in the budget bill that cuts the \$600 million as to how you could do it in a way that would not undermine services. And I don't hear you saying that you could find a way to institute those cuts that wouldn't undermine services.

Mr. SHULMAN. Well, if you look at the allocations, across our enforcement, our service, our operations budget, all the things I laid out would happen. The biggest cut is to enforcement.

Mr. BECERRA. I also want to make sure I emphasize again something else you said, because there is a need to dispel this rumor, this myth floating out there, that the money that IRS needs to try to implement this new patient's bill of rights is somehow all focused on getting IRS agents to bang on people's doors, when my understanding is the bulk of the money, the vast majority of the money, is really used to provide assistance, taxpayer assistance services, or to beef up mostly our IT, our intellectual—our Internet technology, so that we can help process a lot of these claims.

I was looking at the budget that you outlined for the use of the money. Am I correct that 60 percent of the \$470 million that you requested to implement the new patients bill of rights would go towards computer system upgrades, and those things that you need to just implement the bill, getting 30 million Americans now with good health insurance, and that of the 40 percent that remains, that would be used for personnel, two-thirds of that would be used for taxpayer services in other ways to provide a service, not necessarily to go out there and do enforcement?

So, I guess that totals to about 85 percent of the money being used for services, and for better systems operations.

Mr. SHULMAN. Let me make sure I give you accurate numbers. So let me give you the way I—

Mr. BECERRA. Thank you.

Mr. SHULMAN [continuing]. Look at it, which is about 82 percent, or \$390 million of the request, is to support the refundable credit operation. Clearly, the biggest lift for us is the infrastructure around having technology that gets income data smoothly into and

out of, in real time, the 50 exchanges that will be built around the country in the 50 different states.

When people get a refundable credit, we actually send money on a monthly basis to the insurance company that people send that money—so we need to have reconciliation systems with them, feeding it back into the states in a real-time basis.

Only about 11 percent, or \$50 million of the budget, is for enforcement. And so, everybody likes to talk about IRS agents. We have lots of people who are phone operators, technology folks. We're much more boring than the popular image of the agent, in lots of our operations. I think of us as a large financial service operation. We are more—but we are very akin to that. We do a lot of money flows, \$2.3 trillion. And so that is where most of it goes.

The enforcement money in the 2012 budget is largely for traditional tax enforcement, compliance programs around the taxes that are going into effect—that are in effect now, and are going into effect over the next year or two.

Mr. BECERRA. Thank you. Thank you, Mr. Chairman. I appreciate it.

Chairman BOUSTANY. I thank the gentleman. The chair now recognizes Ms. Jenkins for five minutes.

Ms. JENKINS. Thank you, Mr. Chairman. Thank you, Commissioner, for being here.

As the House and Senate continue budget talks in an effort to prevent a government shutdown, it is important that we understand whether the IRS is prepared to handle a government shutdown. So I am just curious. In the event of a shutdown, what is the IRS's plan to process tax returns and issue tax refunds?

Mr. SHULMAN. First of all, I will tell you everybody is hopeful that there will not be a shutdown. We run a \$13 billion financial services operation, and the idea of stopping it for a few days or a few weeks is strange to someone like me who has run big operations. I think the President has been very clear that it is not in anybody's interest to have a government shutdown. My understanding is there is very productive talks going on at this point.

What I will tell you is we had an old plan that looked at government shutdowns based on October 1, when the fiscal year begins. We have never had a government shutdown in the middle of the filing season before. The closer we get to April 15th, the more consideration and factors are at play.

As these dates, I think we are on our sixth CR, have pushed out, we have had to adjust plans going forward. I will tell you right now we are in discussions with OMB and the Administration of exactly what would happen. And so I cannot tell you. Our old plan was we deposited checks, we didn't process returns. That was a plan that was built in 1995, when there was not so much electronic filing. And now we are closely looking at it, and are having discussions.

Ms. JENKINS. Okay, thank you. In your testimony here you mentioned that the average refund is nearly \$3,000. And you say this money can help taxpayers pay their bills, make needed purchases, and to save.

But we all know that this refund money isn't just plucked off the money tree in the back of the Capitol. This is money—this is the taxpayer's money, and it could have been used the whole year for



them to invest, or to make purchases. And I think, instead, they are giving the government, basically, an interest-free loan.

So, I am just, again, curious. Do you see this high level of refund as a deliberate action of taxpayers, or as a result of maybe a Tax Code that is overly complex?

Mr. SHULMAN. I think each taxpayer is different—I think a lot of taxpayers actually use the withholding system to have automated savings so that they can then get a refund. People like to do it.

In my ideal world as a taxpayer, I actually withhold the exact right amount, and I neither pay nor get a refund. That is my own personal goal. It is very hard to hit, because of the complexity of the code and estimating exactly, you know, all the factors that will come in.

And so, it is a fact that we usually put out, you know, \$250 billion to \$300 billion of refunds. Retail sales—the Commerce Department, over time, has looked at this—retail sales usually increase in February through May, as a direct result of refunds. I always encourage people to withhold correctly.

And so, we see it as just a fact of the tax system, neither good nor bad, just a fact, that we give you and you can make your own judgements about.

Ms. JENKINS. But if it was a more simplified calculation, do you think people would deliberately be lending the government interest-free money during the year?

Mr. SHULMAN. I won't speculate on it. I mean I think a lot of it is not—there is the complexity of the code, but there is also the issue of people don't know always exactly what they will make, what their spouse will make, what interest income they might get, how their jobs will change, if they are going to get a second job. So I think there is a bunch of factors.

Ms. JENKINS. Okay. Thank you. I yield back.

Chairman BOUSTANY. The chair now recognizes Mr. Buchanan for five minutes.

Mr. BUCHANAN. Thank you, Mr. Chairman, and I appreciate the Commissioner being here. You met with us a couple of weeks ago, and so I don't know how you get much work done—you are here. But we are excited to see you back.

Let me just touch on a couple of things. And it is along the line of tax simplification. I look at—in our area I was chairman of a Chamber. We had about 2,500 businesses. Most of them are—a lot of these businesses are 3 to 10 employees. There are some that are larger, larger companies, banks, and some other things. But I would say out of the 2,600 probably 2,200 are 20 employees or less. What are you doing to help simplify their ability to file and, you know, quarterly things that they have got to file?

Because I do hear it just takes so much time and effort from these small businesses. You know, a lot of them do not have a controller or a CPA, or they are a CPA but they have got an accountant that is outside. What is the IRS doing to make it simpler for them?

Mr. SHULMAN. As you know, we implement the tax laws that are written. And as you know, I had the conversation with the

chairman earlier about simpler laws would clearly be helpful. But it is not our role.

What we try to do is, given the laws that are on the books, do as much outreach education service as we can. I would be surprised if one of our people wasn't at the Chamber of Commerce on a regular basis in your district, holding education events, explaining tax law changes, being available to businesses.

We spend a lot of time with the practitioner community. For individuals, 66 percent of people use a tax professional. For businesses, including small businesses, it is 80 percent. So if we can get good information and tools to the practitioner community, they can make sure that people file it well.

And we answer millions of calls from small businesses every year. Our phone operators spend a lot of time doing that. We have a dedicated website. We have a dedicated outreach and education unit for small businesses. We have an e-newsletter on tax issues for small businesses that has a distribution of about 200,000. And so we do everything we can, given our resources, given the code—

Mr. BUCHANAN. And secondly, because we have just got five minutes, what about independent contractors? We have a lot of Realtors, everybody else, you know, maybe it is themselves, their husband, but basically there is a lot of people out there—they might be with Amway or whatever they are with, as independent contractors. Is there anything we are doing to—and their situation is probably even more difficult, because they are just themselves, and—is there anything that we are doing to help them and simplify things for them, as well?

Mr. SHULMAN. Again, we have all of the avenues of service. They usually afford themselves of the individual services. We answered 35 million calls last year. We keep having more self-service options on our website, and we will continue to do that. And we are trying just to get the right balance of—you know, with the service resources we have.

My personal view is the vast majority of our service resources should be going to individuals and small businesses who cannot afford themselves of the professional tax community help and are struggling to make ends meet.

Mr. BUCHANAN. And, Commissioner, my colleague mentioned about dispute, when you have a dispute with the IRS. Let us say medium-sized companies or a little larger companies, what is the process—are the negotiators on the IRS side, are they empowered—because you hear these things a lot of time just drag on and on and on. Very expensive, and not only in terms of outside professionals, but very expensive in terms of the internal time it takes an organization—I am not talking about the person that has got 5 employees, someone that has got, in our area, for example, 400, 400 or 500. They have a dispute, it just seems like it drags on forever.

And I guess the question is, you know, what is the process on your side to resolve these things, or have someone in that is bright enough, sharp enough—not that they are all not—but is—are they empowered to get something done and get these things wrapped up and get a compromise or—what is your attitude, or how does it work on your side?

Mr. SHULMAN. I have been very public. I mean if you look at things I have been talking about for the last three years, my real goal with the business taxpayer is to resolve issues and get certainty sooner for the IRS and for taxpayers. We have a whole slew of programs, and I have been pushing them very hard.

Part of it is getting clearer guidance, creating safe harbor, where we can simplify the rules. We have an appeals function. So if you disagree with us, we close out an audit, you can go to our appeals function—

Mr. BUCHANAN. Well, before the appeals, is the auditor itself, the person, can they—do they have a boss that they can go through and try to negotiate it out before it goes to the appeal?

Mr. SHULMAN. Oh, absolutely. But what I was going to tell you is we have expanded what we call fast-track appeals, where we can just go in and audit, invite an appeals officer in to negotiate a settlement.

Our folks have the ability to work through issues. We do have time lines where you have got to get in, you have got to get out with folks.

Mr. BUCHANAN. Yes.

Mr. SHULMAN. Now, some taxpayers complain about the time lines.

Mr. BUCHANAN. Yes.

Mr. SHULMAN. Because they say someone is in, and they are just trying to get issues and get out—

Mr. BUCHANAN. The big thing I hear is just getting it done fast-track. I am glad to hear you have got something like that, because they just don't want things to drag on for a year, they would rather just get the people in the room and try to work something out and move forward, because it costs a lot of money, time, and aggravation over, you know, a period of time.

Mr. SHULMAN. Yes, absolutely.

Mr. BUCHANAN. Okay. Thank you. I yield back.

Chairman BOUSTANY. I thank the gentleman. The chair now recognizes Dr. McDermott for questioning.

Mr. MCDERMOTT. Thank you, Commissioner. I have been listening to this testimony today, and I am not real sure why we are having this hearing. But I heard the chairman mention the Affordable Care Act and the additional responsibilities you will have in auditing people's behavior with respect to purchase of health insurance.

And I understand that this afternoon, later today, we are going to mark up a bill that would prevent any money from being spent in an insurance policy on abortions. And I suspect that the audit responsibility will fall to you to determine whether or not any money has been spent on abortions, or is planned by the insurance companies—it sounds like an insurance function that is going to wind up in your hands.

And I would be surprised if you have already started to think about this, because you don't start to think until we do something, but it is coming down the road. And I have some questions I would like you to think about, and give me a response if you can, in terms of how many additional people you are going to have to hire to look

at all the insurance plans, to be sure that no money is being spent on abortions.

One of the issues that I think ought to be considered in that is also the HSA. If I put my money in an HSA, can I take it out and spend it any way I want on health care costs? And how do you audit that to be sure that I am not taking advantage of the Tax Code to put money in there and then wind up paying for an abortion for whomever?

It seems to me we are adding things. We continually look at the IRS as kind of our unofficial enforcer, and that you wind up with the responsibility for doing that. And I would appreciate if you could give me an answer in writing as to what you think the effect will be, if the bill passes today preventing the use of any health care money for abortion, I would like to see from you an estimate of what it means to the bureaucracy to have to go around and look and be sure that nobody is taking advantage of the Tax Code.

You have any information about that at all at the moment? I mean how many people you are going to have to have in this system to do this?

Mr. SHULMAN. I don't.

Mr. MCDERMOTT. And do you have an estimate of what you are spending already, or you will spend to audit the system, under the Affordable Care Act?

Mr. SHULMAN. On the bill you referred to regarding our involvement, lots of bills are around until bills are passed.

Mr. MCDERMOTT. Right.

Mr. SHULMAN [continuing]. We will look at that, and any question you send me I will be happy to respond to.

Regarding the Affordable Care Act, we laid out in excruciating detail in our 2012 budget what we will need in 2012. And as I mentioned before, the vast majority of that money is technology infrastructure service money to interface with the exchanges, interface with insurance companies to move the money with the refundable credits.

Mr. MCDERMOTT. And do you have—how are you going to enforce the fact that people have or have not complied with the law, the individual mandate?

Mr. SHULMAN. Oh, the individual responsibility payment? We requested some money for that in 2012. All of that money is technology and infrastructure money just around systems. It will basically be document-matching, just like a W-2.

So, the insurance company will either send us fact or coverage, saying "This person is covered," or not. If they say they are not, generally people will voluntarily comply, our systems will match that, and they will say, "I wasn't covered, and here is the payment." If they don't say that, and we see it, we will send them a bill. And the Affordable Care Act was very clear about having some of our enforcement tools, such as a lien or a levy not being available for that.

So, think of it like a credit card bill that you either choose to pay or not pay. If you don't pay, you will get a bill.

Mr. MCDERMOTT. And—but you have no enforcement capacity.

Mr. SHULMAN. Some will call that enforcement capacity, getting a letter from the IRS. It's like a credit card bill, but it will have our letterhead on it.

I believe what you were talking about before in here is that first of all, we are just going to have fact of coverage information. We are not going to know about your coverage, we are not going to know about your personal health issues.

And second of all, this is not the kind of thing that agents spend time on, these dollar amounts. And so you don't have agents rooting around asking these things. You have document-matching, and bills that get sent out.

Mr. MCDERMOTT. So people could get around the bill?

Mr. SHULMAN. What is that?

Mr. MCDERMOTT. People could get around the bill, since no agent is going to ever look into their health care records. You are not going to put agents at work looking into people's health care.

Mr. SHULMAN. Most of our enforcement activity is not based on face-to-face agents. And most people comply voluntarily with the tax laws. Lots of people, when they get in correspondence with us, pay up and feel that is enforcement.

So, I would not characterize it that we anticipate large numbers of people getting around it. But there is always non-compliance, and there is some non-compliance we don't find.

Mr. MCDERMOTT. Thank you.

Chairman BOUSTANY. I thank the gentleman. The chair now recognizes Ms. Black for questioning.

Mrs. BLACK. Thank you, Mr. Chairman. And as I talked to you the other day, Commissioner, you asked me if I had some concerns, and I talked a little bit about people making phone calls, and maybe getting different answers as they called in, one time to the other.

But I want to turn to a piece that I have read in the information that was provided us about telephone assistance for taxpayers, and that it continues to be a problem.

The percentage of callers that successfully obtain the live assistance over the phone is down from 74.2 percent down to 72.6 percent this year. And the average wait times have also increased from 9.9 to 10.3 minutes. And so far, this year, 10.3 percent of the calls were abandoned, and .8 percent reached a busy signal or ended in a disconnection, probably out of frustration. But both numbers are increases from prior years.

And the IRS's goal, as we understand it, is to answer only 71 percent of the calls in this current year, and then 80 percent in 2012, which is down from the goal that was set back in 2007, of answering 82 percent. So the goal has been decreased. And I know that you have requested an additional \$30 million. So my question is, what do you intend on doing with those \$30 million and, with the goal being decreased, just how does that fit? Why a decreased goal?

Mr. SHULMAN. Thanks for the question. Answering the nation's taxpayers' telephone calls is a big deal to us, and something we take seriously.

Let me be very clear about what the level of service is. The level of service, which I checked this morning and is running at about

74 percent this year, is a formula that takes into account people who hang up, as well as the people that get through to a live assister. It does not translate into 26 percent of people unhappy.

We added last year, a call waiting feature. It used to be you just waited. And now it says, "Your wait will be 10 minutes," if it is going to be 10 minutes. If people who hang up after they hear that, because they do not want to wait, and decide to call back later, if you add that, it adds about 10 percentage points. So you are actually up closer to 84 percent.

The reality is, from where I sit and my folks who are stretching and trying to hit 74 percent, it is a pretty straightforward formula. How many people do you have sitting on the phones, answering the phones, being accurate with your questions?

Most of this will be extra seasonal people during filing season. And I am actually pretty proud the agency is maintaining the level of last year, given that we are under a CR and do not know what kind of cuts are coming forward. And so we are trying to balance the money we have against the level of service.

Mrs. BLACK. And my time is running out here, so—I do have a second part of the question.

Mr. SHULMAN. Sure.

Mrs. BLACK. But to that I would say that I hope maybe we use some technology as well, maybe as you say, to give them more information about it will be a 10-minute wait time or whatever, not just personnel, but also looking at other technology that can be used.

But I want to turn the attention to a program called the Historic Preservation Facade Easement Program. And I know that Chairman Jo Ann Emerson was concerned about this, and brought this situation up in Appropriations. And it has come to my attention by someone else back at home, in particular.

And then, also the IRS advisory council in the 2009 general report took issue with what is going on with the audits. And I wondered if you might, in my one-minute time that I have left, speak a little bit about the program and the fact that even the advisory committee recommends that there may be a safe harbor on the audit policy, because of it appearing to be so onerous. And if you could speak to that, I would appreciate it.

Mr. SHULMAN. Sure. I would love you to come to our call centers and see. We have spent a lot of time on technology and productivity. Part of the reason we can still hit 74 percent is because we have squeezed a lot of productivity out of not adding workers this year.

On easements, historic easements is an issue. You get a big tax credit. We need to have some coverage, make sure people don't abuse it, but also make sure that there is historic preservation, and people use those easements.

We take very seriously the IRSAC recommendations. Those people spent a lot of time. And we are looking right now at those recommendations. I cannot speak specifically to the program here, but would be happy to follow up with you on it.

Mrs. BLACK. Well, I appreciate that, because there was a recommendation, and I would like to know what you think about the recommendation, if you all will follow through on that. Thank you.

Mr. SHULMAN. Thank you.

Chairman BOUSTANY. The chair now recognizes Mr. Kind for questioning.

Mr. KIND. Thank you, Mr. Chairman, for holding this hearing. Mr. Commissioner, thank you for being here, and for the service that you provide.

I missed your opening testimony, so I apologize for asking, but do you have an update in regards to the paid preparer regs that you are coming forward with?

Mr. SHULMAN. Yes. We have started registering. We have over 700,000 paid preparers registered this year, which just means they get their name in and they have a number. We are now in the process of working through the testing and continuing education component, which will be next.

I have been very clear that I think this is important for the tax system, to have a minimum level of competence with paid preparers. But we also want to do it in a staged way, so there is no disruption of service to taxpayers.

And so, we registered this year, we are working on the programs for testing, and then we are going to give people several years to pass the test to get in. So it is going to take several years to get up and running.

Mr. KIND. Okay. And what is the response rate, as far as eFiling right now? What percentage are filing?

Mr. SHULMAN. Last year, we were about 70 percent. We are running about five percent higher than that this year. And so it looks to be going in a positive direction.

Mr. KIND. Okay. You know, and any update on the debit card refund program and how well that is working?

Mr. SHULMAN. No updates at this point of the program that the Treasury Department is running.

Mr. KIND. Okay. Let me ask you, we have the, under the Affordable Care Act, tax credits going to small businesses, 35 percent last year, this year we will continue to 2014, when it goes up to 50 percent. Are you encountering any difficulty with small businesses applying for those tax credits under the Affordable Care Act?

Mr. SHULMAN. Most business returns come in in the fall. So we will see what is coming. It is a very targeted group that is eligible. As you know, 10 employees going to 25 employees with a phase-out. And so I think, you would not yet encounter people who are eligible having issues. We have heard from people who wish they were eligible but who fall outside those ranges.

Mr. KIND. Yes, but you are not encountering any degree of difficulty, as far as people determining their eligibility, or being able to figure out whether to apply for the tax credit or not?

Mr. SHULMAN. We have tried to, do outreach, make sure we are available. We know the practitioner community is very, very focused on that, as well.

Mr. KIND. Yes. I checked the website, IRS website, as far as how you are explaining this to the small business community out there, and you also offer some small examples of small businesses, but not a calculator, itself. Is that purposeful, that you are avoiding kind of a plug-in calculator from the IRS website to see if small businesses would be eligible or not?

Mr. SHULMAN. I don't think we were avoiding it. Calculators are good for some things and not for others. Our folks who work on it probably decided it wasn't going to be that helpful for this.

Mr. KIND. Okay. Notification of small businesses. The IRS sent out postcards to small—

Mr. SHULMAN. Yes.

Mr. KIND [continuing]. About possible notification. What about e-notices to small businesses?

Mr. SHULMAN. Yes. We have an e-business newsletter for small businesses, and there has been information about it there. I mean we—

Mr. KIND. Are most small businesses filing electronically these days?

Mr. SHULMAN. Most are.

Mr. KIND. Okay. So—I'm just thinking of the efficiency, and maybe cost savings. Does it make more sense just to notify them through e-notices, as opposed to formal postcards being mailed out?

Mr. SHULMAN. We have tried different methods of communication. We always do that. Most of our methods are electronic, but sometimes we send out postcards to folks, sometimes we don't. It is all based on the population, how we can reach them, what information we have in the database. With our e-business newsletter—not every small business signs up with the IRS, but we actually had a database of potential eligible taxpayers that had addresses. So that is why we sent them.

Mr. KIND. Now I share Representative Becerra's concern that many people have already raised in regards to what the \$600 million in cuts to the IRS would mean, as far as the collection of revenue and the lost revenue that we would miss out on.

But could you today give the committee kind of an update on what type of cost savings measures that you are going through in the IRS—in light of the budget deficits that we are facing, some of the efficiencies that you are trying to encourage?

Mr. SHULMAN. Yes. Absolutely. I am a big believer—and folks know this even before everybody was talking about the deficit. The day I showed up I told our team that I view a job of any big business or big operation is stop programs that no longer make sense, make cuts where you can make cuts, and then invest in the future. And that is—the set of budgets that I put forward to try to do that.

Our 2011 budget—not the 2012—had about \$180 million of cuts. As electronic filing has grown, we have actually reduced service centers and people processing returns. We have taken our technology up to a standardization level that we are extracting \$75 million each year out of our core technology budget. We have standardized on certain technology platforms, made it easier. We have consolidated data centers. And then we have actually just made some cuts in programs. We have cut some outreach programs. We have actually cut some mailing of materials, and we are going to keep doing that, going forward.

I will tell you, given the current fiscal environment, I have also put a hiring freeze in place. Exceptions to come to me to approve, and we are still investing in strategic priorities. We have dramatically cut our travel budget, except for case-related travel this year.



And we have been in the process of putting in contingency plans, so that if there are dramatic cuts, that we could implement them.

I think our employees actually understand. The way I have explained it to them—when I go out in town halls around the country—is we need to find cuts now. We are going to have to make hard decisions. If our budget is cut severely, I would rather have us find the cuts, rather than RIF people. Because in the Federal Government when you RIF everyone thinks you are just finding efficiencies. It is a pretty blunt tool, and it is based on seniority, and who got added last, and people kick down. What I would rather do is find programs that, at least in the hierarchy of priorities, we feel we should make cuts.

Mr. KIND. Great. Thank you. Thank you, Mr. Chairman.

Chairman BOUSTANY. I thank the gentleman. Thank you, Commissioner Shulman, for appearing before the subcommittee. And we appreciate your testimony and your frank answers to all these questions.

Please be advised that Members may have some additional questions that they will submit in writing. And those questions and answers would be part of this hearing record.

Also, Commissioner, no doubt you have heard the news reports about the report that Chairman Herger, Congressman Reichert, and I released yesterday regarding the AARP's structure and function. And early next week we will be sending that report to you to request further examination of the tax-exempt status of the AARP. But I wanted to officially let you know that we will be sending that report to you.

Mr. BECERRA. Mr. Chairman, in regards to that, could I ask is the committee going to inquire of other of these not-for-profit 501(c)(3) or 501(c)(4)'s?

Because as we have served on this subcommittee in the past, that has been one issue I have raised quite often, with regard to the non-profit, charitable world, is are they, in fact, providing a service, a public good, that pays for the loss of revenue that we give to those non-profits through tax-deductible contributions, through the non-tax status that they carry.

And so, I would be interested to know, does the chairman expect that this subcommittee will do further examination of other organizations, not just senior organizations, I know there are a number of new senior organizations that have been out there doing quite a bit of political work, and I would be interested in making sure that we examine the non-profit world all together. But certainly if we are going to look at, in this case, the AARP, other senior groups, as well.

Chairman BOUSTANY. I share the gentleman's concerns. I think they are very legitimate. And as we look at tax reform in that context, we will be having those discussions. And the specific report referenced as a result of questions that were asked by Congressman Reichert and Ginny Brown-Waite, and the report released was a culmination of 18 months of work done to seek answers to those questions.

So, at this time we are focused on that particular issue. But I think, in the context of tax reform, those—your question is certainly an important one, and will be discussed.

Mr. BECERRA. I thank the chairman for that response. If I could just indulge and ask one last question, the issue, as I see it, is not about a particular organization, or about the activities of an organization. To me it is we have a code that says that you can apply to be treated differently from a for-profit entity, which has to pay taxes. And if you are going to get to forgo having to pay those taxes that an otherwise established enterprise has to pay, we should make sure that the public is getting some benefit for it.

Because there are a lot of businesses that want to do the same type of thing and get the same type of break. You know, essentially these not-for-profits get to operate for a far-less cost, because they don't have to pay taxes. And there are a lot of folks who are out there engaging in an enterprise and paying taxes because they have registered as a corporation or some type of business.

And I think it is important for us to make sure that if you are going to try to tell the public that they should not have to pay the same level of taxes that a for-profit enterprise pays, that it should be for a good reason.

And I think the Commissioner would be a great witness to have, along with the folks from his operations, to try to help guide us in making sure that these operations that otherwise would be taxable as for-profit entities are operating as they should, as organizations that legitimately deserve that non-profit status.

Chairman BOUSTANY. Very important questions, and certainly know we have a current body of law that needs to be followed with regard to whether an organization qualifies as tax-exempt or not.

And clearly, the IRS is the agency, the entity that is best positioned to make that determination, to enforce the law.

And so, that is why we are returning this—we are going to send this specific report over. And then we will have further discussions in the context of tax reform. I thank the gentleman. His concerns are legitimate.

With that, the committee stands adjourned. Thank you, Commissioner.

[Whereupon, at 11:13 a.m., the subcommittee was adjourned.]

[Questions for the Record follow:]

**House Ways and Means Oversight Subcommittee on the 2011 Filing  
Season and  
FY 2012 Budget Request  
March 31, 2011**

**Questions for the Record**

**Chairman Charles Boustany**

- 1. During your testimony you explained that a majority of small businesses e-file. However, the Electronic Tax Administration Advisory Committee noted that businesses e-filing are the lowest of all e-filing classes. Could you please clarify the e-filing rates among small businesses for the last three years? What has your agency done to improve the rate of e-filing among businesses?**

**Response:**

E-File % Rates for Business-related Returns				
Form Type	CY 2011 (4/3/11)	CY 2010	CY 2009	CY 2008
1120	32.0%	23.9%	18.7%	13.2%
1120-S	54.3	37.3	30.0	20.9
7004	49.2	35.0	28.1	20.7
1065/1065-B	56.0	36.4	28.3	20.4

(Form 1120, corporate return; Form 1120-S, S corporations, Form 7004, business extension to file; 1065/1065-B partnership returns.)

First, it is important to distinguish between tax returns filed by businesses, and tax returns which include business income. By far the largest numbers of returns that include business income are individual income tax returns filed by self-employed individuals. These returns are included in the overall E-File rate for individuals, which is near 75% for 2011.

With respect to business tax returns – which are lower volume – the IRS has significantly enhanced its E-File technology in recent years, through our Modernized E-File platform. As of 2007, companies that have assets of \$10 million and that file 250 returns (including information returns) must e-file. Both the IRS Oversight Board and the Electronic Tax Administration Advisory Committee have recommended a renewed emphasis on business e-file, and we agree. One area under particular review is the Form 941/Form 944. There are 30 million employment tax forms filed annually, placing these forms second in volume behind individual income tax returns. The IRS is continuing to consult

with ETAAC, and more recommendations are pending. While I am pleased with our progress to date, I believe we still have a long way to go.

**2. According to your written testimony, Taxpayer Assistance Centers are an important source for taxpayers seeking in-person assistance with their tax returns and are especially popular among elderly taxpayers. However, a recent Treasury Inspector General for Tax Administration study found that the placement of Taxpayer Assistance Centers has not kept pace with population shifts and, as a result, a large percentage of the U.S. population does not live anywhere near one of these centers. Besides IRS sponsored Saturday open houses, where taxpayers receive tax filing assistance from IRS volunteers, what is your agency doing to improve taxpayer access to in-person taxpayer assistance? Is the IRS going to partner with U.S. Post Office locations, as the Inspector General suggested?**

**Response:**

IRS has undertaken many successful actions to expand the availability of face-to-face IRS assistance.

In fiscal year 2009, IRS employees worked at nine geographically dispersed Volunteer Income Tax Assistance (VITA) sites, and assisted taxpayers with account and other issues as a supplement to the free tax return preparation assistance provided by our VITA partners and volunteers. We selected these sites to provide additional IRS services because they were located in areas where population shifts were occurring. During FY 2010, IRS employees worked at 27 VITA sites and assisted over 5,300 taxpayers. The IRS is currently staffing 31 VITA sites during the 2011 Filing Season.

As you mention, IRS sponsors Saturday Open Houses. The Open Houses are staffed by IRS employees from various functions within the IRS, including face-to-face assistors and employees from the Collection and Examination functions. The IRS also holds taxpayer outreach events on various Saturdays to inform taxpayers of the Earned Income Tax Credit (EITC) and to provide assistance to taxpayers in determining their eligibility for the EITC. These Saturday activities provide additional service hours beyond the normal 5-day week. In Fiscal Year 2010, IRS conducted seven Saturday events (EITC events and Open Houses) at nearly 200 locations across the country, with at least one location in each state, serving over 45,804 taxpayers. IRS has conducted four Saturday service events so far during the 2011 Filing Season and will conduct two additional Saturday events after the 2011 Filing Season closes. The IRS assisted almost 32,000 taxpayers during the four 2011 events that have been held to date.

In addition to the Saturday events, during the 2010 Filing Season, the IRS provided expanded service hours on weekdays (before 8:30 a.m. and after

4:30 p.m.) and on Saturdays at 16 of our largest and busiest Taxpayer Assistance Centers (TACs) across the country. This expanded service assisted 6,272 taxpayers through the week of April 15, 2010. Based on the success of our 2010 expanded service hours program, during the 2011 Filing Season, we offered expanded hours of service at 36 TACs, including TACs in populous areas and our busiest locations, to serve additional taxpayers. IRS accomplished this effort by staggering tours of duty of existing staff.

Finally, IRS had Facilitated Self Assistance (FSA) kiosks, which provide a form of virtual interaction between the IRS and taxpayers, at 49 TACs during the 2010 Filing Season. The FSA kiosks allow taxpayers to access a number of useful automated services through [irs.gov](http://irs.gov). Approximately 9,700 customers used FSA kiosks during the 2010 Filing Season. The IRS replaced the FSA kiosks used in the 2010 Filing Season with new, more user-friendly FSA kiosks in 37 TACs in February and March of 2011. This upgrade increased our capacity to serve taxpayers in some of our busiest TACs. Nearly 16,000 taxpayers used the kiosks this fiscal year through April 9, 2011.

IRS will consider collaborating with the U.S. Postal Service after the 2011 Filing Season.

- 3. Last week, your agency issued new guidance requiring employers to report the value of employer sponsored health coverage on employee W-2 wage statements. This reporting requirement was added by the Affordable Care Act. Since the information will not affect an employee's tax liability, what is the IRS doing to make sure employees do not include these amounts in income? Is there anything your agency can do to reduce these burdens on employers?**

**Response:**

The IRS has taken action to educate employees and to ensure employees do not report the value of employer sponsored health coverage in income. Every news release and piece of published guidance has stressed prominently that the amounts reported on the W-2 under this provision are not taxable. On Form W-2, the "Notice to Employee" section discusses the cost of employer-sponsored health coverage and specifically states in bold type that this amount is not taxable. Additionally, the "Instructions for Employee" section provides a listing of codes that may appear in Box 12 of Form W-2. The description of Code DD states that this amount is the cost of employer-sponsored health coverage and notes in bold type that the amount reported as Code DD is not taxable. When an employee reads either section, the employee should immediately see the bold type informing the employee that these amounts are not taxable.

The IRS has taken significant steps to reduce the reporting burden on employers. In 2010, the IRS published Notice 2010-69, which provided reporting relief for

Forms W-2 issued for 2011 (generally provided to employees in January 2012). This notice had the effect of making reporting of this information optional for 2011. This allowed employers additional time to make necessary changes to payroll systems or procedures. The IRS more recently issued Notice 2011-28, which provides guidance for W-2s issued for 2012 (generally provided to employees in January 2013), and beyond. This guidance had the effect of making the reporting requirement optional for employers filing fewer than 250 Forms W-2 at least through 2012, and until further guidance on this issue. The notice also provided the answers to a number of frequently asked questions posed by the employer community.

The IRS also requested comments on how future guidance could further reduce the reporting burden while still providing useful information to employees on the cost of their health care coverage. Also, the IRS requested comments on any challenges employers may face in implementing the reporting requirements for the 2012 Forms W-2, and how further guidance could address those challenges.

- 4. In your oral testimony you noted that your agency is working on additional guidance with regard to competency exams that are required of practitioners pursuant to the new paid tax return preparer regulations. Given that competency examinations are slated to begin in June of this year, when can return preparers expect more information regarding the administration of competency examinations?**

**Response:**

We recognized up front that development and rollout of tests for paid tax return preparers would be a critically important endeavor. This is one of several reasons that we are phasing in this requirement over a three-year period. We are making good progress on establishing the infrastructure required for nationwide testing. Additionally, we intend to seek public input on the structure and content of the test. We will continue to communicate frequently with the tax return preparer community with plenty of notice so they can incorporate these new requirements without undue disruption to their business. Our current target is to open the testing process in the fall of 2011.

---

**House Ways and Means Oversight Subcommittee on the 2011 Filing  
Season and  
FY 2012 Budget Request  
March 31, 2011**

**Questions for the Record**

**Rep. Diane Black**

1. My colleague, Chairwoman Jo Ann Emerson, raised the issue of the IRS's administration of the Historic Preservation Facade Easements when you testified before the Appropriations Committee on March 1. I am concerned to hear from our constituents who have been mired in this audit process, and am particularly troubled that even the IRS Advisory Council has raised concerns regarding these audits. According to the IRS Advisory Council's 2009 General Report, this aggressive auditing is straining the agency's resources even while it fails to distinguish between legitimate deductions and abusive tax shelters. Given these concerns, what does the IRS plan to do to improve the efficient and fair administration of this program? What steps does the IRS intend to take to ensure that the intent of Congress to support historic preservation is not frustrated by unjustified regulatory, enforcement and legal actions by the IRS?

**Response:**

In administering the tax law provisions related to easements, the IRS strives to run a balanced program that facilitates the delivery of these important economic incentives, while ensuring that only those taxpayers legitimately entitled to the benefits are allowed them.

Verifying compliance with the requirements outlined in the tax law is complex, and extremely fact-intensive. As with any provision in the tax law that is dependent on valuation, it is also frequently subject to controversy between the government and the taxpayer.

Faced with these complex issues, the IRS has adapted and modified our programs over time, as the issues and environment around us change. We are also open to input from external stakeholders, such as our Advisory Council.

Among other enhancements to the program that we have made in recent years, we have stepped up our technical training efforts to ensure that our staff has the most up to date information in this area. And, we've increased our use of outside experts, as funding allows, making independent valuation recommendations.

2. In 2009, The IRS Advisory Council recommended a safe-harbor audit policy and the creation of an expert easement advisory board as measures that the IRS should take to curb these issues. However, it is my understanding that the IRS has not adopted any of the IRS Advisory Council recommendations. What, if anything, has the IRS done to implement these recommendations? I am aware that IRS believes it does not have the authority under existing law to implement the IRS Advisory Council recommendations. On what basis has the Agency reached this conclusion and what can Congress do to help the IRS implement these recommendations?

**Response:**

The Internal Revenue Service Advisory Council (IRSAC) provides valuable external perspective on tax policies and programs administered by the IRS. The dialog between the IRSAC and the IRS is robust, and covers a number of significant and sometimes controversial issues. In many cases the IRS accepts IRSAC recommendations, and in other cases the IRS does not agree with those recommendations.


With respect to the recommendations that you reference, the IRS did not accept them for both policy and practical reasons that we would be happy to discuss further. In addition to the limitation of authority under current law that you raised, the IRS believes that the benefits that would come from reduced taxpayer burden would be overwhelmed by the non-compliance (whether intentional or not) that would result if the recommendations were adopted.



3. I understand that the National Taxpayer Advocate may be looking at the issue of the Service's administration of the historic preservation easement statutes. There has been a significant drop-off in donation applications over the last few years, while the amount of resources both the IRS and donors expend to resolve these legal disputes have become substantial. In response, can the IRS temporarily suspend enforcement actions related to this program, until Congress considers the Taxpayer Advocate's recommendations for the proper implementation of the program?

**Response:**

The IRS is responsible for administering the tax law as enacted by Congress. Should Congress change the statute, the IRS would also change the manner in which it administers the law to reflect the provisions of the statute as changed.



**House Ways and Means Oversight Subcommittee on the 2011 Filing  
Season and  
FY 2012 Budget Request  
March 31, 2011**

**Questions for the Record**

**Rep. Jim Gerlach**

**What is the ratio of time you are spending in the businesses auditing them, and what is the amount of time they are putting in to cooperate and participate and try to satisfy the auditor's request?**

**Response:**

The average amount of time spent on business examinations varies by the type and size of the business. For example, while the average time spent for the audit of a small corporation with less than 10 million dollars in assets is 38 hours, the average time spent on the audit of a large corporation is 385 hours. Average time spent for the audit of a sole proprietorship is nine hours.

Preliminary studies indicate that the number of hours spent by the taxpayer in responding to a field examination is typically comparable to the number of hours spent by the examiner. Less complicated issues are covered by correspondence examinations. In general, these examinations may take more time for the taxpayer than the examiner, but overall they take less time for both the taxpayer and the examiner. We are currently conducting a study to update and extend our knowledge of taxpayer post-filing costs that will further inform our understanding of the relationships between IRS enforcement activities and taxpayer compliance costs.

---

**House Ways and Means Oversight Subcommittee on the 2011 Filing  
Season and  
FY 2012 Budget Request  
March 31, 2011**

**Questions for the Record**

**Ranking Member John Lewis**

**I noticed that you have a number of open houses this filing season. I would like to know who attended these open houses, and what problems are they facing?**

**Response:**

IRS assisted 16,318 taxpayers during the Open House events held at 96 Taxpayer Assistance Centers (TACs) in 2011. The types of issues addressed during the Open House events are summarized below. The IRS did not track any demographic information from these taxpayers.

**General Issues (TAC)**

- Account-related issues such as payments, transcripts, math errors and notices
- Individual income tax return preparation
- Procedural tasks such as date stamping returns submitted by taxpayers
- Forms and publication requests
- Tax law questions

**Collection Issues**

- Tax liabilities for unemployed taxpayers and/or taxpayers experiencing financial hardship
  - Established installment agreements with the taxpayer or closed the taxpayer's case as "currently not collectible"
  - Established installment agreements for taxpayers with completed, balance due returns
  - Assisted taxpayers with levies of bank accounts and/or wages
    - Provided a partial or full levy release
    - Set up installment payment agreements
  - Adjusted installment agreements based on changes to the taxpayers' financial situation
- Tax liabilities in general
  - Assisted taxpayers with first collection notices and provided payment options
  - Explained the Offer-In-Compromise option and criteria

- Explained the importance of correct withholding and completing new W-4 forms when applicable
- Advised taxpayers to file original returns to replace the substitute return filed by the IRS
- Provided confused taxpayers with several options to resolve their outstanding liabilities
- Assisted taxpayers with collection notices

#### **Examination Issues**

Provided taxpayers with general examination guidance and answered tax law questions

- |  |   |
|--|---|
| <ul style="list-style-type: none"> <li>• General guidance on:                             <ul style="list-style-type: none"> <li>• Examination process</li> <li>• Audit reconsideration</li> <li>• State notice discussion</li> <li>• Notice to file</li> <li>• Amended returns</li> <li>• Records required for examination</li> <li>• Duplicate expense verification</li> <li>• Payments</li> </ul> </li> </ul> | <ul style="list-style-type: none"> <li>• Tax law questions dealing with:                             <ul style="list-style-type: none"> <li>• Child Care Credit</li> <li>• Earned Income Tax Credit</li> <li>• Employee business expenses</li> <li>• First Time Home Buyer Credit</li> <li>• Schedule D – capital gain</li> <li>• Self-employed health insurance</li> <li>• Employment tax</li> </ul> </li> </ul> |
|--|---|

---

[Submissions for the Record follow:]



**Statement of Colleen M. Kelley  
National President  
National Treasury Employees Union**

**On**

**“Internal Revenue Service Budget for FY 2012”**

Submitted to

**House Committee on Ways and Means Subcommittee on  
Oversight**

**March 31, 2011**

Chairman Boustany, Ranking Member Lewis, and distinguished members of the Subcommittee, I would like to thank you for allowing me to provide comments on the Administration's FY 2012 budget request for the Internal Revenue Service (IRS). As President of the National Treasury Employees Union (NTEU), I have the honor of representing over 150,000 federal workers in 31 agencies, including the men and women at the IRS.

### **IRS FY 2012 Budget Request**

Mr. Chairman, NTEU strongly supports the Administration's FY 2012 budget request of \$13.2 billion for the IRS, a 9 percent increase of \$1.1 billion over the current FY 2010 enacted level. We believe that the President's request will allow the IRS to continue helping taxpayers meet their tax obligations, improve enforcement of the tax law and generate much needed revenue for the federal government.

We are particularly pleased the Administration's budget request would provide critical increases for Service enforcement and taxpayer service activities, and would allow the IRS to continue rebuilding its workforce which remains well below mid 1990 levels.

As in previous years, NTEU also supports the budget recommendations proposed by the IRS Oversight Board which have generally called for additional funding above that requested by the Administration. For FY 2012, the Oversight Board has recommended \$13.5 billion in funding for the IRS. We would be inclined to support providing additional funding for the IRS above the Administration's request and look forward to reviewing the details of the Board's recommendation.

### **Taxpayer Services**

Providing quality customer service to the taxpayer is an important part of IRS efforts to help the taxpaying public understand their tax obligations while making it easier to participate in the tax system. Through a variety of channels, the IRS is able to provide year-round assistance to millions of taxpayers, including outreach and education programs, issuance of tax forms and publications, rulings and regulations, toll-free call centers, the IRS.gov web site, Taxpayer Assistance Centers (TACs), Volunteer Income Tax Assistance (VITA) sites, and Tax Counseling for the Elderly (TCE) sites. These efforts have enabled the IRS continue raising the standard of service to America's taxpayers and assisted in efforts to improve voluntary compliance.

In FY 2010, these efforts helped the IRS meet or exceed 83% of the Taxpayer Service performance targets. In addition, IRS taxpayer service activities were critical to its ability to deliver a successful 2010 filing season during which IRS employees processed more than 141 million individual returns and issued 109 million refunds, totaling \$366 billion and answered almost 36 million calls from taxpayers requesting information on new credits available to them. In addition, the IRS also provided in-person service at its 401 Taxpayer Assistance Centers (TACs) located around the country, for taxpayers to resolve tax issues and receive help to prepare their tax returns. In 2010, 6.4 million taxpayers visited a TAC, three percent more than in 2009. Walk-in service at TACs remains popular among elderly taxpayers, those with limited English and computer proficiency, and taxpayers without internet access.

In addition, during the 2010 filing season, IRS expanded hours of service at 16 geographically dispersed TACs, and seven were open every Saturday. In 27 locations, low-income taxpayers took advantage of IRS help in the preparation of both their state and federal tax returns. The IRS held Open House events at 200 TACs and partner sites nationwide to help taxpayers prepare their returns and resolve their tax issues. As a result, more than 31,400 taxpayers were served and over 7,700 returns were prepared at these events.

The delivery of a successful 2010 filing season by the IRS is all the more impressive as employees delivered these numbers while also being confronted by a variety of challenges presented by implementation of provisions in the American Reinvestment and Recovery Act of 2009, the Worker, Homeownership, and Business Assistance Act of 2009, and increased telephone demand for Economic Recovery Payment inquiries.

We were glad to see the Administration's request of \$2.3 billion for taxpayer services acknowledges the good service that IRS employees provided to taxpayers in FY 2010 while also recognizing that additional progress can be made. In particular, we strongly support the proposed additional funding to improve telephone level of service, improve the IRS website and provide a variety of new online services.

In FY 2012, the IRS plans to increase the telephone level of service by adding resources to meet the ever-increasing demand and continuing to make efficiency improvements such as automated self-service applications that allow taxpayers to obtain information on less complex issues such as refund inquiries. These improvements will free up staff to deal with the more complex tax law issues stemming from the passage of new legislation. In addition, the IRS continues to study the effects of services it offers to taxpayers on the internet, at walk-in sites, and on its toll-free telephone lines as well as exploring the relationships between taxpayer errors and unclear correspondence to aid in the development of new approaches to service.

NTEU strongly believes providing quality services to taxpayers is an important part of any overall strategy to improve compliance and that the President's request for taxpayer services will enable the IRS to deliver another successful filing season, improve the responsiveness and accuracy of taxpayer service, and support Service efforts to enhance taxpayer compliance.

### **Enforcement**

Mr. Chairman, NTEU believes a strong enforcement program that respects taxpayer rights, and minimizes taxpayer burden, plays a critical role in IRS' efforts to enhance voluntary compliance, narrow the tax gap and reduce the deficit. In FY 2010, IRS enforcement efforts brought in almost \$58 billion in enforcement revenue, an 18% increase over FY 2009. In addition, other key IRS enforcement programs continued to show progress over FY 2009. These include a 6% increase in collection case closures, a 20% increase in Automated underreporter (AUR) contact closures, an 8% increase in large corporate audits and an 11 % increase in the number of individual return examinations.

That is why NTEU was happy to see the Administration's budget request would provide a \$462 million increase in funding for IRS tax enforcement above the current FY 2010 enacted level, including additional resources made available through a program integrity cap adjustment.

This increased funding will enable the IRS to continue strengthening current Service compliance programs designed to close the tax gap in several areas, including: increasing compliance by addressing offshore tax evasion through more examinations and full implementation of the Foreign Account Tax Compliance Act (FACTA); implementing information reporting requirements approved by Congress in 2008 to validate income reported by businesses by reconciling their income with their payment card receipts and third party transactions; and improving tax debt collection coverage and collection processes. The proposal will also allow IRS to continue to focus on compliance issues and new responsibilities arising from recent tax law changes included in major legislation, including the American Recovery and Reinvestment Act and the Affordable Care Act.

These investments in IRS enforcement programs are expected to generate \$1.3 billion in additional annual enforcement revenue, resulting in a return on investment (ROI) of 6.4 to 1, once new hires reach full potential in FY 2014. In addition, investment in new enforcement initiatives will also encourage voluntary compliance, further increasing revenue. According to the IRS, the deterrence value of these investments and other IRS enforcement programs on voluntary compliance is conservatively estimated to be at least three times the direct revenue impact.

NTEU strongly supports targeting additional resources to programs that would help close the tax gap, including new initiatives that deepen and broaden IRS' focus on international tax compliance of high net worth individuals and entities. The IRS has demonstrated that targeted compliance resources more than pay for themselves through increased revenues, which has motivated past Congresses to target additional funds to these enforcement activities. In addition to generating additional revenue for the federal government, reducing the tax gap will help strengthen public trust in the fairness of the tax system which will positively impact voluntary compliance with tax laws.

#### **Physical Security**

Mr. Chairman, as you know, last February, in what authorities believe was an intentional attack, a pilot crashed his small plane into a building housing almost 200 IRS employees in Austin, TX, killing one employee and seriously injuring several others. This brazen and cowardly attack, serves as a grim reminder of the great risk that the men and women of the IRS face each and every day in service of this country.

As one of the most public faces of the U.S. Government, the IRS and its employees often bear the brunt of anti-government rhetoric and threats. According to the Treasury Inspector General for Tax Administration (TIGTA) which is charged with investigating threats and assaults against IRS personnel, more than 1,200 threat and assault cases were referred to TIGTA for investigation between 2001 and 2008. The cases resulted in more than 167 indictments and at least 195 convictions.



That is why NTEU was happy to see that the Administration proposed \$15 million to enhance physical security for IRS employees. This includes \$10 million to expand guard serve at Taxpayer Assistance Centers (TACs) during filing season, \$1.5 million to improve security at IRS facilities around the country, and \$3.9 million to provide additional resources to identify and investigate individuals or entities whose anti-government or anti-tax rhetoric exhibit behavioral traits associated with domestic terrorism.

NTEU believes these critical investments will enhance the overall security of IRS employees in the work place, while maintaining open access for the taxpayers that they serve.

### **Contracting Out**

Mr. Chairman, NTEU recognizes that in the current fiscal crisis, it is critical that the federal government look for ways to maximize its resources and to root out waste, fraud and abuse wherever they find it. One way in which NTEU believes that the federal government can best accomplish this is to reform the broken competitive sourcing process, and bring contracted work back in-house. By ensuring federal employees are able to compete for work with contractors on an even playing field, and identifying areas in which the government could perform this work more effectively and efficiently, the federal government will be better able to provide high quality services and will save taxpayer dollars. The Administration has already begun to reform federal contracting by requiring federal agencies to cut wasteful contract spending, reduce overreliance on contractors, and improve oversight and accountability. These efforts are expected to result in \$40 billion in annual savings by the end of 2011 which could be used to ensure agencies have the necessary resources and staffing.

In recent years, Congress has acknowledged the inherent flaws in the competitive sourcing process and has included language in year-end spending bills that prohibit the use of funds to begin new public-private Circular A-76 competitions for another year. NTEU strongly believes the current A-76 competition moratorium should be continued for another year until further steps are taken to reform the broken competitive sourcing process that has eroded the ability of agencies to perform many critical functions, and has led to contractors performing work that should be performed solely by federal employees.

In addition, we would strongly encourage Congress to continue the current prohibition on the use of funds for private collection agencies through FY 2012. The use of private collection agencies to collect tax debts has repeatedly been shown to be a waste of taxpayer dollars and lead to taxpayer abuse. The 2006 initiative resulted in widespread taxpayer abuse and a loss of almost \$5 million to the federal government, after subtracting program administration costs and commissions payable to the PCAs. While the IRS ended the private tax collection program in 2009, it still retains the statutory authority to revive the program in the future.

### **Conclusion**

Mr. Chairman, thank you again for allowing NTEU to provide our thoughts on the Administration's FY 2012 budget request for the IRS. We strongly believe that by investing in demonstrably effective enforcement and taxpayer service programs, the Administration's request will allow IRS to provide taxpayers with top quality service, enhance voluntary compliance, narrow the tax gap and reduce the deficit.

