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THE INTERNAL REVENUE SERVICE OPERATIONS AND THE 2010 TAX RETURN FILING SEASON

HEARING

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT

OF THE

COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

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INTERNAL REVENUE SERVICE OPERATIONS AND THE 2010 TAX RETURN FILING SEASON

THURSDAY, MARCH 25, 2010

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

The Subcommittee met, pursuant to notice, at 10:04 a.m., in Room 1100, Longworth House Office Building, the Honorable John Lewis [Chairman of the Subcommittee] presiding.

[The advisory of the hearing follows:]

HEARING ADVISORY

FROM THE COMMITTEE ON WAYS AND MEANS

Lewis Announces a Hearing on Internal Revenue Service Operations and the 2010 Tax Return Filing Season

March 18, 2010

House Ways and Means Oversight Subcommittee Chairman John Lewis (D–GA) today announced that the Subcommittee on Oversight will hold a hearing on Internal Revenue Service (IRS) operations, the 2010 tax return filing season, and Fiscal Year 2011 budget proposals. **The hearing will take place on Thursday, March 25, 2010, at 10 a.m., in the main Committee hearing room, 1100 Longworth House Office Building.**

The Commissioner of the Internal Revenue Service, the Honorable Douglas Shulman, will be the only witness at the hearing. Any individual or organization not scheduled for an oral appearance may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

FOCUS OF THE HEARING:

In 2009, the IRS collected $2.35 trillion and processed 236 million tax returns, including 144 million individual income tax returns. The Subcommittee will review, and discuss any challenges arising during, the current tax return filing season with a focus on: the availability of assistance to taxpayers; the most common taxpayer questions and errors; tax return processing; and recent tax refund scams. Further, the Subcommittee will consider how the economy has affected taxpayers this filing season.

The Subcommittee also will review overall IRS operations. Specifically, the Subcommittee will focus on: (1) the adequacy of taxpayer services, including toll-free telephone service; (2) fairness in the examination and collection programs, including increased reliance on correspondence examinations and liens; (3) efforts to reduce the $345 billion tax gap; and (4) needs related to security at IRS facilities. As part of its consideration of IRS operations, the Subcommittee will review the Administration's Fiscal Year 2011 budget proposal for the IRS of $12.6 billion, an increase of 4 percent over Fiscal Year 2010 levels.

In announcing the hearing, Chairman Lewis said, **"A successful filing season is critical to confidence in our federal tax system. It is important for taxpayers to know that their returns will be processed efficiently and refunds will be issued quickly. I look forward to hearing from the Commissioner on the status of the filing season and services that are available to low-income taxpayers or those experiencing economic difficulties."**

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1. All submissions and supplementary materials must be provided in Word or WordPerfect 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.

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

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.

Chairman LEWIS. Good morning. The hearing is now called to order.

Today the Oversight Subcommittee will review the operation of the Internal Revenue Service and the tax filing season.

Before we begin, I would like to express our continued sympathy to the IRS employees in Austin and throughout our country. I want them to know that their safety is our top concern. I also want them to know that we value the good work that they do to help taxpayers, process tax returns, and collect our federal revenue.

Mr. Commissioner, we want to thank you for your leadership, for your vision, and for your deduction. We are pleased to have you before us. First we would like to thank you for coming to this hearing today, and for holding hundreds of open houses this filing season to help taxpayers who are having serious financial problems. We also would like to learn if there is more that can be done to help taxpayers this season, either in person or on the telephone.

We thank you, Mr. Commissioner, again for your leadership on the regulation of tax return preparers. I believe that the regulation of tax return preparers will protect taxpayers and enhance compliance.

Finally, we will explore the agency's proposed budget. We will consider what must be done to provide the agency with the re-

sources that it needs to meet its core tax mission and its increasing responsibilities, including those under the health reform legislation.

We on this subcommittee have full confidence that the IRS can balance taxpayer service and enforcement with the support of the Congress. I am hopeful that others on the subcommittee and in the Congress will join me in pledging their support today.

Now I am pleased to recognize the distinguished Ranking Member, Dr. Boustany, for his opening statement.

Dr. BOUSTANY. Thank you, Mr. Chairman, and thank you for holding the hearing. And I thank you for yielding time to me.

Commissioner Shulman, welcome. Thank you once again for appearing before this Subcommittee. And more generally, I want to thank you and every IRS employee who works for you for their hard work and their dedication to public service.

And I want to make it clear that even when we in Congress criticize certain IRS operations and question certain responsibilities and how they are handled, we are doing this in the context of our job in oversight. And we are not—I want to emphasize not—personally attacking the fine public servants who work at the agency, and we are not attacking your leadership on a personal level.

I also want to mention the horrific attack on the IRS offices in Austin, Texas on February 18th. Let us continue to honor the memory of Mr. Vernon Hunter, the IRS employee and Vietnam veteran who lost his life in this very senseless attack. And as I said on the House floor on March 3rd, we also should recognize the courage and heroism of those men and women, including IRS employees, first responders, and others, who responded to the attack to ensure that our country did not suffer even greater losses.

And I want to offer my pledge to work with you, and that pledge also to the agents and employees of the IRS, that we will work to ensure that all safety needs are met with your agency. So I just wanted to offer that. I enjoyed our conversation yesterday, and I look forward to future conversations as well on this issue.

Mr. Chairman, I want to say though our debate is often sharp and contentious, as we saw during the health care debate over the weekend, clearly there is no license for violence in our society, nor is there license for the kinds of racial slurs and other slurs that we heard about.

And so, you know, we should continue a vigorous debate on the issues and try to stay aboveboard and keep it from degenerating to, you know, a total lack of civility. So I wanted to offer that publicly.

Before Commissioner Shulman begins his testimony, I want to highlight two issue sort of importance to me. The first is the IRS's role in health legislation that the President just signed into law. This legislation envisions the IRS having a central role in administering a new national health insurance system and enforcing the rules.

During the 2008 presidential campaign, then-Senator Obama and Candidate Obama attacked Senator McCain's health care reform plan on two main points. In an October 4, 2008 memo, then-Candidate Obama argued against the McCain approach because, "It pays for its new tax credit by taxing employee health benefits for

the first time in history," and, "The new tax credit would go directly to insurance companies, not individuals."

I find this ironic that the Democrats' government health care plan, in the bill that was now signed into law, does precisely these two things. The health care bill imposes a 40 percent tax on what the Democrats call "excess benefits," and turns the IRS into a collection agency for health insurance companies. These so-called tax credits won't actually end up in the taxpayers' pockets. Instead, they will end up in the insurance companies' profits.

The second topic I would like to mention involves the Democrats' failed stimulus bill. This past Monday, Commissioner Shulman, you joined Vice President Biden and Treasury Secretary Geithner in celebrating this year's increase in average tax refunds.

And you said, I quote, "The average tax refund has reached $3,036 this year, a $266 increase from a year ago. The Recovery Act is a major factor behind these larger record refunds." And then you went on to suggest that the tax benefits provided in the stimulus bill were putting more money in people's pockets.

But we have done some analysis on the economic data, and we see a different story. In fact, higher refunds provide further proof that the stimulus bill was a failure. The economic data show that people earned less income in 2009 than in 2008 due to job losses and wage cuts.

For instance, between the end of 2008 and the end of 2009, the unemployment rate, we all know, went from 7.4 percent to 10 percent. Non-farm private sector employment dropped by 5 million jobs over the course of 2009. Yet many people who first became unemployed in 2009 probably over-withheld during the period they were working because they set their withholding based on an analyzed salary that either later disappeared or was diminished.

And as a result, their year-end income was lower than expected, and now they are entitled to a tax refund. Thus, larger refunds are evidence of a worsening economy in 2009, which in turn is evidence of a failed stimulus bill.

So, Commissioner Shulman, I look forward to your testimony today, hearing your thoughts on these and other issues. And Mr. Chairman, I yield back.

Chairman LEWIS. Thank you very much, Dr. Boustany, for your statement and for your extended remarks on the climate and atmosphere here in Washington.

Dr. BOUSTANY. Thank you, Mr. Chairman.

Chairman LEWIS. Now we will hear from our witness, IRS Commissioner Doug Shulman. I ask that you limit your testimony to five minutes. Without objection, your entire statement will be included in the record. Welcome.

STATEMENT OF DOUGLAS H. SHULMAN, COMMISSIONER, INTERNAL REVENUE SERVICE

Mr. SHULMAN. Thank you, Mr. Chairman, Ranking Member Boustany, Members of the Subcommittee. I appreciate this opportunity to testify about the filing season and our 2011 budget.

2010 filing season has proceeded smoothly thus far. Telephone-assisted levels of service have improved since last year, when they

declined due to unprecedented demand and enactment of tax-related legislation.

Accuracy rates and customer tax law account questions remain very high. Overall, filing is down a little bit at this point, which we think is due to the severe snowstorms and weather. E–File remains up, and the trend continues in the right direction, where we are getting more electronic filing. I would also mention that in this challenging economy, average refunds are up by about $266 this year, to about $3,036 this year.

We have taken several steps this year, building on steps we took last year, to help taxpayers through some of these unprecedented difficult times. The most notable that I would mention is I announced earlier this month that we are changing the eligibility rules for our offer and compromise program, where someone can settle a tax debt.

In the past, you looked at three-year average earnings, so you looked back. And someone who lost a job would average in, when they had a job, their earnings. Now we are just looking at current income, making settlement offers with people. And then, if they get a job, we will do an adjustment in the future.

We also mentioned, Mr. Chairman, as you mentioned as well, we are holding special Saturday open houses. We are assembling all the people needed to make a decision and solve taxpayer decisions on the spot. We will hold about a thousand of those this year, the first one this Saturday.

We are also working hard to implement the recent Hiring Incentives to Restore Employment Act, also known as the Jobs Act, where people receive a 6.2 percent payroll tax incentive that goes directly to small businesses. We are working on guidance; by second quarter, people will be able to claim that, and that should help with jobs in this economy. We are looking forward to supporting that legislation.

In recognition of the critical role that the IRS plays in this economy, the President has given us a judicious investment in both service and enforcement programs in his 2011 budget. That budget is going to allow us to carry out things like our continued focus on offshore tax evasion; our focus on making sure high income individuals and corporations pay the proper amount of taxes; our effort to oversee the tax return preparer community, which is integral to our strategy for compliance and service; and will also give us the funds to finish our tax account database projects, which is going on for a number of years. We will be able to complete it for the 2012 filing season, assuming Congress approves the budget.

Let me end by giving you a quick update on the incident in Austin where an individual flew a plane into an IRS building, killing one of our employees. This was an incredibly sad event for the IRS. But it is also an event that reminded me of the important work that the men and the women of the IRS do every day, and that it is work that is sometimes not appreciated by those who would blame this agency for the nation's tax laws.

First, I will tell you we have no reason to believe that this attack could have been prevented. And we have no recollection to believe that this was part of any organized opposition to the agency. How-

ever, I am very concerned that this incident not fan the flames of ignorance about the IRS's core mission and our approach.

While we do engage in compliance activities for the small portion of Americans who aren't paying their fair share of taxes, the vast majority of our work is serving the hardworking taxpayers of this country—processing returns, sending out refunds, answering questions on the phone, trying to help people navigate a complex tax system.

I am incredibly appreciative of the support that this committee has shown the agency during the difficult days after Austin. And I request that all Members of the Committee join me in explaining to the public that the vast majority of Americans experience an IRS that is merely trying to help them process a tax return and get a refund; and that at its core, we are an agency of public servants working to serve the American people.

Mr. Chairman, this concludes my oral testimony. I am happy to answer questions.

[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 2011 BUDGET REQUEST
MARCH 25, 2010

Introduction and Summary

Chairman Lewis, Ranking Member Boustany and Members of the Subcommittee on Oversight, thank you for this opportunity to testify on IRS' efforts to ensure a successful tax filing season this year. I would also like to thank you for allowing me to provide you with an overview of our proposed FY 2011 Budget and what we hope to accomplish with these resources.

The 2010 filing season has proceeded smoothly and with few problems. There have also been some noteworthy gains. For example, telephone assistor level of service (LOS) has improved by more than 25 percent last year when it declined due to an unprecedented demand for service caused by the enactment of tax-related legislation.

Accuracy rates for both customer tax law and accounts questions remain in the 90-plus percentile. Overall filing is down three percent, due in large part to the effects of the economic downturn. We are seeing lower than expected traditional paid practitioner e-file volumes as taxpayers seek other ways to file their returns, such as on-line. However, e-file as a percentage of total individual returns is up from 80 percent to 83 percent – continuing a very positive trend. And in a still challenging economy, it is good news that the average refund is $3,036 – up by almost 10 percent as compared to last year.

The IRS is also taking several additional steps this tax season to help people having difficulties meeting their tax obligations because of unemployment or other financial problems. Most recently, on March 9, 2010, the IRS announced additional steps it is taking to assist unemployed taxpayers, the most significant being new flexibility for offers in compromise. For those taxpayers facing economic troubles, including recent unemployment, IRS employees will be allowed to consider a taxpayer's current income and potential for future income when negotiating an offer in compromise. The standard practice is to review offers based on income in prior years. The IRS also announced that it will hold hundreds of special Saturday open houses to give struggling taxpayers more opportunity to work directly with IRS employees to resolve issues. These steps are an expansion of efforts that began more than a year ago and also include special outreach

with partner groups to unemployed taxpayers and the availability of more information on a special page of the IRS website.

Mr. Chairman, in recognition of the critical role that the IRS plays in the nation's economy, the President's FY 2011 Budget submission includes a judicious investment in the IRS' core service and enforcement programs. It also includes the funding needed to work toward timely completion of the core taxpayer account database, a key priority for the agency.

The funding in the President's Budget will be used to carry out the IRS' strategic and balanced agenda that includes: improved service to taxpayers; a robust and targeted enforcement program to address offshore tax evasion and improve tax compliance for corporate and high-income taxpayers; better use of data, such as credit card and securities basis information reporting; completion of the new taxpayer account data base and enhancements to our electronic filing platforms, as well as improved IRS website offerings and performance; and workforce development to ensure that we have a talented and capable workforce for the foreseeable future.

The IRS will also continue to administer on-going, tax-related provisions of the American Recovery and Reinvestment Act of 2009 (Recovery Act), the Worker, Homeownership, and Business Assistance Act of 2009, and any other tax provisions that have been extended, such as eligibility for the 65 percent COBRA health care tax credit extended through March 31, 2010 by the Temporary Extension Act of 2010 (PL 111-144) and which may be extended until December 31, 2010 by the American Workers, State and Business Relief Act (HR 4213).

The 2010 Filing Season

Mr. Chairman, although three weeks remain in the current filing season, it has proceeded smoothly and with few problems, which were quickly identified and remedied. As will be discussed later in my testimony, the IRS and its volunteer partners continue to help taxpayers struggling through these difficult economic times.

The IRS is also beginning its implementation of the Hiring Incentives to Restore Employment (HIRE) Act that was signed by the President on March 18th. Under the new law, employers who hire unemployed workers this year (after February 3, 2010 and before January 1, 2011) may qualify for a 6.2 percent payroll tax incentive, in effect exempting them from their share of Social Security taxes on wages paid to these workers after the date of enactment. In addition, for each worker retained for at least a year, businesses may claim an additional general business tax credit, up to $1,000 per worker, when they file their 2011 income tax returns. The IRS is working on revised forms, instructions, and necessary programming so eligible employers will be able to claim the new tax incentive on their employment tax form beginning with the second quarter of 2010. Information and answers to frequently asked questions will soon be available on IRS.gov.

General Filing Season Data

As of March 13, 2010, the IRS received 68.7 million individual returns. Overall filing is down three percent, due in large part to the effects of the economic downturn. We are seeing lower than expected traditional paid practitioner e-file volumes as taxpayers seek other ways to file their returns, such as on-line. However, e-file as a percentage of total individual returns is up from 80 percent to 83 percent – continuing a very positive trend and showing the IRS' commitment to a robust electronic tax administration program.

The number of taxpayers e-filing their returns from a home computer continued to grow this filing season. More than 21.2 million prepared their own e-file return – almost a seven percent increase over the same time period last year. However, Free File continued to show a decline, dropping by five percent over last year. Nevertheless, all qualifying taxpayers, including those filing for the Earned Income Tax Credit (EITC), are encouraged to use Free File to ensure a speedy refund.

Through March 13, 2010, the IRS issued 57.8 million refunds for a total of $175 billion, as compared to 61 million returns for a total of $169 billion over the same time period in 2009. The average dollar refund totals $3,036 as compared to $2,770 for the same week last year, an increase of 9.6 percent. Over the same time period, the IRS directly deposited 47.9 million refunds to taxpayers, as compared to 48.6 million last year. Starting this filing season, taxpayers could also purchase up to $5,000 of Series I U.S. Savings Bonds using their federal tax refund. Through March 12, 2010, more than 13,713 taxpayers have taken advantage of this great opportunity, requesting more than 50,000 bonds totaling approximately $4.8 million.

Working with media and its many stakeholders, the IRS publicized that taxpayers filing electronically with direct deposit can get their refunds in as few as ten days. Based on the most current Refund Timeliness data, the average time to process a refund for a paper tax return is six to eight weeks this year.

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 13, 2010, IRS telephone assistors answered 9.64 million calls, a 15.3 percent decrease over the same period last year. The IRS also completed 18.3 million automated calls, a 12 percent increase over last year's 16.3 million, reflecting a growing taxpayer appetite for quality self-serve options.

Particularly gratifying was the strong rebound in Assistor Level of Service (LOS) which currently stands at 74.2 percent over last year's 60.9 percent – a 21.9 percent gain.

The drop in LOS in 2009 was partially due to the number of taxpayers calling to obtain their prior year adjusted gross income, which is used to satisfy the signature requirements when e-filing a current year return. More taxpayers were also calling regarding math errors and refund issues related to the Recovery rebate credit and questions generated by the economic downturn and the Recovery Act.

To clarify, LOS is a measure used by the IRS for both planning and internal management of our live customer service representative (CSR) telephone assistance services. This measure is derived through a mathematical formula that essentially equates to the success rate of customers that call the IRS for live telephone assistance on our 1-800 help line at any given point in time. However, it does not account for those calling that choose to call back another time based on anticipated wait time.

This year, the IRS added an estimated wait time feature as a convenience for taxpayers. In addition, increased funding in the President's FY 2011 Budget would be used to improve the telephone LOS from a projected 71 percent in FY 2010 to a target of 75 percent in FY 2011.

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

Website Usage and New Media

IRS.gov has become the preferred source of information for millions of taxpayers to get answers to their tax questions and economic recovery legislation, and to prepare and file a federal tax return accurately and on time. IRS.gov/Español offers many of the same services and information in Spanish.

As of March 16, 2010, the number of visits to the website is four percent less than last year's numbers over the same time period – approximately 121.1 million. However, visits to the "Where's My Refund" electronic tracking tool are up by 13.3 percent.

When taxpayers visit the IRS.gov website, they will first see a rotating spotlight feature on the front page. The spotlights, which change every few seconds, highlight important taxpayer information, such as "Making Work Pay," "Homebuyer Credit," Tax Law Changes Can Benefit You," "Where's My Refund" and "What If Scenarios" that deal with payment and other financial problems.

Taxpayers can also use electronic tools such as the EITC Assistant to determine if they qualify for the refundable tax credit or click on "Tax Benefits of the American Recovery and Reinvestment Act of 2009" to learn about energy, education, new vehicle and homebuyer credits available that could help them save money.

The IRS also produced a number of podcasts this filing season that are available on IRS.gov and iTunes. In addition, the IRS created more than a dozen YouTube Videos on a variety of subjects including the "Education Tax Credit," "Making Work Pay," and the

"New Homebuyer Credit." Many are available in English, American Sign Language and Spanish. These are new ways for the IRS to reach out to a new generation of taxpayers.

Walk-In Contacts

The IRS continues to provide in-person service at its 401 Taxpayer Assistance Centers (TACs). As of March 13, 2010, approximately 1.38 million taxpayers were served – a 5.1 percent decline over the previous year, reflecting a continued weakening in the demand for such service.

However, walk-in service still remains popular among elderly taxpayers, those with limited English and computer proficiency, and taxpayers without Internet access. As discussed later in my testimony, the TACs are a useful filing season resource for taxpayers resolving tax issues and needing help preparing their tax returns.

Helping Struggling Taxpayers

The IRS is taking several additional steps this tax season to help people having difficulties meeting their tax obligations because of unemployment or other financial problems.

The steps build on efforts begun in the 2009 tax filing season to help taxpayers facing financial difficulties obtain the maximum refunds to which they are entitled by encouraging them to take advantage of applicable tax credits, such as the EITC and those contained in the Recovery Act, and to accelerate their refunds.

We also recognize that some people are struggling to meet their tax obligations and need assistance. The IRS wants to do everything it can to help those taxpayers who have lost their job or face financial strain, especially those who have done the right thing in the past and are facing unusual hardships.

New Flexibility for Offers in Compromise

For some taxpayers, an offer in compromise – an agreement between a taxpayer and the IRS that settles the taxpayer's debt for less than the full amount owed – continues to be a viable option. IRS employees will now have additional flexibility when considering offers in compromise from taxpayers facing economic troubles, including the recently unemployed.

Specifically, IRS employees will be permitted to consider a taxpayer's current income and potential for future income when negotiating an offer in compromise. Normally, the standard practice is to judge an offer amount on a taxpayer's earnings in prior years. This new step provides greater flexibility when considering offers in compromise from the unemployed. The IRS may also require that a taxpayer entering into such an offer in compromise agree to pay more if the taxpayer's financial situation improves

significantly. These immediate steps are part of an on-going effort by the IRS to ensure the availability of the offer in compromise program for taxpayers.

Saturday Open Houses

Even though the IRS provides tax assistance to individuals and families every day of the year, the focus for Saturday Open Houses this year was to help those dealing with difficult economic times. The first of these was held on Saturday, February 20th, when more than 200 Taxpayer Assistance Centers went the extra mile and opened their doors for extended service hours. The IRS plans to hold hundreds of special Saturday open houses over the next couple of months to give struggling taxpayers more opportunities to work directly with IRS employees to resolve issues. The next Open House will be March 27. Dates and times for the additional Saturdays in the spring and early summer will be announced shortly.

During the expanded Saturday hours, taxpayers will be able to address economic hardship issues they may be facing or get help claiming any of the special tax breaks in last year's Recovery Act, including the:

- Homebuyer tax credit
- American Opportunity Credit
- Making Work Pay Credit
- Expanded Earned Income Tax Credit

In addition to these special Saturdays, taxpayers can take advantage of toll-free telephone assistance and regularly scheduled hours at local Taxpayer Assistance Centers. Taxpayers can find the location, telephone number and business hours of the nearest assistance center by visiting the Contact my Local Office page on IRS.gov.

Low-income taxpayers, people who lost their jobs, and even those with a fear of the IRS and who had not filed their taxes in years, received help in preparing their returns and in resolving their tax issues. Local volunteer tax preparation sites, as well as many Stakeholder Partnership, Education & Communications (SPEC) employees, pitched in to help as the massive rally of tax assistance unfolded throughout the nation.

Special Outreach Efforts to Unemployed

The IRS is working and coordinating with state departments of revenue and state workforce agencies to help taxpayers who are having problems meeting their tax liabilities because of unemployment or other financial problems.

These coordinated efforts may include opportunities for taxpayers to make payment arrangements and resolve both federal and state tax issues in one place.

Special Section of IRS.gov Created

Taxpayers who are unemployed or struggling financially can find information on a new page on the IRS website, IRS.gov. This online tax center has numerous resources including links to information on tax assistance and relief to help struggling taxpayers.

Other Options Available for Taxpayers

The IRS will continue to offer other help to taxpayers, including:

- Assistance of the Taxpayer Advocate Service (TAS) for those taxpayers experiencing particular hardship navigating the IRS;
- Postponement of collection actions in certain hardship cases;
- Added flexibility for missed payments on installment agreements and offers in compromise for previously compliant individuals having difficulty making payments;
- Additional review of home values for offers in compromise in cases where real-estate valuations may not be accurate; and
- Accelerated levy releases for taxpayers facing economic hardship.

In addition, the IRS will accelerate lien relief for homeowners if a taxpayer cannot refinance or sell a home because of a tax lien. As previously announced, a taxpayer seeking to refinance or sell a home may request the IRS make a tax lien secondary to the lien by the lending institution that is refinancing or restructuring a loan. The taxpayer may also request the IRS discharge its claim if the home is being sold for less than the amount of the mortgage lien under certain circumstances.

Return Preparer Initiative

The IRS recently unveiled a major initiative to regulate tax return preparers, who are a critical part of the tax system. Given the complexity of the tax code, more and more Americans now turn to a preparer to help them file their taxes. The IRS estimates that there are somewhere between 900,000 and 1.2 million paid tax return preparers. Making them an integral link to our service and compliance strategies will help the IRS to do its job.

The IRS plans to require registration, minimum competency testing, and continuing education of paid tax return preparers. In addition, once a testing process is set up and running, the IRS will create a public database of preparers, so that taxpayers can find out if they are dealing with a qualified preparer.

The IRS is also shifting enforcement resources to focus on preparers. Beginning this filing season, the IRS is expanding “knock and talk” and other programs to visit thousands of preparers to discuss their operations and ways to reduce preparer error rates.

The goals of the strategy are to leverage the return preparer community to improve service to taxpayers, increase compliance, and enhance the integrity of the overall tax system.

The Administration's FY 2011 Budget Funds Key Priorities

The total resources requested to support IRS activities for FY 2011 are $12,971,962,000. This amount includes $12,633,270,000 from direct appropriations, an estimated $144,592,000 from reimbursable programs, and an estimated $194,100,000 from user fees. The direct appropriation is a $487,147,000 increase, or a 4.01 percent increase over the FY 2010 enacted level of $12,146,123,000.

Enforcement Program

The FY 2011 President's Budget Request includes an Enforcement account increase of $293.4 million for investments in strong compliance programs, including a robust initiative to address offshore tax evasion. As previously noted, additional enforcement resources will address underreporting of income associated with international activities and expand enforcement efforts on noncompliance among corporate and high-wealth taxpayers.

Increased resources for the IRS compliance programs yield direct, measurable results through high return on investment activities. The new enforcement personnel funded through a program integrity allocation adjustment in the FY 2011 President's Budget will generate nearly $2 billion in additional annual enforcement revenue once the new hires reach full potential in FY 2013. Similar to past budgets, the allocation adjustment applies to the Enforcement and Operations Support accounts, and is justified by the net positive value enforcement resources deliver. Vigorous enforcement also encourages voluntary compliance, further increasing revenue, by generating public awareness of the consequences of not meeting one's tax responsibilities. The return on investment estimate does not include the revenue impact from 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.

Explanation of Enforcement Budget Activities

The FY 2011 President's Budget request is $5,797,400,000 in direct appropriations and an estimated $61,506,000 from reimbursable programs for a total operating level of $5,858,906,000. The direct appropriations level is an increase of 5.3 percent from the FY 2010 enacted level and includes additional tax enforcement activities funded through a program integrity allocation adjustment. This appropriation funds the following budget activities.

- **Investigations ($651,966,000 from direct appropriations and an estimated $50,567,000 from reimbursable programs)** This budget activity funds the criminal investigation programs that uncover criminal violations of the internal

revenue laws and other financial crimes, enforce criminal statutes relating to these violations, and recommend 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 ($4,974,618,000 from direct appropriations and an estimated $10,245,000 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, excise, and estate and gift tax exams), international collections and international examinations. The budget activity also supports appeals and litigation activities associated with exam and collection.

- **Regulatory ($170,816,000 from direct appropriations and an estimated $694,000 from reimbursable programs)** This budget activity funds the development and printing of published IRS guidance materials; interpretation of tax laws; advice on general legal services, rulings and agreements; enforcement of regulatory rules, laws, and approved business practices; and taxpayers support in the areas of pre-filing agreements, determination letters, and advance pricing agreements. The Office of Professional Responsibility is funded within this budget activity and 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 Program

The FY 2011 President's Budget includes a Taxpayer Services account increase of $43.1 million. The increase includes $20.9 million to improve telephone level of service, increasing the level of service performance target to 75 percent from 70 percent in FY 2009 and 71 percent in FY 2010.

Providing quality taxpayer service is especially important to help taxpayers 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 correspondence from the IRS.

Explanation of Taxpayer Service Budget Activities

The FY 2011 President's Budget is $2,321,975,000 in direct appropriations, an estimated $34,159,000 from reimbursable programs, and an estimated $127,000,000 from user fees, for a total operating level of $2,483,134,000. The direct appropriations level is an

increase of 1.9 percent from the FY 2010 enacted level. This appropriation funds the following budget activities.

- **Pre-Filing Taxpayer Assistance and Education ($693,753,000 from direct appropriations and an estimated $1,459,000 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 ($1,628,222,000 from direct appropriations, an estimated $32,700,000 from reimbursable programs, and an estimated $127,000,000 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.

Operations Support

Explanation of Budget Activities

The FY 2011 President's Budget is $4,108,000,000 in direct appropriations, an estimated $48,927,000 from reimbursable programs, and an estimated $67,100,000 from user fees, for a total operating level of $4,224,027,000. The direct appropriation level is an increase of 0.6 percent from the FY 2010 enacted level. This appropriation funds the following budget activities as well as $25 million to improve the IRS.gov website infrastructure and redesign the website to meet taxpayer needs and the growing demand for more electronic services.

- **Infrastructure ($889,929,000 from direct appropriations, an estimated $398,000 from reimbursable programs, and an estimated $16,100,000 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 ($1,337,776,000 from direct appropriations and an estimated $33,110,000 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 ($1,880,295,000 from direct appropriations, an estimated $15,419,000 from reimbursable programs, and an estimated $51,000,000 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. The IRS business programs rely on these systems to process tax and information returns, account for tax revenues collected, send bills for taxes owed, issue refunds, assist in the selection of tax returns for audit, and provide telecommunications services for all business activities, including the public's toll-free access to tax information.

Business Systems Modernization (BSM)

Explanation of Budget Activities

The FY 2011 President's Budget is $386,908,000 in direct appropriations. This is an increase of 46.6 percent from the FY 2010 enacted level. This appropriation funds the planning and capital asset acquisition of information technology (IT) to continue the modernization of IT systems and to move toward completion of the new taxpayer account database. The completion of the core taxpayer account database is the cornerstone of modernization and is a prerequisite to the development of 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. It also funds BSM labor and related contract costs.

Health Insurance Tax Credit Administration (HITCA)

The FY 2011 President's Budget is $18,987,000 in direct appropriations. This is an increase of 22.4 percent from the FY 2010 enacted level. This appropriation funds the administration of a refundable tax credit for health insurance to qualified individuals, which was enacted as part of the Trade Adjustment Assistance Reform Act of 2002. The additional resources will help administer the Health Coverage Tax Credit expansion found in the Recovery Act.

FY 2011 Budget Adjustments

The IRS funding increase for FY 2011 is $487,147,000, which includes $219,523,000 for maintaining current levels, a temporary base adjustment of $3,494,000 to support the Recovery Act's expansion of the Health Coverage Tax Credit (HCTC), a decrease of $32,680,000 from non-recurring activities, a decrease of $157,958,000 from efficiencies and savings, and a program increase of $454,768,000 to improve taxpayer service, strengthen enforcement, and complete the new taxpayer account database. By FY 2013, the revenue-producing enforcement investments are projected to increase annual enforcement revenue by nearly $2 billion. The Budget supports these activities by proposing the following initiatives:

- $20,945,000 to increase the telephone level of service, which includes a $9.0 million reallocation from the FY 2010 enacted levels for Taxpayer Service grant and advocacy programs;
- $247,446,000 to reduce the tax gap by investing in a strong compliance program; and
- $167,585,000 to complete development of the new taxpayer account database and continue investments in electronic filing systems.

Building on the FY 2010 Enacted Level

The FY 2010 enacted level for the IRS is $12,146,123,000, supporting an estimated 95,070 FTE.

Maintaining Current Levels

- ***Adjustments Necessary to Maintain Current Levels: +$219,523,000 / 0 FTE*** Funds are requested for: FY 2011 cost of the January 2010 pay increase of $47,473,000, the proposed January 2011 pay raise of $119,537,000, the cost of the increase in Federal Employee Retirement System (FERS) agency contribution percentage of $16,392,000, and non-labor related items such as contracts, travel, supplies, equipment, and a GSA rent adjustment of $36,121,000.

Base Adjustments

- ***Resource Adjustment to Support Recovery Act-HCTC Program Expansion: +$3,494,000/ 0 FTE*** This temporary base increase will provide additional contractor funding for the continued support, sustainability, administration, and operation of the HCTC program. Taxpayer participation in the HCTC program is expected to grow because of the Recovery Act. The additional contractor support will allow HCTC to serve a significantly larger participant population.

- ***Technical FTE Adjustments: $0 /-318 FTE*** This adjustment reflects permanent changes made to ensure FTE levels are fully funded in the base budget.

Efficiencies and Savings

- ***Non-Recur Savings: -$32,680,000 / 0 FTE*** This is the net of reductions of non-recurring, one-time costs associated with the IRS FY 2010 enforcement initiatives (e.g., IT equipment and training).

- ***Increase e-File Savings: -$22,808,000 / -472 FTE*** This decrease is a result of savings from increased electronic filing (e-File), which is projected to lead to fewer returns filed on paper in FY 2011. The number of returns filed electronically is expected to increase substantially in FY 2011 with the addition of the recently enacted Worker, Homeownership, and Business Assistance Act of 2009

(Public Law 111-92), which requires electronic filing by all tax preparers filing more than ten returns in a calendar year.

- ***Information Technology (IT) Infrastructure and Process Improvements: -$75,000,000 / 0 FTE*** The IRS will reduce infrastructure costs through process improvements in IT infrastructure. Initiatives such as the Information Technology Infrastructure Library will allow the IRS to improve the quality of IT services. In addition, the IRS is working to achieve a Capability Maturity Model Integrated certification that will yield efficiencies in software engineering.

- ***Reduce Procurement/Contracting: -$25,000,000 / 0 FTE*** In accordance with Presidential guidance on controlling contracting costs, the IRS will generate savings by improving the effectiveness of existing acquisition practices and reduce the cost of contracts.

- ***Reduce Printing, Travel, and Training: -$10,000,000 / 0 FTE*** The IRS will generate savings by reducing agency-wide printing of selected internal manuals, selected training materials, and other items, non-case related travel and non-technical training.

- ***Reduce Tuition Assistance Program (TAP): -$5,150,000 / 0 FTE*** The Tuition Assistance Program provides funding to employees for courses that support both career development and the IRS mission. In FY 2011, the IRS will generate savings by restructuring this program.

- ***Eliminate Selective Mailing of Forms and Publications: -$20,000,000 / 0 FTE*** The IRS will generate savings by eliminating the non-mandated notice inserts; the automatic mailing of Form 1040, U.S. Individual Tax Return, tax packages; and the automatic mailing of business tax products.

Program Reinvestment

- ***Submission Processing Consolidation (Atlanta): +$2,792,000 / 0 FTE*** Increased use of e-File has led to consolidation of the 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 Decrease

- ***Reduce Taxpayer Service Grant and Advocacy Programs: -$9,000,000 / 0 FTE*** The FY 2010 appropriation included an additional $3,500,000 to expand Taxpayer Advocate Service case processing activities; $500,000 to increase the Low-Income Taxpayer Clinic (LITC) grants program; $1,000,000 to increase the Tax Counseling for the Elderly (TCE) grants program; and $4,000,000 to increase

the Volunteer Income Tax Assistance (VITA) grants program. These program decreases will realign the programs to the 2010 requested level to fund the Increase Telephone Level of Service initiative.

Program Increases

- ***Improve IRS.gov: +$25,000,000 / 0 FTE*** This initiative, part of a multi-year plan, will initiate the migration of IRS web content and applications from the current outdated portal infrastructures to a new consolidated IRS web environment. These funds will enable the IRS to complete the first phase of the migration of the taxpayer-facing content and applications and to begin the second phase of the migration and transition of approximately 35 percent of the public and partner-facing applications to the new environment.

- ***Increase Telephone Level of Service: +$20,945,000 / 0*** FTE Recent legislation has led to an unprecedented demand for telephone services over the past few years. In addition, the additional complexity of – and time needed to resolve – many phone calls resulted in a decline in the telephone level of service. This initiative will improve the telephone level of service from a projected 71 percent in FY 2010 to a target of 75 percent in FY 2011 through a program increase of $11.9 million and a $9.0 million reallocation from TAS and the LITC, TCE and VITA grant programs.

- ***Address Business and Individual International Compliance: +$121,086,000 / +781 FTE*** This initiative supports the Presidential priority to address offshore tax evasion and builds on the IRS FY 2010 international enforcement initiative. It will allow the IRS to continue its multi-year investment in international tax compliance activities. It increases coverage of the most strategically important international issues, including large enterprises with international components operated by businesses and investors through multiple interrelated financial and tax entities and high-wealth individuals and the complex business enterprises they control.

  This initiative will increase examinations of additional international issues pertaining to international structures involving tiered pass-through entities, corporations, and high-wealth individuals by a projected 4,864 cases. The increase in examinations will generate $812.2 million in additional enforcement revenue once the new hires reach full potential in FY 2013.

- ***Reduce the Reporting Compliance Tax Gap: +$77,679,000 / +700 FTE*** This initiative will improve compliance by increasing examination of field and correspondence individual return audits by 61,100 annually; business return audits by 1,200; audits targeting employment, excise, and estate and gift taxes by 9,300; and Automated Underreporter (AUR) document matching individual return audits by 234,000. This request will generate $659.6 million in additional enforcement revenue once new hires reach full potential in FY 2013.

- ***Reduce the Nonfiling and Underpayment Tax Gap: +$38,181,000 / +406 FTE*** This initiative will allow the IRS to broaden its collection coverage and address the tax gap more effectively by increasing staff resources for field collection and the Automated Collection System (ACS) program. The additional staff will produce an additional 144,000 tax delinquency accounts (TDA) (i.e., balance due accounts where returns were filed, but the taxes have not been paid) and 22,500 tax delinquency investigations (TDI) (i.e., investigations of taxpayers with unfiled returns who have not responded to a notice). This request will generate $474.4 million in additional enforcement revenue once new hires reach full potential in FY 2013.

- ***Support of Increased Enforcement Activities: +$5,000,000 / +65 FTE*** Most tax enforcement actions result in downstream Accounts Management activities, including account adjustments, assisted phone calls, amended returns, and installment agreement preparation. This funding will allow the IRS to assist taxpayers to resolve issues early in the enforcement process, pay their taxes, and respond to and close out various enforcement actions. Improving the response to taxpayers who have received enforcement notices should increase revenue and reduce interest paid.

- ***Maintain Recovery Act Staffing: +$5,500,000 / +31 FTE*** Among other responsibilities, the IRS is mandated by the Recovery Act to administer the new bond provisions. The Treasury is required to issue a direct payment to the bond issuer. The unique nature of this new role requires continuous compliance reviews and verification throughout the administrative life of the bonds. This initiative will extend IRS staffing resources received in the Recovery Act to administer ongoing Recovery Act bond provisions.

- ***Business System Modernization (BSM): +$167,585,000 / +156 FTE*** The BSM increase is a top priority for the IRS and will allow the completion of the new taxpayer account database for the 2012 filing season. The new taxpayer account database will result in faster refunds for taxpayers, improve service accuracy and timeliness, and enhance data security. Completion of the taxpayer account database is a prerequisite for other major initiatives such as significant expansion of online paperless services and next-generation enforcement technologies. The ability of the IRS to support increasingly complex taxpayer service and compliance initiatives will be severely limited until it is completed.

Legislative Proposals

The FY 2011 President's Budget includes a number of legislative proposals intended to improve tax compliance with minimum taxpayer burden. These proposals will specifically target the tax gap and generate nearly $26 billion over the next ten years. Among other proposals, the Administration proposes to expand information reporting, improve compliance by businesses, strengthen tax administration, and expand penalties.

Expand information reporting – Compliance with the tax laws is highest when payments are subject to information reporting to the IRS. Specific information reporting proposals would:

- Require information reporting for private separate accounts of life insurance companies;
- Require information reporting on payments for services to corporations;
- Require a certified Taxpayer Identification Number (TIN) from contractors;
- Require increased information reporting on certain government payments;
- Increase information return penalties; and
- Require information reporting on expense payments relating to rental property.

Improve compliance by businesses – Improving compliance by businesses of all sizes is important. Specific proposals to improve compliance by businesses would:

- Provide Treasury regulatory authority to require that information returns be filed electronically;
- Require corporations and partnerships with assets of $10 million or more that are required to file Schedule M-3 to file their tax returns electronically;
- Provide Treasury regulatory authority to reduce the current threshold for requiring electronic filing (250 or more returns filed during a calendar year) and include certain other large taxpayers not required to file Schedule M-3 (such as exempt organizations;
- Implement standards clarifying when employee leasing companies can be held liable for their clients' federal employment taxes; and
- Increase certainty about the rules pertaining to classification of employees as independent contractors.

Strengthen tax administration – The IRS has taken a number of steps under existing law to improve compliance. These efforts would be enhanced by specific tax administration proposals that would:

- Expand IRS access to information in the National Directory of New Hires for tax administration purposes;
- Make repeated willful failure to file a tax return a felony;
- Facilitate tax compliance with local jurisdictions;
- Extend statutes of limitations where state tax adjustments affect federal tax liability;
- Improve the investigative disclosure statute;
- Repeal the requirement of a partial payment with an application for an offer-in-compromise;
- Allow assessment of criminal restitution as tax; and
- Codify the "economic substance" doctrine.

Expand penalties – Penalties play an important role in discouraging intentional noncompliance. A specific proposal to expand penalties would:

- Impose a penalty on failure to comply with electronic filing requirements; and
- Clarify that the bad check penalty applies to electronic checks and other forms of payment.

Improve Tax Administration and Other Miscellaneous Proposals

The Administration has put forward additional proposals relating to IRS administrative reforms. These proposals would:

- Improve the foreign trust reporting penalty;
- Apply the Federal Payment Levy Program to contractors before providing Collection Due Process; and
- Clarify that a vendor levy on "goods and services" would not exclude "property."

Conclusion

Mr. Chairman, thank you again for this opportunity to provide testimony on the 2010 filing season and the President's FY 2011 Budget for the IRS.

The IRS continues to demonstrate improvement in key areas, including service, and the ability to react effectively and quickly to evolving situations, such as the economic downturn, and make a meaningful difference in taxpayers' lives.

We also urge passage of the President's proposed FY 2011 Budget for the IRS. It gives the IRS much needed resources to provide taxpayers with high quality customer service and bolsters IRS enforcement in critical areas, such as unlawful offshore tax evasion. It also makes wise investments for the next generation of technology and the IRS workforce. I also urge this Subcommittee to support the enactment of the legislative proposals included in the Budget to improve compliance. That concludes my testimony. I would be happy to answer any questions.

Chairman LEWIS. Mr. Commissioner, thank you for your statement. And as Chair of this Subcommittee, and the Ranking Member and I think all Members of the Subcommittee and our Full Committee, will do our part in explaining the role of the Internal

Revenue Service, all of the employees, in doing the job that they are authorized and committed to do. So thank you again for your service.

At this time we will open the hearing for questions. I would like to remind members that we will follow the Givens rule for questions. And I ask that each member be brief and abide by the five-minute rule.

Mr. Commissioner, are you concerned that there has been an increase in the number of extensions and the use of credit cards to pay taxes this filing season? What advice does the IRS have for taxpayers in financial distress this filing season?

Mr. SHULMAN. You know, we haven't seen any major trends that are troubling to us thus far. I think the advice I give people this filing season is similar to other advice, with one caveat, given that there are more people unemployed than in the past who may be unable to pay their tax obligation.

I mean, in general we tell people, pay on time. If you can't pay on time, still file a return and we will work with you. We are encouraging people to electronically file and direct deposit because if you do, you can get your refund in ten days, get cash into people's pockets.

I think the important thing for this year is, you know, I have instructed all of our people in all of our operations, especially our collections operations where people have—are actually owing the IRS money and due to the government, that we need to—while we need to collect the money needed to fund the government, we also have to meet each taxpayer based on their individual circumstances.

And so the best advice I can give people is if they can't pay, they should still file. They shouldn't disappear. They should call us. Our people can work with folks. They can put them on an installment plan. If they qualify, they can get an offer in compromise. We can work through people's issues with them, and it is important for people to remember that.

Chairman LEWIS. Mr. Commissioner, I notice that the budget proposal shifts $9 million to toll-free telephone assistance from low-income services such as the VITA program and low-income taxpayer clinics.

Would this affect the IRS' service to low-income taxpayers?

Mr. SHULMAN. As you know, Mr. Chairman, we are in tight budget times, with deficits higher than the President would like. He asked every agency to try to be as efficient as we could and make a series of tradeoffs.

That budget tried to do that. Our telephone service serves a number of low-income, elderly citizens, and so it wasn't where we wanted it to be. Some money was shifted from the VITA, the low-income taxpayer clinics, et cetera. I think it is a very reasonable discussion to debate whether that should be shifted or not.

Chairman LEWIS. Thank you. Now I turn to the Ranking Member, Dr. Boustany, for his questions.

Dr. BOUSTANY. Thank you, Mr. Chairman.

Commissioner Shulman, with regard to the increase in average refund that I referenced in my opening statement, can you share with us evidence that you might have that the higher utilization of stimulus tax credits is driving the refund data?

Mr. SHULMAN. So I was listening closely when you gave your opening statement, and hadn't—not familiar with the analysis you did around employed/unemployed. You know, there are a number of things going into refunds, including 1.4—or almost 2 million people have gotten the first-time home-buyers' credit already, which is $7500, which clearly increases refunds. The Make Work Pay credit, most Americans are getting $400, or $800 if they are a married couple. I would be happy to work with your staff afterwards and give you our analysis.

Dr. BOUSTANY. I appreciate that because it would seem to me that some who—or perhaps many who started the year with a certain level of income and saw a decline over the course of the year and had withholdings on the front end, that could be a major factor in driving up the percentage of their—of refunds, or the increase that we have seen. So we would like some data just to sort of, you know, really dig into that, to understand what is going on, in the interest of oversight.

And before I get—I have a couple of health care questions. But in a previous subcommittee hearing, we talked a lot about the first-time home-buyer tax credit, and some of the fraud issues. I know we have worked with you to address this problem to help with tools that you might need.

And could you give us an update on the correction of some of the problems we were seeing with that tax credit?

Mr. SHULMAN. Yes. I mean, the first thing I would say, any time there is a very short term for implementation, narrow window, and a $7500 or $8000 credit, you are going to see fraud.

What we try to do is balance getting the money out to people, where the intent was to get money to people to help stabilize the home market and help them buy a home, and minimize fraud. An important tool for us is to have math error authority. And so we had no authority if we saw an indicia of fraud to actually stop and change your refund. We either had to do a full-blown audit, which can take time; stop a refund, and sometimes stop a refund from someone if we find out that the indicia doesn't come through; or we needed to put the refund out and not do anything.

We came back and asked Congress to give us audit authority, which they did, or math error authority, which was very important. We have also now asked for more documentation from home buyers, to see actual closing documents. And so some of the past problems, we think, are solved.

I will tell you we have taken a major number of audit resources and shifted them to first-time home-buyer credit. We have shifted—we probably, by the end of this year, will have opened 200,000 audits to make sure that there is not fraud in that program.

Subsequently, Congress passed a second first-time home-buyer credit bill that also had a—people who had owned their home for five years, lived in it for three consecutive years, et cetera. That is going to cause similar issues for us.

And I think it is important for people to know, when there are short-term things and use the IRS to stimulate the economy, we are going to do our job. We are going to be a distribution mechanism. But there is also opportunity for fraud, and we are going to have to make those tradeoffs and resource tradeoffs.

Dr. BOUSTANY. Thank you. And going to health care now, I referenced the premium tax credit and how it will go directly to insurance companies. Is it true that those taxpayers who do receive this premium tax credit will not actually see the money in their refund checks, but rather the IRS will send tax dollars directly to the health insurance companies under the new law?

Mr. SHULMAN. Let me just say something about kind of our role around health care. You know, our role is to administer the tax portions of the health care law. And I really think of us as, you know, the payor bank that needs to process and do lots of financial transactions around that to make sure the benefits are going to the right place.

My understanding is—if you are talking about the tax credits to help people buy insurance, yes, my understanding is that we are going to try to work that out in a way that is the most efficient for the system.

I think the law contemplates that people will work through the exchange. The exchange will give us whatever information is needed. And instead of them sending money to the health care provider, that money will be sent directly.

Dr. BOUSTANY. All right. Thank you. And one final question, Mr. Chairman, if you don't mind.

The CBO came out with some estimates, and the figure of $10 billion over the next decade in additional funding was cited, on top of the base budget, to carry out the new authorities that you are going to need to deal with the new health care law.

Do you agree with this estimate, or have you done some internal work? Were you consulted on this?

Mr. SHULMAN. We were not consulted by CBO. That is their estimate. Their tradition is to come up with their own estimates of administrative costs. But that is—I think it is 5 to 10 billion is the number that is accounted for in the overall cost of the legislation.

What we do is watch legislation. Clearly, we have been involved in planning. Now that the legislation is passed, I have a staff working on the actual numbers that it will cost for us to implement the tax portion of the health care bill. And we will be coming up with those numbers, you know, as quick as we can.

Dr. BOUSTANY. And given that a lot of these provisions don't go into effect until 2014 that affect the agency, so this is really a six-year figure, in effect.

Mr. SHULMAN. Again, it is a CBO figure, so I don't know how they came up with them.

Dr. BOUSTANY. Okay. Well, one final thing. You mentioned the additional resources going into dealing with the first-time homebuyer tax credit. And I just want to express my deep concern about the resource demand on IRS as this new law is implemented. And we will work hopefully very closely with you to examine those requirements.

Mr. SHULMAN. Yes. No, what is interesting about the tax system is, over time, it has become a very efficient distribution mechanism, not just in this country; all tax authorities are asked to do things. We have proven quite adept at it, with the stimulus checks under President Bush, Recovery Act under President Obama, the earned income tax credit we have administered for years.

As the head of the agency, the important thing for me is to be given plenty of leave time, being given administrative flexibility, and then being given the right resources to implement it. And so I feel very confident we can implement well what Congress passes, given that we have those three things, which I have confidence we will have in the case of the health care legislation.

Dr. BOUSTANY. We shall see. Thank you.

Chairman LEWIS. Thank you. Now we turn to Mr. Davis for his questioning.

Mr. DAVIS OF ILLINOIS. Thank you very much, Mr. Chairman, and thank you, Commissioner, for being here.

Following up a little bit on the question just raised by my friend from Louisiana, would this also count as jobs being created, the number of additional employees that you might need for Internal Revenue Service?

Mr. SHULMAN. You know, I don't know. Sure. If there are jobs, you know, if I hire someone, that is a job in the Federal Government. I think generally the President's approach has been to have jobs bills focused at the private sector, growing small businesses, growing the economy that way.

Mr. DAVIS OF ILLINOIS. Well, I think a job is a job, especially if it is one that is needed, and it becomes part of the job creation.

But let me ask you: There is some concern about how helpful the Service is being to low-income taxpayers, given that we are in the season, earned income tax credits and those kinds of things.

Could you explain how impactful you think the Service is being right now for low-income taxpayers?

Mr. SHULMAN. Sure. We are very focused on trying to do outreach, help people get their returns prepared, work with volunteer organizations across the country. My belief is, you know, while we are a large financial service organization for many people, we are not like a financial service company who gets to choose its customers and decides which customers it wants to serve and which it doesn't want to serve. We need to serve every last taxpayer, and we need to serve them well.

And so some people want internet service. Some people are going to go hire an accountant. But often elderly, lower-income taxpayers need specialized help by the IRS. We have low-income taxpayer clinics which can help people resolve issues, which we fund.

We have an extensive VITA program, which is the Volunteers in Tax Administration, where we train people, give them computers, et cetera. Our biggest VITA partner is AARP, but we work with any number of nonprofits across the country, 10,000 sites.

We have tax clinics for the elderly. We do earned income taxpayer outreach events. One was done with the Chairman; we would love to do it with other folks. We have taxpayer assistance centers all over the country.

If a low-income taxpayer clearly can't meet their obligation, I mentioned in my opening statement, we have some special programs like an offer in compromise program. We are adjusting that during these really difficult economic times. We are holding a thousand open houses, where people can come in and get their tax problem resolved.

You know, we do have limited resources, and we need to balance the resources across all of our demands. But I think that this agency has a special obligation to meet people who can't afford an accountant or don't have a computer to use tax software. So we have got a number of programs, and we spend a lot of time, a lot of effort, on outreach, education, and service.

Mr. DAVIS OF ILLINOIS. There has been some concern in the past about the ability of people who are incarcerated to perpetuate scams in terms of filing, getting checks, having relatives and friends cash them.

Can you give us an update on how that has been handled?

Mr. SHULMAN. Yes. You know, before I came into the job, I know this was a major focus. The IRS has stepped up its efforts working with state and federal law enforcement agencies, prison systems, et cetera, to make sure we can try to match and make sure that someone incarcerated isn't perpetrating fraud.

Sometimes, I will tell you, though, someone was employed for half a year, is then incarcerated, and actually can file a return from prison. So that happens.

The big problem, sir, really, at the end of the day, is now if someone perpetrates fraud, the biggest penalty we can have is we have—they are under criminal investigation and they go to jail. Once somebody goes to jail, that penalty has already been taken care of. And so the question is: When someone perpetrates fraud in jail, what is the penalty for them?

We also have limitations around we can't share with the warden someone's tax information because of tax privacy laws. And so we think we have made great progress. It is never going to be fully eradicated. But, you know, we have been quite focused on this.

Mr. DAVIS OF ILLINOIS. Thank you. Mr. Chairman, can I have a second here? I have got—there is some concern that has been expressed by secondary filers that your computer system may not pick up the information as readily. I will submit that in writing, and see if we can get a response to it.

Mr. SHULMAN. Absolutely.

Mr. DAVIS OF ILLINOIS. Thank you. Thank you, Mr. Chairman.

Chairman LEWIS. Thank you.

Now we turn to Mr. Etheridge for his questioning.

Mr. ETHERIDGE. Thank you, Mr. Chairman.

Mr. Shulman, thank you for your testimony. Thank you for being here this morning.

Let me just mention an issue with IRS that is very pleasant. Last month I was able to participate in an IRS free file event that we held in North Carolina at Fayetteville Tech. And I was pleasantly surprised.

We had over 20 community-based organizations, and roughly 60 students and a number of families from Fort Bragg, which is, as you probably know, right adjacent there and a large installation. They came and used the free file system that you are working with. And North Carolina is a free file state, as you probably know.

So let me thank you and all your people who were able to help because this is a great process between the federal and the state,

doing taxes online for free. And I personally enjoyed it. I think the folks there really appreciated the outreach and the help.

And let me just congratulate you because I am glad that you have now signed, I think, a new five-year deal with the Free File Alliance to provide this service to the American taxpayers. And I think that is a great help to people who really don't have a real sophisticated—but it helps them get it done quickly. They can do it online and get the returns quickly. So I congratulate you on that.

Let me move to another point now because I am pleased that you mentioned the HIRE Act in your testimony a little while ago. And I know that these credits are going to and can make a big difference for businesses. And I think it will help our economy grow.

But one of the biggest criticisms of the 1977 to 1978 Tax Credit Act was that folks didn't know about it, or at least said they didn't. I was in business, happened to know something about it, and used it.

But my question to you this morning is: What has IRS done and what are you doing to make sure through groups that businesses are aware that this is available to them and can use it to their advantage?

Mr. SHULMAN. Thanks for the question. So we immediately, you know, put out press around this, worked with press offices around the country. Frankly, the whole administration is mobilizing around this, is supporting it.

And so, you know, sometimes a tax provision gets passed and the IRS publicizes it. Now, you know, we have got the advantage of important jobs acts. We have got the White House. We have got the Treasury. Everybody is mobilized to get the word out.

We are also working with practitioners. Most small businesses use an accountant or a tax preparer, someone else to work on their taxes. And so we are getting the word out through our extensive practitioner network, which is important, and the payroll providers. A lot of people, you know, do the payroll tax through the payroll providers, and so we are holding regular conference calls. We are pushing that information out.

I would also note, in the health care legislation, the first thing we are going to need to implement is a tax credit for small businesses who put—to help them offset their costs of providing health care to their employees. And so we are immediately mobilizing around that effort.

Mr. ETHERIDGE. And how much is that? How much is that?

Mr. SHULMAN. It is 35 percent——

Mr. ETHERIDGE. Thank you.

Mr. SHULMAN [continuing]. Now and it will go to 50 percent, I think, when it is—you know, by 2014.

Mr. ETHERIDGE. And what is the starting date on it?

Mr. SHULMAN. Starting date was last January 1, so it is for this tax year.

Mr. ETHERIDGE. Thank you. One other question. I just think it helps to get—every time we get an opportunity to get it out, we need to remind folks when it is.

As you know, many Americans are struggling, and that is why we are doing many of the things we are doing. And I think all of us talk about our experiences, and certainly, as you know, North

Carolina is really above the national average in terms of unemployment, which is a little unusual for us in our state. I have counties in my district where it is approaching 15 percent.

So my question is, I guess, what additional steps can we take and are you able to take to help make folks know what tax cuts that have been passed are available to many of these people? You have talked about it some already. And how can taxpayers reduce their taxes currently as a move forward?

Because I think—I notice that you talked about compromise, and that the IRS offers in its compromise, it dropped to about 72 percent during the last administration. Is this a measure that you plan to implement more often as we move into these very difficult times we now have?

Mr. SHULMAN. So a couple things. We actually just started a program this month where we are partnering with state unemployment offices to promote the tax credits people can get, to promote our open houses, et cetera.

And so recognizing that unemployment is a problem everybody is trying to tackle, we are actually going to the unemployment offices so when people show up there, they will be able to get IRS literature. They will be able to understand that they should claim the Make Work Pay Credit. If they get out of work, they can get a COBRA subsidy, things like that.

We are also letting them know about the changes in offers in compromise, the open houses. We are publicizing in state unemployment offices at a local level. And so we are going to go the extra mile.

I mean, we have this fine line to walk. I mean, I am responsible to raise all the money to fund the government. And people who can pay need to pay, and we need to run our programs for that. But again, we also need to walk in taxpayers' shoes.

And if you are struggling and trying to put food on the table and have medicine and put your kid through college, if we can be helpful and use our flexibilities to help people through this tough time to keep them, you know, in good financial condition for the long term, for their own benefit and also to be taxpayers, that is good for the IRS and it is good for them.

On offers in compromise, that program has declined dramatically. I think it is a good program. We are looking very hard at what we can do to reverse this. I think the single most important one is one that I compliment the Chairman and the rest of the committee for supporting, which is repealing the 20 percent down payment, which came into effect at about the same time this started plummeting. I don't think there is any reason people should have to put a 20 percent down payment when, by definition, they are having a hardship situation.

We are also looking to see when in the collection process is the appropriate time to introduce it. How can we streamline the program, potentially have some online tools so people can go in and figure out if they are eligible. And so I actually have a whole team looking at this because I think it is a program that is under-utilized. I would like to figure out how to get the utilization back up.

Mr. ETHERIDGE. Mr. Chairman, thank you for your time and your patience because we do want everyone to pay what they are

due to pay but, you know, fairness to help those who need help, too. Thank you, sir, and I yield back.

Chairman LEWIS. Thank you.

Now we turn to Mr. Kind for his questioning.

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

Mr. Shulman, thank you again for being here to testify. We appreciate the job you and everyone at the IRS does on behalf of the country.

You know, Dr. Boustany raised the issue of the health care reform bill, and I think there is a lot of misinformation and a lot of misperception about the role that the IRS is going to play in the implementation of the recently passed health care bill. So let me ask you a series of questions, and as much as you can, just answer yes or no to clarify some questions that I have about the exact role that the IRS will play.

The health care bill that was just signed by the President is not going to fundamentally alter the relationship of the IRS with the American taxpayer, will it?

Mr. SHULMAN. No.

Mr. KIND. And you said that right now you are moving forward as far as doing calculations as far as the costs and the staffing needs that the IRS has. But you haven't made any of those final determinations yet, have you?

Mr. SHULMAN. That is correct.

Mr. KIND. And the IRS agents are not going to be going out and auditing taxpayers to verify if they have obtained acceptable health insurance, will they?

Mr. SHULMAN. No.

Mr. KIND. In fact, it is going to be the insurance companies that will be merely certifying whether or not an individual has obtained health care coverage. And they will be certifying that to the IRS?

Mr. SHULMAN. Yes. Let me—it is probably worth me just——

Mr. KIND. Sure.

Mr. SHULMAN [continuing]. Being very clear because I think there have, you know, been some misconceptions out there.

The way we envision this working is HHS, Department of Health and Human Services, and the exchanges will be working with the insurance companies to determine what is acceptable coverage. All that will happen with the IRS is similar to a current 1099, where a bank sends the IRS a statement that says, here is the interest someone has, and they send it to the taxpayer.

We expect to get a simple form that we won't look behind that says, this person has acceptable health coverage. There are not going to be any discussions about health coverage with an IRS employee.

Mr. KIND. In fact, I would envision that the major role the IRS will play is trying to get information into the individuals' hands and businesses about the various tax incentives that the health care reform bill has, and how they can best access those incentives and utilize them. Is that right?

Mr. SHULMAN. Yes. I mean, the role of the IRS is going to be, again, the tax portions of this, not the health portions of this. And what we are going to do is try to make sure people are educated. There is information. We process payments quickly. We also will

make sure that there is no fraud and abuse in the system, as we always do.

Mr. KIND. So the IRS is still going to pick up the phone and answer questions in regards to tax incentives under health care bill?

Mr. SHULMAN. Yes.

Mr. KIND. And I assume the IRS will try to build some type of online education service, too, for people to access as far as what they are eligible for?

Mr. SHULMAN. Absolutely.

Mr. KIND. And you will probably be performing some additional outreach services with businesses and taxpayers about the health care bill?

Mr. SHULMAN. Absolutely.

Mr. KIND. And as you indicated to Mr. Etheridge, you are already moving forward on the 35 percent tax credit that small businesses are going to be getting this year already with the enactment of the health care bill?

Mr. SHULMAN. That is our first move.

Mr. KIND. And no taxpayer is going to be subject to any IRS liens or levies or jail time for failing to disclose insurance requirements to the IRS?

Mr. SHULMAN. That is what the legislation calls for, yes.

Mr. KIND. And as soon as your internal review is done, I assume you are going to report back to Congress what type of resources you will need for staffing or for additional funds in order to implement the health care bill?

Mr. SHULMAN. Yes. I do want to be clear, as I was with Mr. Boustany. We will need resources to implement the tax provisions in this legislation. And we will look forward to working with the committee to make sure we have the proper resources to serve the American people.

Mr. KIND. Thank you. And let me just ask you a final question, that reports are coming out that there is roughly a 10 percent increase in the average return for taxpayers filing. And I think you have indicated and made public statements that that in large part is attributed to the various tax relief that taxpayers are receiving under the American Recovery Act. Is that your opinion?

Mr. SHULMAN. Yes. I mean, clearly the Recovery Act is a major portion of that.

Mr. KIND. So more money in taxpayers' pockets during this tough economic time due to the Recovery Act. And the only proviso to that is that the returns coming in are a little bit slower. And so we don't have the complete returns, or even the typical number of returns, at this point of the year. Is that right?

Mr. SHULMAN. Yes. It is 3 percent down. We have about half the tax returns have come in at this point, which is more or less average. It is a small decline, but it is not statistically significant.

Mr. KIND. The number that I am looking at here, that in 2009 the average tax return was about $2,770. But now in 2010, that jumped up to $3,036, so roughly a $266 additional refund to the average taxpayer.

Does that sound about right to you?

Mr. SHULMAN. That is the current run rate, yes.

Mr. KIND. Great. Thank you, Mr.——

Dr. BOUSTANY. Would the gentleman yield?

Mr. KIND. Yes. I would be happy to yield.

Dr. BOUSTANY. Just for clarification on the health care issue, Commissioner, could you talk to us about the compliance side with regard to the individual mandate? Obviously, in terms of being able to enforce compliance, what is going to be your role with regard to any penalties paid in this?

Mr. SHULMAN. Yes. So my understanding of the bill—and again, you know, this is a bill that some of it has passed; a big portion has passed, but there are still some, you know, pieces of the reconciliation which adjust things—you know, the insurance company will send to us whether or not somebody has coverage or not. People will do their self-filing, as they always do.

If they file, they will—if they file, and they have to have insurance if they have money to have insurance, so not everybody has a requirement, as I understand it; there is also an exception for lower-income people who can't afford insurance—it will come in and they will adjust their tax rate, and based on whether they have insurance or not.

And the Tax Code is used, and the tax return is used, as the financial incentive around this. So our role will be people will either pay their taxes or not. If they don't pay their taxes, then they will get a letter from us saying what you owe.

Mr. KIND. Mr. Chairman, just one last question, reclaiming my time.

Just so we are clear, there is no mandate for individuals to have to go out and purchase insurance under the health care bill. They can choose to purchase insurance. But if they don't, we are going to be asking them to contribute a little bit so that if they do get sick or injured and they do go into the emergency room, that those costs aren't going to be passed on to people who are paying for insurance or swallowed by the health care providers themselves.

But it is going to be an individual choice whether they want to have insurance or not. But if they don't, for the first time we are asking them to contribute a little bit so that the cost of the uninsured isn't passed on to Americans who have insurance in our current system.

Thank you, Mr. Chairman.

Dr. BOUSTANY. If the gentleman would yield?

Mr. KIND. My time is expired.

Chairman LEWIS. Thank you.

Now we turn to Mr. Becerra for his questioning.

Mr. BECERRA. Thank you, Mr. Chairman.

Commissioner, good to see you. Thank you for being here. And I want to congratulate you and offer you our support—I won't say condolences, but support. Because condolences, support, are required because you are now going to be tasked with additional work to try to make sure that the $40 billion in tax credits, tax cuts that small businesses will receive under this health care bill, and the close to around $400 billion in tax cuts that individuals will receive to help them cover the cost of health insurance because of their tax credits, will be administered through your shop.

And so support because we need to make sure that you do this well, and condolences because we always expect you to do more

than is humanly possible, given the time and the resources that you have. So make sure that it is more support than condolence that we ultimately give you in that regard.

Mr. SHULMAN. I will ask of that, sir.

Mr. BECERRA. Absolutely, and please. The last thing I think anyone in this committee would like to see is that we delay the ability of Americans to purchase affordable and quality health care simply because we are unable to get them their credits, tax credits, quickly enough. So let us know how we help you administer this as you go on and do your business.

I also wanted, as I said, to congratulate you because you just issued regulations on something I think is very, very important for those of us who represent a large population of middle class and modest income families.

What you issued recently as regulations is critical, saves hundreds of dollars, in some cases thousands of dollars, and perhaps lots of headache for a lot of these families that end up filing returns using tax preparers and thinking that they have now done the right thing by using a tax preparer, who should be more skilled and knowledgeable on the preparation of tax filings.

And yet they find out that they were either incorrect in their filing or they were duped in their filing, and certainly in many—and too often in the cases that they were overcharged for the filing.

And so I wanted to just make sure I understand what your regulations call for that are now out there for consideration and comment. It is the case—it is the case today that just about anyone can put out a shingle and say, I will prepare your taxes and charge any amount. In fact, in most states there is more regulation over who cut your hair or my hair than there is over who prepared your taxes or my taxes.

And you issued some regulations to try to help us provide some sanity within this industry because more often than not, we find Americans who could have filled out the simple 1040 form being charged hundreds of dollars to do what could have been done by a basic computer program, or perhaps the person by himself or herself, just reading the basic instructions of the IRS instruction manual.

And so I am hoping you give me a quick synopsis of what your regulations are proposing.

Mr. SHULMAN. Sure. So we put out a report which gave a road map over about three years of moving from a place where we largely have minimal oversight over tax return preparers to really trying to bring a minimal level of competency to all tax return preparers. We think there are about a million of them. We think that is a good, efficient use of leveraging our resources for service and effort.

The basic road map is this. People will have to get an identification number if they prepare returns, which we call a PTIN in those regulations we just put out yesterday. And we are hoping to get the PTINs up and running for next filing season.

Next, people will have to take a minimum competency exam, basically that they can do a 1040. And then we are looking at doing a small business exam, too, to make sure small businesses are receiving the same level of service.

They will have to have continuing education, which is general tax education except for some of that will have to be ethics and some of that will have to be tax law changes; because of the pace of tax law changes, it is an important thing where people can make mistakes.

We will then put a database out. This will come down the road, once people take the test and have continuing education responsibilities, so the American people can look up and say, are they working with a registered return preparer, give them some level of confidence, their working with them.

And then we are going to shift some oversight and enforcement resources into this area because there will be people who go underground, and we want to find them and make sure they are not preparing returns.

And so that shift will happen over time. But immediately, we actually did thousands of visits to preparers this season to remind them of their obligations. We sent out 10,000 letters to remind people of their obligations. So we are already starting to make that kind of education and enforcement shift.

Mr. BECERRA. And let's be clear. The legislation I have, which would move in the direction that you are proposing in your regulations, and I believe the regulations you have issued, would not apply to a tax accountant or an attorney who we already can tell, from their education and their work experience, are prepared or are versed in the preparation of tax filings.

This is for folks who we are not certain what type of educational background they have, what type of experience they have. And so what we are trying to make sure is that there is level of competency that gives them the right and the opportunity to go out there and sell themselves and tax preparers.

Mr. SHULMAN. That is correct. We exempted people who already have a professional competency test, a minimal level of competence. They need to prove ongoing education—attorneys, enrolled agents who are enrolled with the IRS, and CPAs.

With that said, I did say that over the next couple of years, once we start tracking people, we are going to see and be able to see what differences there are between the accuracy of returns. And it is something we are willing to revisit if, you know, we go down the line.

But we didn't think we should put an extra level of requirements on a group that already has requirements.

Mr. BECERRA. And, Mr. Chairman, one final question, if I may.

Commissioner, when we say we are going to require this competency of people who prepare these forms, someone could try to get away by saying, well, I am the one that signed the form, but I have a shop of people who help prepare these.

How do you make sure that the people who actually do the preparation will be required to have the competency so that we make sure that someone can't try to skirt this new regulation by saying, I signed it, I prepared it, yet in fact they have a whole bunch of folks who don't have experience who are actually doing the work?

Mr. SHULMAN. There are a couple of things. One is we want to make sure the people you are talking about, who are sitting in a shop actually coaching taxpayers through their return, helping

them with their return, get registered. We also don't want to make someone who is a front office receptionist, who takes tax returns and types in the information and doesn't use any judgment calls and doesn't have any conversations with the taxpayer—we don't want to put the requirement on everyone who ever touches a return.

And so we have tried to craft these regulations carefully. One is, you know, if someone is sitting there and you think they walked you through your return and they are your preparer, then they are going to need to sign.

We can usually see—there is usually a threshold number of what is humanly possible as far as sending in returns in a time basis. So if we see somebody sending in, you know, a couple thousand returns under their name, we are going to send somebody out to see, you know, who is really doing all those returns.

We will also be doing, you know, random blank audits of folks. And we will also be looking for lots of mistakes. And so we will be putting in place compliance programs on the back end around this requirement.

Mr. BECERRA. Commissioner, thank you. Chairman, thank you.

Chairman LEWIS. Mr. Commissioner, thank you for your time and for your testimony. We wish you well. The Subcommittee appreciates your views, and we look forward to another meeting with you in the days and months and years to come.

Also like to thank the staff on both sides of the aisle for your help on this hearing, and thank the Ranking Member and all of the Members for attending.

There being no further business, the hearing is now adjourned.

[Whereupon, at 10:57 a.m., the Subcommittee hearing was adjourned.]

[Submissions for the Record follow:]

Submission for the Record:
Hearing on Internal Revenue Service Operations and the 2010 Tax Return Filing Season held on March 25, 2010

Committee Members:

I am the case that puts the lie to the Commissioner's testimony of March 25, 2010 before the House Ways and Means Committee. Recognizing the "critical role that the IRS plays in the nation's economy," Commissioner Shulman boasts that accuracy rates for customer tax law questions remain in the 90-plus percentile; that IRS employees will be allowed to consider a taxpayer's current and future income when negotiating offers in compromise; and that funding will be used to carry out a robust and targeted enforcement program, to improve tax compliance and enhance workforce development.

Before discussing the critical role the IRS has played in destroying the nation's commercial fishing industry, let me state that I am also the poster child for the failure of the Internal Revenue Service Restructuring and Reform Act of 1998. On the very same day that the head of the IRS was testifying before the Committee, I was summoned before a Revenue Officer to be told that my principle residence was going to be seized, that he did not need judicial approval to do so (IRC § 6334(e)), that all fishermen are self-employed (IRC § 3121(b)(20)), that he has never heard of the boat reporting law (IRC § 6050A), that an offer in compromise is not an option, and that IRC § 3403 doesn't apply to me. Obviously the IRS is still being allowed to pick and choose what laws they will enforce, and against whom. As a twenty year veteran of the agency, he proudly told me that I would be his first home seizure since 1998.

Fishing boat captains and crew were determined to be employees of the boat owner by the U.S. Supreme Court in 1970 (United States v. Webb, 397 U.S. 179). As a result of the Court's decision, the Internal Revenue Service assessed boat owners for the federal income and social security taxes they owed on their employees. Rather than pay the taxes they claimed would bankrupt them, boat owners successfully lobbied Congress for the passage of IRC § 3121(b)(20) of the Tax Code in 1976, which excepted from employment, for tax purposes only, services of fishing boat crewmen and captains whose terms of employment conformed to the guidelines enumerated in the new law. To ensure compliance with the guidelines, Congress required boat owners to report the distribution of shares for each voyage to the IRS, IRC § 6050A, aptly titled, reporting requirements of certain fishing boat operators.

My discussion with the IRS concerning the employment status of commercial fishermen began in 1988 when my former husband, a commercial fisherman, was fired from a job because he objected to a certain deduction to a trade association the boat owner was taking from the gross proceeds of the trip prior to apportioning shares to the crew. It took me nine years to get the agency to issue a technical advice memorandum which still failed to address all the applicable laws and regulations concerning the employment status of fishermen. However, my ex-husband was determined to be an employee for tax purposes for tax years 1994, 1995, and 1996 by the IRS. Those employment tax liabilities have led to the proposed seizure of my house. I was never

his employer.

As previously mentioned, I have been told that there is no “boat reporting law.” Congress insisted that "in order to permit the Internal Revenue Service to maintain a method of insuring that the crewmen to be treated as self-employed correctly report their income to the IRS, the amendment also requires boat operators to report the identity of the self-employed individuals serving as cewmen, the weight and type of the catch distributed to each crewmen, or, in cases of distributions of proceeds of the catch, the dollar amount distributed to each crewman. The operator is also to report the percentage of each crewman's share of the catch, as well as his own percentage." (General Explanation of the Tax Reform Act of 1976).

To enable the IRS to follow the money paid to the “self-employed" crew, and to ensure that those crew were truly “self-employed,” boat operators were required to file information returns, form 1099-F, stating the percentage of the operator's and each crewman's share of the catch, and the type and weight of the share or the dollar amount received. Compliance could be confirmed if the percentages added up. Simply put, in order to establish self-employment status of the workers, the percentages everyone received over the course of the year must add up to 100%. When deductions are taken from the proceeds of the trip prior to calculating shares, the percentages will not add up to 100% at the end of the year. Self-employment status cannot be confirmed - the workers are employees.

In the mid 1980's the money trail was abandoned and the 1099-F's disappeared, but IRC § 6050A and Treas. Reg. § 1.6050A-1 remain intact. Now the IRS, unencumbered by a paper trail, simply treat all fishermen as self-employed. The question is, why? And by whose authority? Certainly not Congress’s, because the laws have not been changed.

When the law was enacted in 1976, it was estimated that the revenue loss would be $13 million annually. Perhaps the IRS Commissioner could tell the taxpayers what the true cost of the agency’s failure to monitor tax compliance in the fishing industry is now. How much damage to the industry has been caused by what is nothing less than an unauthorized IRS subsidy - in the form of a reprise from the burden of employment taxes - which has undoubtedly kept marginal fishing boats in the fisheries because the IRS illegally subsidized their labor costs?

Not only are the crews being forced to pay the employer’s share of FICA tax, they are also being forced to subsidize the boat owner’s expenses in order to stay employed. The IRS claims it has no restrictions on the type or amount of deductions that can be claimed by the owner as a trip expense to be paid for by the crew. Hence, the boat owner’s dues to trade associations, some of whom finance and employ some of the nation’s Fisheries Management Council Members who determine who will and will not be allowed to fish, can be paid for by the crew who receive absolutely nothing, or lose their jobs, when the management councils dole out quotas for the right to fish the nation’s waters. As in my ex-husband’s case, anyone who complains about the deductions or the boat owner’s failure to comply with the law ends up fired and unemployable in the industry - and at the wrong end of the IRS enforcement actions.

The IRS' failure to enforce the law has led to an overinvestment in the fisheries and the so-called crisis of "over-fishing" that surprisingly can only be cured by handing over the rights to the fisheries to those who overinvested in the fisheries. Individual fishing quotas have become the elixir of choice for the Councils and their backers who stand to reap windfall profits from the privatization of the country's fishery resources. Quotas have historically been assigned to vessel owners, not the crew. Although the crew can be forced to pay the price of the quota as a trip expense, when the quota is transferred or sold by the vessel owner, the crew gain nothing. In 1994, six years after I broached the subject of expense deductions with the IRS, a review of the Surf Clam/Quahog quota plan released by the National Marine Fisheries Services raised questions of lease manipulations and possible tax law violations, and the negative impact the quota price deduction as an operating expense was having on the crew. Investigation of lease arrangements in regards to tax implications was at the time suggested. It is highly doubtful such an investigation has occurred.

Failure to record the percentage share of the catch due and paid to the captains and crew not only promotes worker misclassification, but prevents documentation of the true catch history and industry participation of the non-vessel owning fishermen who may seek to obtain quota shares in those fisheries where quota may be allocated to crew.

The Administration has pledged to eliminate incentives for employers to miscalssify their employees in order to evade employment taxes and other employment laws and to vigorously enforce the tax laws and increase compliance through examination and collection programs. It has been my experience that the IRS refuses to examine employees even in those cases, such as mine, where it has been shown that the employer misclassified an employee and failed to comply with reporting provisions. This Committee should demand an explanation from Mr. Shulman as to why the Internal Revenue Service is not using the tools handed it by Congress to end worker misclassification and to close the tax gap in the fishing industry, and why the employee, and not the employer, is being held liable for the payment of employment taxes, contrary to the law, and contrary to the treatment of other taxpayers.

Respectfully submitted,

Cheryl J. Latos
April 6, 2010

Statement of Colleen M. Kelley

National President

National Treasury Employees Union

On

"Internal Revenue Service Budget for FY 2011"

Submitted to

House Ways and Means Subcommittee on Oversight

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1750 H Street, N.W. • Washington, D.C. 20006 • (202) 572-5500

Chairman Lewis, Ranking Member Boustany, and distinguished members of the Subcommittee, I would like to thank you for allowing me to provide comments on the Administration's FY 2011 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 2011 Budget Request

Mr. Chairman, NTEU strongly supports the Administration's FY 2011 budget request of $12.6 billion for the IRS, a 4 percent increase of $487 million over the FY 2010 level. We believe that the President's request will allow the IRS to continue helping taxpayers meet their tax obligations while also improving enforcement of the tax law.

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 efforts to rebuild its workforce which is still down by almost 20,000 since 1995.

I would also note that in previous years, NTEU has supported the budget recommendations proposed by the IRS Oversight Board which have generally called for additional resources above that requested by the Administration. For FY 2011, the Oversight Board has recommended $13.495 billion in funding for the IRS. While we have not seen the specific details of the Board's proposal, we would be inclined to support providing additional funding for the IRS above the Administration's request and look forward to reviewing the Board's recommendation.

Taxpayer Services

Mr. Chairman, helping taxpayers understand their tax reporting and payment obligations is the foundation of taxpayer compliance. 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.

The IRS' comprehensive approach to taxpayer service played a critical role in allowing it to deliver a successful 2009 filing season, despite dealing with a number of difficult challenges posed by the residual effects of the 2008 Economic Stimulus Payment program and implementation of the American Reinvestment and Recovery Act. During this time, IRS employees processed more than144 million individual returns and issued 111 million refunds, totaling $339.6 billion; answered almost 39 million calls from taxpayers requesting information on new credits available to them; and helped more than 6.2 million taxpayers at the 401 Taxpayer Assistance Centers located around the country. And while these numbers show that employees providing taxpayer services are helping taxpayers understand and meet their tax responsibilities, more can and should be done.

We were happy 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 2009 while also recognizing that additional progress can be made. In particular, we strongly support the $20 million in additional funding to improve telephone level of service.

As you know, demand for telephone service remained extremely high in FY 2009 as taxpayers called to obtain information regarding economic stimulus payments and new Recovery Act credits. The significant increase in call demand stressed existing resources which negatively impacted the level of service. But despite the high call volume, IRS achieved a 70% level of service and maintained account and tax law accuracy rates of over 93%.

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 and reduce the tax gap.

That is why NTEU was happy to see the Administration's budget request would provide a $293 million increase in funding for IRS tax enforcement above the FY 2010 level, including additional resources made available through a program integrity cap adjustment.

A large portion of this increase will be invested in strengthening current Service compliance programs designed to close the tax gap by combating offshore tax evasion, expanding enforcement efforts on noncompliance among corporate and high-income taxpayers, and addressing underreporting of income associated with international activities. These investments are expected to generate $1.9 billion in additional annual enforcement revenue, resulting in a return on investment (ROI) of more than 9 to 1, once new hires reach full potential in FY 2013. This estimate does not account for the deterrent effect of IRS enforcement programs, estimated to be at least three times larger than the direct revenue impact.

Mr. Chairman, NTEU strongly supports targeting additional resources to programs that would help close the tax gap. 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.

Section 1203

Mr. Chairman, while meaningful funding for the IRS is important to operations, NTEU also believes that in order to maximize efficiencies at the IRS, Congress must act to modify Section 1203 of the IRS Restructuring and Reform Act of 1988 (RRA 98). Commonly known as

the "Ten Deadly Sins," Section 1203 outlines ten infractions for which IRS employees must be fired, including the untimely filing of federal income taxes even when a refund is due. No other federal or congressional employee is subject to similar mandatory termination.

Without question, Section 1203 has had a negative impact on the morale of the IRS workforce and is impeding the ability of the IRS to perform its mission. According to numerous GAO reports, IRS employees greatly fear the threat of being fired under Section 1203. This in turn has had a chilling effect on the ability of IRS employees to do their jobs. In particular, employees specifically attribute the decrease in recommending a seizure of taxpayer's assets to Section 1203. Clearly, Section 1203 impedes IRS' enforcement mission and is unfair to the IRS employees who must work under the constant threat of losing their jobs.

NTEU believes mandatory termination for Section 1203 violations is unduly harsh and should not be the only disciplinary action available. We advocate amending RRA 98 to allow for appropriate penalties other than mandatory termination for Section 1203 violations and to allow for independent review of determinations.

To be clear, NTEU does not condone any violation of law or rules of conduct by its members at the IRS or in any other government agency. Violations of some rules clearly warrant termination of employment. However, one group of federal employees should not be singled out and required to be fired for offenses that do not subject other executive, judicial, or legislative branch employees to the same penalty.

Mr. Chairman, the large majority of IRS employees work hard, follow the rules and pay their taxes on time. It is patently unfair to hold those who are charged with enforcing the tax laws to a higher standard than those who write them. NTEU asks for your support for changes to section 1203 of the IRS Reform and Restructuring Act, so that tax fairness applies to all Americans, even those who work at the IRS.

Security at the IRS

Mr. Chairman, in light of recent events, I would also like to reflect for a moment on the issue of safety and security of IRS employees. As you know, on Thursday, February 18, 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. The attack, in which one IRS employee perished and several others were seriously injured, 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. I know the subcommittee joins with NTEU in sending our condolences to the family of the fallen IRS employee and to all those affected by this senseless tragedy.

Mr. Chairman, as the Federal inventory of buildings has steadily increased over the last 30 years, the uniformity and implementation of security standards have varied greatly. Prior to 1995, minimum physical security standards did not exist for nonmilitary federally owned or leased facilities. But even with established minimum safety standards, security at federal facilities can vary greatly from agency to agency and even from building to building.

This is particularly true for agencies like the IRS, which must offer public access to provide customer service. The IRS is widely dispersed with approximately 755 facilities throughout the nation. These facilities can range from one-person offices to large tax return processing campuses with thousands of employees. There are also different tenant sharing arrangements at these facilities, from being housed as an IRS-only office to sharing building space with other Federal agencies and other private companies. In buildings where the IRS is not the lead agency or tenant (i.e., the largest organization in the building) the IRS must propose changes through a building security committee.

NTEU members have consistently voiced concern over the inconsistency of safety and security measures at IRS facilities across the county, in particular, at facilities like Taxpayer Assistance Centers (TACs) which must offer public access in order to provide customer service. In many instances, there is an absence of any type of security presence at these TACs, which has heightened fears among employees that they are particularly vulnerable to threats and attacks.

Unfortunately, IRS has been slow to recognize the importance and necessity of providing a security presence at all IRS facilities. In fact, just recently, in the face of strong opposition by NTEU and our members, the IRS was forced to abandon an initiative to "standardize" its use of contract guards and dogs at various locations across the U.S., which would have resulted in the elimination or reduction of guard service at 42 posts. While NTEU was successful in fighting this planned reduction of guard services, many IRS facilities remain woefully unprotected. According to IRS, of the roughly 755 IRS facilities located nationwide, just 275, or 36%, have some type of security detail. Thus, 480 IRS facilities, roughly 64%, are without any security presence whatsoever. This is clearly unacceptable.

Mr. Chairman, the absence of adequate security at IRS locations is just one of many security related concerns reported by NTEU members in recent years, which also include: IRS taxpayer walk-in centers without metal detectors, or operational, monitored security cameras; insufficient perimeter lighting; inoperable security equipment; parking areas without security camera coverage; security service spread thin by guards required to leave their posts and patrol loading docks during deliveries; security devices ordered but uninstalled due to inadequate funding; malfunctioning security cameras, security gates and magnetometers; IRS walk-in centers with only cipher locks on the front doors; open loading docks without a security presence; excessive waits for security personnel arrival after making an emergency call; security cameras discovered to not have film after a robbery; and inoperable fire alarms.

As you can see, IRS workers' concerns about the heightened risk of threats and attacks at IRS facilities, in particular, at those which must offer public access in order to provide customer service, are not unfounded.

Mr. Chairman, I would like to state my appreciation to IRS Commissioner Shulman and Treasury Secretary Geithner for their efforts in the aftermath of the Austin IRS attack and I am hopeful that we can build on those efforts to improve worker safety at the IRS.

NTEU Recommendations

In an effort to help IRS minimize the threat of violence against IRS employees as they administer the Internal Revenue Code, NTEU proposes the following recommendations: (1) IRS undertake a comprehensive review of safety and security measures at all IRS facilities; (2) ensure IRS employees have access to any and all information on those individuals that could pose a threat; (3) grant law enforcement officer (LEO) status to IRS Revenue Officers.

Comprehensive Review of Safety and Security Measures at all IRS Facilities

In light of recent events and ongoing concerns by IRS employees about their safety and the security of IRS locations, NTEU believes that IRS should immediately undertake a comprehensive review of safety and security measures at all IRS facilities around the country. In particular, IRS should review the current established physical security standards and requirements for the protection of Service facilities and personnel. The review should consider whether or not each facility has, among other things; the proper risk assessment security level designation; sufficient entry control systems, including guard or other armed presence and magnetometers; sufficient perimeter security, exterior lighting, proper designation of restricted areas, and operable security equipment.

We also believe that to the greatest extent possible, IRS should solicit the participation by IRS employees themselves in the review as they may be able to offer a unique perspective on the problems and challenges associated with securing IRS facilities, its employees, as well as the taxpayers who frequent them.

Input from employees on the front lines can be particularly helpful as the security needs at IRS facilities can vary greatly, depending on their mission, size, etc.

As the Internal Revenue Manual notes, in order to ensure that a Post of Duty (POD) is properly protected, careful planning is necessary to ensure that appropriate protective measures are in-place and tailored to the facility's specific mission, threat, and functional requirements. PODs may vary greatly in size and function, so each requires close examination for tailored security countermeasures. The function of the office, the type of records maintained, the equipment in the POD, the size, population, if visitors frequent the facility, etc., are all determining factors to consider when planning security.

Mr. Chairman, NTEU believes that it is important for IRS employees to feel safe and secure in the workplace as they carry out their duties and stands ready to work with the IRS to ensure the proper safeguards are in place to ensure the safety of IRS employees.

Ensure IRS Employees Have Access to Information

As you may know, the IRS Restructuring and Reform Act of 1998 (RRA 98) required the IRS to stop designating taxpayers as Illegal Tax Protesters (ITP) or any similar designation. This ITP designation was used previously by the IRS to identify individuals and businesses using methods that were not legally valid to protest the tax laws. The designation was also intended to alert employees to be cautious so they would not be drawn into confrontations with potentially

dangerous taxpayers. Congress decided to require IRS to drop the ITP designation over concerns that the label could bias IRS employees and result in unfair treatment of the taxpayer.

While the ITP designation was abolished, RRA 98 did provide IRS the authority to implement additional procedures, such as the maintenance of appropriate records, in connection with this provision so as to ensure IRS employees' safety.

NTEU believes it is critical that IRS ensure that any and all information relevant to employees' safety will always be available to them.

LEO Status for Revenue Officers

NTEU is very concerned about the level of threats and violence against IRS employees, and in particular, against Revenue Officers (ROs), who often must meet with taxpayers on a one-on-one basis in the course of conducting their investigations.

According to the IRS, between 2003 and 2007, RO's reported more than 480 cases involving Potentially Dangerous Taxpayers (PDTs), a designation assigned to taxpayers who have demonstrated a capacity for violence against employees of the IRS, contractors or their families, and Caution Upon Contacts (CAUs), defined as those incidents that posed a less immediate and less serious threat.

This report comes at a time when the threat of violence against Federal employees is receiving increased attention and anti-government sentiment remains at an all-time high.

But despite these startling figures, ROs are not authorized to carry and or use firearms in performance of their official duties and are forced to request assignment of an armed escort to ensure their own safety. According to TIGTA, it expects the necessity for armed escorts to increase over time as the IRS places additional focus on collection and enforcement activity.

NTEU strongly believes that the high number of threats and assaults recently reported by TIGTA once again illustrates the clear need for RO's to be granted LEO status. That is why NTEU strongly supports H.R. 673, the "Law Enforcement Officers Equity Act," which would grant law enforcement retirement benefits to ROs at the IRS. These officers face dangerous situations as they enforce the United States Tax Code and collect delinquent taxes. Most people see these individuals as law enforcement officers, and many have reacted to their inquiries with threats, assaults, and in some cases gunfire. Yet, these men and women are being denied the rights and benefits of their colleagues who are considered to be law enforcement officers.

While some in the government have expressed concern that legislation providing coverage for these officers would have a negative impact on personnel costs for government agencies, this argument is fundamentally flawed. Granting LEO status to ROs will actually decrease personnel costs by increasing morale and officer retention, thus decreasing the costs associated with training new officers.

NTEU asks members on the subcommittee to support this critical legislation that will enhance the safety and security of Revenue Officers as they carry out their tax enforcement mission.

Conclusion

Mr. Chairman, thank you for the opportunity to provide NTEU's thoughts on the Administration's FY 2011 budget request for the IRS. We believe that by investing in demonstrably effective enforcement and taxpayer service programs, the Administration's request will ensure the IRS continues to meet its mission of providing America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

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