

**FULL COMMITTEE HEARING ON
ENTREPRENEURS AND TAX DAY:
HOW IRS POLICIES AND PROCEDURES
IMPACT SMALL BUSINESSES**

HEARING

BEFORE THE

**COMMITTEE ON SMALL BUSINESS
UNITED STATES
HOUSE OF REPRESENTATIVES**

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**FULL COMMITTEE HEARING ON
ENTREPRENEURS AND TAX DAY:
HOW IRS POLICIES AND PROCEDURES
IMPACT SMALL BUSINESSES**

Wednesday, April 14, 2010

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
Washington, DC.

The Committee met, pursuant to call, at 2:07 p.m., in Room 2360, Rayburn House Office Building, Hon. Nydia M. Velázquez [Chair of the Committee] presiding.

Present: Representatives Velázquez, Moore, Dahlkemper, Schrader, Nye, Bean, Graves, Bartlett, King, Buchanan, and Coffman.

Chairwoman VELÁZQUEZ. Good afternoon. This hearing is now called to order. With tax day now just hours away, most Americans are wrapping up their paperwork, looking forward to 12 months without touching a W-2. For many small business owners, however, the process is still underway. The weak economy, along with a series of new tax measures has compounded its historic complexity, making the process of filing a small business tax return especially challenging. This is not the first time our committee has met to discuss the tax challenges facing small firms. In the past, small businesses have told us that complexity is the most stubborn of those obstacles. With good reason—entrepreneurs face more than 200 IRS forms and schedules. The process of navigating this maze of regulations is not only complex, it is expensive and time consuming.

Businesses with fewer than 20 workers spend roughly \$1,300 per employee on tax compliance, and according to one IRS study, up to 80 hours. At a time when many businesses are struggling, every hour counts and so does every dollar. This afternoon we will discuss the role that the IRS plays in helping entrepreneurs meet their tax obligation and examine the agency's management of certain Recovery Act tax incentives. Last year, Congress passed one of the largest and most sweeping tax cuts in U.S. history. The Recovery Act incorporated \$15 billion in relief for entrepreneurs, including provisions to not only put cash back in their pockets, but to increase demand for their products, such as the first-time home buyers' tax credit.

Now we need to be asking whether or not those refunds and the resulting economic boost are being disbursed effectively. With the economy still struggling, it could use a fresh influx of circulating

capital, and it is critical that the IRS do everything it can to stoke, rather than restrict, our economic recovery. But as one study recently found, that isn't happening.

Since 2005, the agency has increased its small business audits by 30 percent. Meanwhile, audits of large companies dropped 21 percent. I understand that in light of our Nation's fiscal constraints, closing the \$345 billion tax gap is critical to our long-term prosperity. But so are small businesses. These are the companies that create 70 percent of new jobs and will play a leading role in rebuilding our economy. Any effort to increase our tax base must be done in a way that is responsible, fair and not unduly burdensome to small businesses. Small firms should be able to look to the IRS as an ally, not an enemy.

Given the myriad of available small business schedules and incentives, entrepreneurs need to know that they can count on the IRS to address their concerns quickly and answer their questions accurately. The agency's move to increase staff levels within the Small Business/Self-Employed program should be an important step in delivering those resources, and I was pleased to see Commissioner Shulman place a greater emphasis on small firms overall.

In this afternoon's conversation, we will discuss the improvements he has made and look to see if more can be done. Tax law operates most effectively when small businesses have certainty and stability and now is the time for policies to deliver both. Now is the time for incentives that encourage would-be entrepreneurs to start up and existing businesses to expand. With the proper tools, America's small firms can strengthen the economic recovery that is currently underway and spark the job creation we are waiting to see. With that, I would like to welcome and thank Commissioner Shulman for being here today. I know this is a busy time over at the IRS, and I look forward to hearing from you. So now I will yield to Ranking Member Graves for his opening statement.

[The statement of Ms. Velázquez is included in the appendix.]

Mr. GRAVES. Thank you, Madam Chairman, and I want to thank you for calling this important hearing on tax issues affecting small businesses. Special thanks to Commissioner Shulman for testifying today. Unemployment is hovering around 10 percent; new home sales are still falling; consumer confidence is low; and our government's rampant spending could soon jeopardize the United States' AAA credit rating that keeps borrowing affordable. The unsustainable policies of government bailouts, skyrocketing Federal spending, higher taxes and record national debt have had a devastating effect on small businesses. In order to hire new workers, expand operations and help our economy, entrepreneurs and small business owners, need some certainty. However, right now the only thing that is certain for small business owners is more taxes and more regulation. Today's businesses are facing more uncertainty than ever as they try to determine the real impact of the new health care law is going to have on their families, their businesses and their community. I am particularly concerned about who is going to enforce the new health care mandates on individuals and small businesses and how much it is going to cost.

Estimates on this information vary, and no one seems to know the real numbers. Initiating such a massive overall of health care without first having a clear understanding of the cost and impact to me is a recipe for disaster. In addition to the health care laws, \$569 billion in tax increases, employers have to worry about other tax hikes that may be just around the corner. The expiration of the 2001 and 2003 tax cuts threatens to raise the capital gains rate on dividends from the current 15 percent for middle-class taxpayers and 20 percent for higher income earners to as much as 45 percent. This is not the kind of policy that is going to allow small business owners to expand and create jobs.

Rather than increasing taxes and unfairly punishing small businesses, one of the best steps we could take to help small business owners is simplifying the Tax Code. The IRS taxpayer advocate reported that U.S. taxpayers and businesses spend about 7.6 billion hours a year complying with filing requirements. In fact, tax complexity has been consistently ranked as the number one issue facing both taxpayers and the IRS. By making it easier for small businesses to navigate the Tax Code, we could save them the time and expense of hiring tax professionals. Churchill once said that a nation trying to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handle. Forcing small business owners to create the majority of private sector jobs to carry the financial burden of damaging Washington initiatives is only going to lead to more unemployment and fewer opportunities for Americans. Again, Madam Chairman, I want to thank you for holding this hearing. I look forward to Commissioner Shulman's testimony today.

[The statement of Mr. Graves is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you. Now it is my pleasure to welcome the Honorable Douglas Shulman, IRS Commissioner. He is the 47th commissioner of Internal Revenue and began his 5-year term on March 24, 2008. Prior to joining the IRS, he worked for the Financial Industry Regulatory Authority, the private sector regulator of all security firms doing business in the United States. The IRS collects approximately \$2.4 trillion in annual tax revenue that funds most government operations and public services. Welcome.

**STATEMENT OF HON. DOUGLAS SHULMAN, COMMISSIONER,
INTERNAL REVENUE SERVICE**

Mr. SHULMAN. Thank you, Madam Chairman, Ranking Member Graves. Members of the committee thanks for giving me the opportunity to testify today. The IRS has two equal parts of its mission: Service and enforcement. I have been very clear since I started that we need to excel at both. For the vast majority of American taxpayers—small businesses included—they are trying to wrestle with the complex Tax Code and get it right. We need to be there to educate them, give them world-class service, and for those who don't pay their taxes, we need to run rigorous compliance programs.

My written testimony highlights our efforts for the small business community especially focusing on outreach, but I want to highlight a few things we are doing here today. We have moved

swiftly to implement the new laws in the last 15 months that were intended to help small businesses. We have put out over \$9 trillion in net operating loss carrybacks, which was part of the Recovery Act. The HIRE Act, which was signed into law last month, gives small businesses an important incentive to start hiring again and we are working to implement that quickly. We have already begun to mobilize and let small businesses know the new tax credit that is available for them to help buy insurance, health insurance for their employees. These actions reflect our commitment to service.

As I said, most small business owners want to pay what they owe. They don't want to pay too much. And they certainly want to take all credits and deductions that are available to them. So we have redoubled our efforts to make sure small businesses know what credits what deductions are available to them. At my prompting, the agency has also shown greater flexibility in dealing with small businesses. After all, the public trust depends on people believing that everyone is paying what they owe, but this trust also demands that we be flexible and principled in dealing with taxpayers who are in financial trouble. This year we are holding hundreds of special Saturday open houses staffed by my employees where we can resolve problems on the spot and we are dedicating in May and June a number of those open houses just to small businesses, to help them work through installment plans, help them clean up tax debt, help them work out settlements. We remain committed to service at the IRS.

Today as everybody knows, too many small business owners continue to struggle to make their payroll, secure lines of credit, provide health insurance coverage, contribute to their employees' retirement plans and stay current with their taxes. As Commissioner, I have sought to give our employees the guidance and discretion they need to assist small businesses with the service that they need. Let me end with a word about our employees and our employees' commitment to public service.

This February, many of you may know, an individual flew a plane into an IRS building in Austin, killing one of our employees. We have no reason to believe that this attack could have been prevented or that it was part of an organized opposition to the agency. However, I continue as Commissioner to be concerned that the IRS, and especially its employees, who are doing the work of the American people, not be demonized. The IRS is filled with dedicated public servants who serve taxpayers every day.

I am very appreciative of the support that Congress gave the agency immediately after the attack, and I ask all members of this committee to help me in explaining to the vast majority of Americans that when they interact with the IRS, it is us getting a refund to them. It is us answering a question, and that at its core we spend just as much time on service as we do on compliance.

So in closing, Madam Chairwoman, let me assure you that I appreciate that the Small Business Committee needs the IRS to provide service and education. We are going to continue to search for ways to do our job better, and I look forward to working with you and all the members of this committee as we move forward.

[The statement of Mr. Shulman is included in the appendix.]

Chairwoman VELÁZQUEZ. Thank you. Commissioner, starting in 2011, credit card companies and merchant banks will be required to verify the taxpayers' ID number for businesses they provide services for. If the bank cannot confirm the team, it is required to withhold 28 percent of the gross credit card transactions. If there is a mistake, this could have major consequences for honest small businesses. How will the IRS ensure that small firms are not harmed by paperwork errors?

Mr. SHULMAN. One of the problems that many small businesses have, as you alluded to, is they are not hiring. Accountants keep their books every day. They have record keeping issues they have cash issues, et cetera. And our hope is actually that this regulation will help people with getting a simple statement from their credit card company about their gross receipts which will help reduce the paperwork and let them file their taxes.

I have been very clear from the outset that we think this piece of legislation that Congress passed is an important piece of legislation because information reporting helps us do our job and it helps simplify the job of small businesses. But we have been doing a lot of outreach, both to the small business community and to the credit card community to make sure there is smooth implementation. If we see issues like people having hard times—we won't hesitate to jump on it and help people sort through any issues.

Chairwoman VELÁZQUEZ. Recent reports indicate that the average tax refund is up nearly 10 percent over last year and that the IRS has already sent out \$6 billion more in refunds than last year. Would you attribute increasing reforms to provisions contained in the Recovery Act, like the home buyer tax credit, increased sections 179 expensing, energy efficiency tax credits and other refundable credits and deductions?

Mr. SHULMAN. Yes. I mean, I think it is certainly a factor. There were major tax cuts and tax credits. A lot of those tax credits are now coming out in people's refunds. Just the fact that you get an \$8,000 tax credit for buying a house, obviously there are a number of people who have bought houses and that has increased the average refund.

Chairwoman VELÁZQUEZ. As of mid-March, the IRS has sent out a record \$175 billion in refunds, and the average tax refund was over \$3,000. However, at that time, nearly half of all taxpayers had not filed their returns. Do you have any updated data on the amount of refunds the IRS has sent out or if the average refund has changed?

Mr. SHULMAN. The average refund stayed around \$3,000. About 90 million returns from filed as of Friday last week which were our last count. We expect another 20 million to 30 million this week, and then there is usually about 10 million extensions. So this year the only major change in trends that we have seen has been the increase in refund amount, which clearly there has been a lot of tax law changes that is attributable to that.

Chairwoman VELÁZQUEZ. Let's talk about the increase in business audits that I mentioned in my opening statement. A recent study determined that audit hours of small businesses have increased by 34 percent while large corporate audits have decreased by 33 percent between 2005 and 2009. Small firms are worried that

small business audits will rise because the audits are easier and quicker to complete. Can you discuss why small business audits continue to rise? And will the IRS focus their enforcement efforts for closing the tax gap on large corporations rather than small businesses?

Mr. SHULMAN. There was a study released on Monday that I have serious concerns about the way that it characterized our numbers. We are a pretty transparent organization. We have data books and reams of data. That study actually used a very specific number which was audit hours of closed cases. And so if you look, they use 2005 as an example, which was an anomaly year because my predecessor had a campaign to close a number of cases and get all of the cases current that year. And they added up multiple years of audits for closed cases that year, which I think is a skewed statistic.

And then they did the same thing with the small businesses. Let me give you the numbers that I think are the most relevant to see where our audit resources are spent.

Chairwoman VELÁZQUEZ. Didn't the study also show that three out of four large corporations are not being audited by the IRS?

Mr. SHULMAN. Let me give you the broad audit numbers. These are the numbers. These are our published numbers and the ones—rather than commenting on theirs. Our audit rate overall for individuals is 1 percent.

Chairwoman VELÁZQUEZ. And small business too and large corporations?

Mr. SHULMAN. So for people who make more than \$1 million—I am just going to give you four numbers—it is 6.5 percent. For businesses which are defined as large, over \$10 million in assets it is 14.5 percent. For businesses under \$10 million in assets it is less than 1 percent. So the small businesses in this country have a smaller chance of being audited than an average individual and a 1-in-14 chance of being audited as compared to a large business. And then as you go up the scale for large businesses, if you are what you think of as a multinational, they are under continuous audit.

Anyone with more than \$20 billion of assets, there is 100 percent chance of being audited. If you have got \$5 billion or more of assets, there is a 50 percent chance of being audited. So I feel very comfortable that we have been for the last 5 years increasing our resources because there had been a dramatic decline in compliance resources for a 10-year period that we are in the process of reversing. But I, by no means, think we are disproportionately focused on small business. If anything, they are the lowest number.

Chairwoman VELÁZQUEZ. You mentioned in your statement that a small business solution Saturday is planned. Would you please tell us, how will you determine the main topics for the forums? What will be the focus?

Mr. SHULMAN. So the topic is whatever a business is having trouble with. So we define topics by the taxpayer that comes to us. I have a motto that I go around the country and talk to our employees and I say, our job is to walk in the taxpayers' shoes and meet them based on what their needs are. So if there is a small business who got way behind on their taxes or had a lot of profit last year

and their cash flow has fallen off the books and they literally can't pay, trying to work out some sort of a payment plan.

If there is somebody who has complexity and trying to figure something out, doing that. The way this will work, call your local office set up an appointment, we will make sure all the right people are there. And we may have an agent there who can settle the case; we may have a collection person if they are in collection; and we have appeals officers there if someone who disputes what has happened in an audit so they can settle it.

Our goal is to solve problems on the spot. Our first set of open houses we had last month, 88 percent of the people who showed up walked away with all of their issues resolved, which was the goal of these open houses.

Chairwoman VELÁZQUEZ. Okay. So without waiting for one of those solution Saturdays that you are planning, I will tell you that one of the issues that small businesses are confronting today is they are struggling to meet tax obligations because of the economic downturn that we are experiencing. So I would like to ask you, why is it that the IRS has accepted 72 percent fewer OIC than 2001? And is the IRS taking action to increase OICs for small businesses in 2010?

Mr. SHULMAN. Yeah. I am glad you asked me about that because when I came in, I looked at our Offer-in-Compromise program. I was not pleased that people weren't using it as much and that applications that were coming in weren't accepted. We made a major change this year which we announced in January. In the past, our policy was, if you wanted to come in for a settlement, an Offer-in-Compromise, we would look at your last 3 years of income to determine your ability to pay, recognizing that a lot of people are unemployed. People have shuttered some of their businesses and there are people who really can't meet basic living expenses and pay.

We changed our criteria starting in January that we are now looking at current income. So we are not looking at whatever you made a couple of years ago. We are looking at what you are making right now and assessing your ability to pay, which my hope is for taxpayers who are struggling, that will help them out.

Chairwoman VELÁZQUEZ. Given the economic crisis and the fact that small businesses continue to struggle and especially to get access to capital, are you planning to do anything to simplify the OIC's process? Because one of the complaints that we hear from small businesses is about the fact that the process is complicated and is complex.

Mr. SHULMAN. We have been looking at that. Our first step was to do what I mentioned. We are also looking at seeing if there is a way to simplify it. So I mean, what I would tell you is I am very focused on this. I actually have a working group with an outside consultant looking at ways we can improve the program. Obviously within the confines of the law and the flexibility that is given to us because we can't just compromise any debt. We don't have that kind of authority, but it is something that we are definitely looking at.

Chairwoman VELÁZQUEZ. Thank you. I have more questions but we will continue and then in the next round I will ask you. Mr. Graves.

Mr. GRAVES. I have questions, too, Madam Chair. But we have a time conflict, so I will pass it to Mr. Buchanan.

Mr. BUCHANAN. I want to thank the ranking member. Madam Chair, thank you for putting on this hearing on today. Commissioner Shulman, I was interested, how did you manage to be up on the Hill the day before tax day?

Mr. SHULMAN. I was invited.

Mr. BUCHANAN. Let me mention a couple of things. And I have been in business 30 years before I got here in 2007 and in small business primarily. Why is the Tax Code so complex? I mean, I read the other day, or someone showed me that USA Today reported 60,000 pages of Tax Codes, deductions and this. I can't imagine anybody ever signs a tax return that is accurate because I know in my case—I had a bunch of different businesses, and my CPAs fill it out. We want to get it all right. But isn't there a way we could simplify this process, especially for small businesses? Many of them may have 15 employees or less. It just seems like it is crazy. What are your thoughts on it?

Mr. SHULMAN. My thoughts are, my job as Commissioner of the IRS is to administer the law that Congress writes and policy-makers write. So I am a big fan of simplification because I have to go out there and be the one who interacts with the American people with this complex Tax Code. I would ask you and use your expertise, you know, the Tax Code is used for everything from collecting the funds to run the government to administering credits for a variety of targeted social programs to giving breaks to different industries and different special interest groups along the way. I think the reason it is so complex is that the Tax Code, over the last 20 years, has been used more and more for specialized purposes rather than the general raising of funds to run the government.

Mr. BUCHANAN. It is how many thousands of pages is what is amazing to me. I want to get into the heart of what I want to talk about. I know the Democrats and Republicans, all of us have focused on helping people get back to work, but yet it looks like we are going to take our taxes up to 39.6 and then they are asking for a surtax of 5.4. Now most businesses—and I am in Florida—99 percent of the businesses register in Tallahassee, our capital, are classified as small businesses. Most small business, as you know, have pass-through income, whether they are an LLC, sub S, partnership, sole proprietorship, whatever they might be. So it just seems strange to me in a time where we are trying to create jobs, we are going to be raising taxes from 34 percent to 45.

Is that your understanding of what this will net out to be if the Bush tax cuts sunset and we add a 5.4 percent surtax to people making over \$200,000 or \$250,000 which are—a lot of those people I know, a lot of those people are running small businesses, so we are going to add another 10 percent in tax to their bottom line, which is another liability. Is that your understanding?

Mr. SHULMAN. You know, I would defer you to the Joint Committee on Tax. Again, you know, my job is to interface with the American people to run the tax system, to administer the laws on the books, not to run the economics of where the—

Mr. BUCHANAN. I am not asking for the economics. I am asking for your understanding. My understanding is that is going to take the top tax bracket of the tax cuts, do sunset up to 39.6 and then another 5.4 surtax which I told you, most small businesses, as you know, have pass-through income. So it seems to me—because I get asked this. I go to town hall meetings. People are saying, What is the net, the top tax bracket? I have got a person who said, I have 40 jobs. I am trying to figure out how to get some cash flow. I can't borrow from the banks. I need access to capital. Are they going to charge me another 10 percent in tax? I think that is something you should know ideally or should figure out.

Mr. SHULMAN. I don't want to respond to a bunch of moving numbers and do it accurately for you. So I would be happy to work with my colleagues at Treasury, work with your staff and get you that net effect so you can answer that for your constituents.

Mr. BUCHANAN. The other thing is, is that in terms of the jobs bill—and maybe you can run this down too—the President and I both agree. I talked to him. He was up in Baltimore—about the idea of taking capital gains to zero from 15 percent, just with conceptually the idea that at some point that it would sunset. And the reason I think it is important is because there is a lot of capital on the sidelines. People don't have confidence in the economy. I would just say they don't have confidence in the Congress and the administration, a lot of small business people. Do you have an opinion on that or a thought at all about capital gains? I think the President supports it. Not forever but for a period of time. And I support it because I think that small businesses—our community banks and our area has been decimated. They did a lot of lending 3 years ago. Banks aren't lending in general. So again we are trying to find a way to get capital available and there is some capital. There are people who thank have money but they don't have the confidence. But yet if it goes to zero maybe for a couple of years, it could make capital available for people that invest it in the small businesses.

Mr. SHULMAN. So there is actually a proposal in the President's 2011 budget to have no capital gains for certain investments for entrepreneurs in small businesses. So I think conceptually, my understanding is—I haven't talked to the President about this. I can't speak for him—but that he has been quite supportive of this. I ran a small business. I started one.

Mr. BUCHANAN. I like it a lot more.

Mr. SHULMAN. So I totally understand all the things from operations to raising funds, et cetera. And I think that, again, you know, it is not the arena I spend my time playing in, the policy arena. I spend my time in the administration arena, on the numbers on the books. But I think anything we can do to get funds and capital to small businesses is a good thing.

Mr. BUCHANAN. The other thing, we have an ag community in our area, a pretty substantial ag community, and of course, across the country in small businesses. I am against raising taxes or the tax amount we have on estate taxes. Where does that sit today? Is it your understanding that if someone passed away today, they pay zero; the next year, they pay 55, is that where that sits today?

Mr. SHULMAN. I think it is influx. That is what is on the books now, but I think that Congress hasn't decided what it wants to do. I think there has been talk about people taking it up. I think we are not in a good situation right now because there is uncertainty, right? So yes, if someone died today, you know the estate tax has expired. But the Congress has the option to make it retroactive and there are different parts of the provision. So I think right now for my job and for the American people, it is not in a good place.

Mr. MOORE. [presiding.] Excuse me. The gentleman's time has expired.

Mr. BUCHANAN. Thank you.

Mr. MOORE. The chair next recognizes the gentlelady from Illinois, Ms. Bean. Ms. Bean, do you have questions?

Ms. BEAN. Thank you, Mr. Chairman. First of all, thank you so much for being here and providing your testimony. I also want to thank your staff, has been out to help at some of the constituent service fairs in the Eighth District that I represent as well as the—I have done a small business Federal resources form specifically to allow small businesses to come in contact with the agencies that do provide resources towards their success.

And you had Lynda Dyer at our Constituents Services Fair and Yolanda Ruiz at the Small Business Fair. Both were very well received and they did answer very specific questions about tax credits that were available to both constituencies.

I would like to back up and ask you about the—of the \$280 billion of tax cuts that were included in the stimulus, money of those—many of those cuts were directed to the small business community, the NOL carryback being one, the 179 bonus depreciation that we had in there. We had the smart grid technology, we had health IT initiatives along with—we happened to have at our forum, we had the DOE there to talk about some of the grants there and the IRS was able to talk about some of the specific questions for those that came. I would like to specifically talk about the NOL carryback. I believe I saw in your written testimony but I don't know if I heard you say it that there were 40,000 businesses that have already participated in the NOL. And I think there was a number I saw here. Was 22.6 billion.

Mr. SHULMAN. From the—so there is \$9 billion between the Recovery Act and then there was the extension that happened in the fall. We staffed up that operation because we recognized a lot of small businesses. This was their lending when credit was crunched. This was their access to capital and we wanted to make sure we got that out quickly.

Ms. BEAN. So it was a total of how much?

Mr. SHULMAN. \$9 billion is the number where we are running, but these move every day.

Ms. BEAN. Good. I am really glad to hear you say that. I think it is really important. There are a lot of fears the business community has had in these uncertain economic times, but there have been tremendous resources provided to assist small businesses, both in the guarantees that we provided to the SBA lending programs so there would be capital flowing in over 20 billion has been put in the hands of small businesses through the SBA lending programs that we increase the government guarantee on also as part

of the stimulus, but I think you said well carryback bonus depreciation and other initiatives are important as well.

So I want to thank you for highlighting that. And one other thing, I guess I would also mention, is of the 6 million small businesses in the country, 5.8 of them are under 50 employees. So for those who are concerned about ramifications or mandates or penalties to small businesses, there will be no penalties or mandates for those 5.8 million of the 6 million businesses. There is only 200,000 that are over 50. And of the 200,000 businesses that have more than 50 employees, only 5 percent don't already have insurance. So there is no issue there for those companies.

So while there are some fears and concerns as people are learning what is actually in the bill, it is important that we clarify that this is a very positive move forward and of those businesses, of the 6 million, four of them are eligible for tax credits that will assist them, for those who already have insurance, to pay their premiums, and for those who don't, it will assist them to enter the health care market and provide coverage to themselves and their employees.

So I just wanted to clear up the record on that because there sounded like there was some confusion. Thank you. I yield back.

Mr. MOORE. Dr. Bartlett, the gentleman is recognized for 5 minutes.

Mr. BARTLETT. Thank you very much. Thank you for your testimony. I was in small business in another life before I came here, so I understand what we are talking about. For a small business to be able to pay their taxes, don't they have to charge more for their product or their service?

Mr. SHULMAN. Well, I think, you know, the U.S. Tax Code, people can figure out what they are going to do. So that is a presumption that you are welcome to make.

Mr. BARTLETT. Well, I think most people would agree with that. Doesn't that then make this a very regressive tax since the—it simply becomes another part of the cost of doing business, and if they can't pass it on to the consumer, they go out of business, don't they? So doesn't that make tax on business a very regressive tax? Because the poorest of the poor have to buy the products of business? Bill Gates doesn't care. He can pay the tax. Why do we want to have this really regressive tax? Why don't we make this a fair tax, just don't tax business at all and tax the people who buy the product, isn't that fair?

Mr. SHULMAN. Like I told your colleague, I am going to defer on broad tax policy and broad characterizations of how the taxes work. My job is to kind of get it technically right and make sure we administer it fairly.

Mr. BARTLETT. I understand that. I understand that you don't develop policy, that you simply administer the policy that is developed from the laws that the Congress passes. But if you really look at the tax on business, if they can't pass that on as a part of the cost of doing business, then they can't continue in business, so then that makes it a very regressive tax. My question is, why do we want to have regressive taxes? Why don't we simply tax the product when it is bought by people, rather than increasing the cost of the product, wouldn't that greatly simplify the tax?

Mr. SHULMAN. Again, I think you are talking about a VAT.

Mr. BARTLETT. No, sir. I am not talking about a value added tax. That is a horrible tax. It is a hidden tax. And I like a consumption tax. In fact, I would like to tax in big red letters, big red numbers at least as large as the cost of the product so that when you bought a product, you knew what taxes you were paying. I remember when I was younger, you went to the gas station. You bought your gasoline. There were a number of numbers on the gas pump there, and it was the cost of the gas and the cost of the taxes that were added to it. Now it is just all lumped in together. I think it is 40-some cents taxes we pay in Maryland but that is hidden. Whatever taxes are hidden, they are easier to collect, aren't they?

Mr. SHULMAN. Again, you know, these are all conversations that are very interesting to me. But the kind of broad characterizations of what is hidden, what is not, what is regressive, what is not, I am going to stay away from.

Mr. BARTLETT. I am always concerned that we wanted to tax businesses, not understanding that what we are doing is hurting the poorest of the poor who have to buy the product of that business. And since you tax the business, you increase the cost of the product unnecessarily or the small business can't stay in business if they can't collect enough money to pay their taxes, right? So now we have increased the cost of the product. I have trouble understanding why we want to hurt poor people. I would like to make things cheaper for poor people and to collect the taxes from those who can pay the taxes.

Last year I think 52 percent of Americans got more from government than they paid into the government. Why would we want to increase the cost of the things that these people are buying by taxes? I would like to have a zero tax on business. I think that is the fairest tax, the simplest tax and simply to collect it from the consumer. Why wouldn't that be a better tax system? I know you are not in the policy. You are in administration. But wouldn't that simplify your job if we did that?

Mr. SHULMAN. Again, I encourage you to take it up with the Ways and Means Committee and the other tax writing committees.

Mr. BARTLETT. Thank you. Thank you very much. I appreciate your testimony. Thank you.

Mr. MOORE. Thank you. And the chair recognize himself for one question. My question is focused on the IRS's task of educating taxpayers about the new laws that may affect them. As you know, the IRS' small business self-employed divisions specifically provides information, service and education to the millions of small businesses and self-employed taxpayers. As you also know, in 2009, this division hired over 3,500 additional employees for a total of almost 30,000 employees. How are these new employees being utilized by the IRS? And how are all the employees of this division being utilized to assist small business taxpayers in general? If you would, sir.

Mr. SHULMAN. As I mentioned before, we spent a lot of time on average. Let me give you some of the output measures, which are I think interesting. In 2009, we attended or held 2,400 symposium seminars for small businesses to help them understand the Tax Code, directly reaching 180,000 small business taxpayers. We have

members of the staff in that division who put out a small business electronic newsletter every month that goes to 170,000 small businesses or their tax advisers. Again, specifically to help them understand small business tax provisions.

I mentioned the open houses that are being staffed by people from that division. We have phone forums where 3,000 people can get on the phone, e-mail in questions and answer any questions they have got about issues. We hold those throughout the year. And we hold what we call nationwide tax forums where we send people from that group to help people understand their tax obligations. There is one we have in Las Vegas every year, that is 5,000 people who show up who either advise or are small businesses in taxes.

So that division clearly has a compliance role and does a variety of compliance but has a tremendous amount of time spent educating taxpayers doing outreach.

Mr. MOORE. Thank you, sir. The chair will next recognize Mr. King for 5 minutes.

Mr. KING. Thank you, Mr. Chairman. Commissioner, thank you for your testimony. I appreciate you being here today. I want to suggest for your opening remarks, too, that I believe there are also a lot of highly qualified people who work for the IRS. And I am seeing the President and ObamaCare look to expand those numbers by 16,000 to 17,000 people. That is a huge number at a cost of \$10 billion.

I have watched the private sector shrink dramatically under the nationalization of private sector policy that actually began under the Bush administration, was accelerated dramatically under the Obama administration. And by the way, everything that began under the Bush administration that sent us in that direction was supported by then-Senator Obama. There is no exit strategy to divest ourselves from the Federal consumption of the private sector. I did hear a notice that some of Citigroup might be spun off. I don't think there has been any action on that at this point. But you add to that ObamaCare, the student loan program all being nationalized, it is curious to me there is no exit strategy on the part of the Federal Government.

Do you find yourself in a position here to enforce tax policy? And again, I would compliment the workers and their intelligence and skills there. I think you know also by their reputation that I think they could also do very well in the private sector. So I don't have any hesitation about the skills.

I do have a couple of things that I would like to follow up on. With ObamaCare and the collection that you apparently will be soon required to carry out, can you tell me the discussion that has been in the open dialogue has been about the IRS having the authority to withhold a refund if one does not comply with the mandate to purchase insurance for their employees or perhaps as individuals, soul proprietors, partnerships, LLCs, et cetera? And does your power go beyond that, beyond withholding a refund? What about the tax lien component of the collection that the IRS, I expect, will be using when the refund is not a tool that is effective for them?

Mr. SHULMAN. Let me respond and give you a sense of what I view our role as and then get to your specifics. One is, as I mentioned in my opening statements, I think that there has been some irresponsible demonizing of the IRS around this health care debate. First of all, there is no 16,000 people out there that are going to be hired.

Mr. KING. How many?

Mr. SHULMAN. That was a number put out by a study. It wasn't put out by us.

Mr. KING. How many?

Mr. SHULMAN. So that number is just floating around. I don't have a number for you. Second of all—

Mr. KING. Excuse me, Mr. Commissioner. My clock is ticking here. I would point out that you did feel free to speculate on capital gains tax cuts, which has been floated by the administration, but not willing to talk about policy changes when Mr. Buchanan talked about the increase in small business taxes. So I just want to make sure that we are on a subject matter where that we can get definitive responses.

So do you have a number that you could give me as to how many IRS agents? If a person doesn't have a number, then how can they have a number that the number that is out there isn't accurate?

Mr. SHULMAN. I can argue about the number because I actually get to set how many agents are out there, and I haven't set how many people are out there. Second of all, what I was talking about, which I think is irresponsible, people throw around numbers like agents and 16,000 agents. Well, most of what we are going to have to do around the health care law is—

Mr. KING. Commissioner, my time is ticking here. If you are going to set the number, what will you set it at?

Mr. SHULMAN. I will finish and answer the question.

Mr. KING. There is 1 minute and 13 seconds left on our clock. I am sorry I have to be abrupt, but I would like to get a response if I could, please.

Mr. SHULMAN. Most of what we are going to spend our time on is building computer systems to get credits to people and administering tax law provisions. Right now there is no—

Mr. KING. Commissioner, I do have to interrupt you because you have not answered any of my questions. And I have asked if you have the authority to apply a tax lien beyond withholding someone's tax refund as a means to enforce ObamaCare. And I have asked you if you are going to set the numbers of agents or officers or employees of the IRS, and you disagree with the number at what you expect to set it at. If you will not answer either one of those questions, I don't think there is any reason for us to carry on this dialogue.

Mr. SHULMAN. The law specifically prohibits liens, levies and seizures. Most of what you can think about when you think about the requirement to buy insurance and the penalty to not have insurance is it will be like a 1099. The insurance company will send the employee and say either you have the insurance or you don't. They will send that same information. And a letter will go out. This is not the kind of thing that we have agents for.

Mr. KING. So how do you follow up?

Mr. MOORE. The gentleman's time has expired.

Mr. KING. Mr. Chairman, I ask unanimous consent for an additional minute.

Mr. MOORE. We have got one more person who needs to have a chance to ask questions here.

Mr. KING. Do I hear an objection?

Mr. MOORE. I am objecting.

Mr. KING. Okay, Mr. Chairman, let the record note that the witness refused to answer my questions and I have been gavelled down before I could get an answer. I apologize to the chairman for having to be rude and abrupt.

Mr. MOORE. Thank you, sir. Mr. Schrader, you are recognized for 5 minutes, sir.

Mr. SCHRADER. Thank you, Mr. Chairman. Mr. Commissioner, thank you for coming.

Mr. SHULMAN. Thank you.

Mr. SCHRADER. I guess I don't agree with everyone on the panel that would have individuals pay all the taxes in this country. I think there is a shared burden that needs to be going forward. I am a little surprised that some people seem to be suggesting that we need to increase taxes on individuals, especially in these very, very difficult times. I don't think America is really ready for that. I am interested in, you know, some of the recommendations that the taxpayer advocate has made. I came in late. I apologize if you have addressed this. But there are several changes regarding some of the check box things on form C and adding lines to form C that most small businesses file their returns with. Was that discussed at all? Are you familiar with that?

Mr. SHULMAN. No, it wasn't. And I am not sure exactly what you are talking about.

Mr. SCHRADER. Well, it is my understanding that for the last several years, the taxpayer advocate report had talked about making some changes to form C and trying to simplify it a little bit, make it a little bit more user-friendly for small businesses. Well, I will get to you later then to make it easier for you going forward.

We have also introduced a bill on home office deduction simplification. And hopefully that will lend its way through this Congress at some point in time. I am trying to make it easier for small businesses—I mean, really small business, mom and pop shops, shops with, you know, a token office in their home or residence, how they could take advantage of that. Do you see that as something being popular that a lot of business folks would end up taking advantage of going forward?

Mr. SHULMAN. I think the home office, figuring out which piece of that is an expense and not, is incredibly complicated for people. They are trying to figure it out. I would welcome simplification.

Mr. SCHRADER. I went through that a little bit when I started up my farm in trying to allocate a chunk of my house to that. I was trying to figure out the mortgage piece, the insurance piece, the property tax piece. It became very, very difficult. So some of that stuff would be very, very helpful. I guess the other comment I would be interested in is with regard to the health care bill. It looks like there is going to be a lot of tax credits for small busi-

nesses, particularly as they deal with some of the health insurance things.

I would assume that most small businesses are not aware of this, at least not to any great degree. Do you see a way we would be getting that word out to make sure small businesses concerned about health care in general but wanting to do the right thing, which I think most small business—my little veterinarian clinic included—try to do, how they can access some of the small business tax credits for many, many businesses out there?

Mr. SHULMAN. Yes. So obviously the recently passed health care bill is a big bill. It is a multi-year bill. And one of the reasons why I am unable to answer some of the things that will come into place in 2014 is the bill was just passed and we are focusing on the things we have to do this year. Just to be very clear and get on the record, what we are doing is administering the tax provisions, not the health provisions. The things that we have to do this year is get a credit program up and running, out to small businesses to help them pay for health care. There is a new tax on tanning salons. There is a therapeutic discovery credit to give tax grants to companies who come up with innovative ways and innovative therapies.

So that is what we are very focused on. The thing that is immediately effective is the small business tax credit. We have put out questions and answers. We have deployed our people who do lots of outreach to small business every day to make sure people know that this is available to them because we want people to get credits that are available to them. And we plan on doing a lot of outreach and would be able happy to do with any member of this committee outreach events in your district on this other or tax provisions and also on just general how IRS can help the open houses, things like that. So we are very focused on doing outreach on the early provisions in this law, just like we are with every law.

Mr. SCHRADER. I appreciate that because I think that is going to put money in the pockets of many small businessmen and women right now so they can improve their bottom line, hire people and expand their business. The last question would be, the Blue Dogs of which I am a member, are putting out a fiscal platform, trying to make sure we get our own fiscal house in order now that we have helped save the country. And what we are trying to do is, one of the elements is program integrity. Would you comment a little bit? One of the pieces is empowering the IRS. I happen to think that is a good thing, to make sure that some people who aren't paying their fair share in taxes pay their fair share. I don't mind paying mine. We get great services in my State, education, health care, public safety. There are some benchmarks you can use to figure out for a dollar of investment in the IRS, we can get something back?

Mr. SHULMAN. The general benchmarks we use—I am a big believer that compliance comes about because of service and enforcement. So we put a lot of money into service, trying to help people just to meet their tax obligations, understand the complex code. So the best benchmark we have is just a 5-1 return on the overall IRS budget and our dollars that are brought in—not the overall collection for the country but the dollars from direct IRS actions.

Depending on the program, though, we have up to 20-to-1 returns, some of our document matching programs. In our appropriation every year we have details about program by program, the return and we would be happy to share that with you.

Mr. SCHRADER. Thank you very much. I yield back.

Mr. MOORE. The gentleman's time has expired. The last questioner is Mr. Coffman. You have 5 minutes, sir.

Mr. COFFMAN. Thank you, Mr. Chairman. Commissioner Shulman, please know that my colleagues, for your employee that was lost in Texas, the families of the diseased are in our thoughts and prayers and very respectful of not simply his service to his country through the IRS, but his service to the country through the military prior to that.

Mr. SHULMAN. Yes.

Mr. COFFMAN. You all certainly do the best you can do under these challenging times.

Mr. SHULMAN. Thank you.

Mr. COFFMAN. I have a question about the new health care law. It will require you to develop a host of new forums, collection methods and implementation strategies. What is the timeline for these changes to develop this?

Mr. SHULMAN. Yes. So as I mentioned, there is a bunch of things that went into effect immediately. And that is what we have got a team working on right now. We also are putting teams together now to look at the longer-term impact of what happens. Most of the individual provisions and the employer provisions go into effect in 2014. So if you think about us building our systems, generally you want to have systems built a year ahead of time and then they are going to have to interface with the exchanges, insurance companies, employers because you think of us as the payment system around that. That means you need to get it designed in 2012 within a couple of years. Just so I am clear, I don't have numbers now, but we are diligently working on them and we are trying to scope this out. We have people going through the entire bill and we are hoping to be able to come to Congress in the near future and work out exactly what resources we are going to need in a lot more details.

Mr. COFFMAN. Is the time frame to have this up and running by 2014 realistic?

Mr. SHULMAN. I think it is. My understanding is that it was designed to give plenty of lead time. For us, we are running tax provisions which we do every day. A lot of times Congress passes things retroactively or passes things in December that we have to implement in January. So we are not through the entire bill but I am confident that if we have administrative flexibility and if we are given proper resources, that at least for our portion, we will be prepared by 2014.

Mr. COFFMAN. Do you have any feeling as to what the budgetary impact of that will be in terms of ramping up to meet the obligations of the bill?

Mr. SHULMAN. I don't right now. Obviously, CBO put a number out there which is the tradition. CBO puts out numbers which Congress votes on. I think it will be potentially in that range, but it is just really too early to say.

Mr. COFFMAN. Well, let's see. I think the Congressional Budget Office came up with this \$10 billion in costs, additional funds and 17,000 employees. Is that at all accurate in your view?

Mr. SHULMAN. Sir, the only number they came up with was \$5 billion to \$10 billion over 10 years. They didn't come up with an employee number. My understanding is—and we didn't do those numbers with them—is that they recognized a lot of that is technology interface to get the flow of funds back and forth. A lot of that is service and answering questions on the phone. So the employee number, I really don't know, as we had this discussion with your colleague. I think the broader numbers—we are still getting our arms around it but it could be within that range.

Mr. COFFMAN. So it could be in the 17,000 individual range?

Mr. SHULMAN. No, no, no. I am just talking about the number range.

Mr. COFFMAN. When do you think you will have the costs down and be able to project out the cost for the implementation as well as the number of personnel?

Mr. SHULMAN. I think we will be able to know the costs for the next year and a half provisions through fiscal year 2011 pretty soon. I think the rest really depends on design, a bunch of choices that are made, how these exchanges get set up, et cetera, because again, a lot of us, it is just flowing money and doing interchange on the money provisions, not on the health provisions, with the exchanges. So I really don't have a date for you exactly when.

Mr. COFFMAN. Okay. But the exchanges are not the enforcement?

Mr. SHULMAN. But the exchange is you sign up at an exchange and you get your tax credit in exchange and it is based on tax data. So there is going to be a lot of information flow going back and forth.

Mr. COFFMAN. Okay. Very well. Madam Chairman, I yield back the balance of my time.

Chairwoman VELÁZQUEZ. [presiding.] Mr. Graves.

Mr. GRAVES. Thank you, Madam Chairwoman. Commissioner, could you walk me through? Obviously, we have been talking a lot about health care and what your role is going to be. But would you walk through with me what your role is going to be with the verification process, kind of clarify that? As far as verifying whether or not, a small business has complied with the mandate or is that going to be part of the collection process beyond that?

Mr. SHULMAN. So let me give you as much as I can right now with me still getting up to speed on this because it is a new provision and it doesn't go into effect for a while. One is with individuals who will be required to have adequate health insurance, the way that I think this is going to work is, first of all, I want to be 100 percent clear, IRS is not going to be involved in any way in the sensitive health matters of individuals. I think HHS and insurance companies will work out what adequate coverage means. We will get a simple yes/no information return from the insurance company, the same information return—think of it like a 1099 will get sent to the individual which will say, attach this to your tax return and show that you had coverage or you are going to have to have a fee that you pay, and we will get that same thing that says, Yes, they had it or no, they didn't.

So I think of it similar to a 1099 right now that we get for dividend income where we get information from a brokerage firm about your dividends and we go off of that information. So it will be information reporting and information matching.

For employers, the shared responsibility provision, as I understand it, it is only for people who employ more than 50 employees. And if they don't offer health insurance and an employee goes into an exchange and gets federally subsidized health insurance and gets a benefit and again, I think we will administer that like we administer anything else. People will pay in. If we see a lot of employees that are getting subsidized insurance from an employer and they haven't self-reported that, that will trigger something. But we haven't really worked through any of the compliance programs.

Mr. GRAVES. Do you foresee problems with if an individual doesn't attach their verification or says that they have got their health insurance, goes ahead and sends in their return, goes through the process? Are still going to have to go ahead and charge them the penalty for not doing that or you will have to verify it someplace? That is going to be a horrendous issue trying to figure out how you are going to move forward. Because, there are going to be people out there who just aren't going to attach that or aren't going to comply or whatever the case may be. But is that burden going to fall on you completely to then make a phone call to—you don't even know who the insurance company is, for that matter.

Mr. SHULMAN. We will get an information return from the insurance company and we match that against the return of the individual. I don't even know that they will need to attach it because we will have the information, and they will get a letter. And we have automated programs right now where if you don't report your interest from your bank but we get information from your bank that you had interest you will get a letter. Or we can make an adjustment on your return, and so I think it will work very much like that. I think of this like other tax provisions that we administer.

Mr. GRAVES. Thank you, Madam Chair.

Chairwoman VELÁZQUEZ. Commissioner Shulman, the new uncertainty tax position reporting will apply to business taxpayers with assets in excess of \$10 million. Was it even considered that there are numerous small businesses that have equipment, land and inventory that might push them above this threshold and will face increased reporting compliance costs?

Mr. SHULMAN. Yes. So that is our standard number where we put people into large business. There is no specific definition of large or small business, but the 10 million cutoff is what we use for electronic filing, it is what we use. It gets you out of our small business division into our large business division. It is \$10 million and having audited financials so audited financials that are audited under the standard where you have to take a reserve for uncertain tax positions. And so this proposal which is an important one of ours is looking at basically getting a list of where people think that they have uncertain tax positions. We are in the notice and comment period and we ask specifically about the \$10 million asset question and ask is that the right threshold.

Chairwoman VELÁZQUEZ. Would the IRS consider raising the \$10 million threshold?

Mr. SHULMAN. We haven't seen the comments yet, when we are in comment period and ask for specific questions, absolutely. I mean, we would consider anything depending on the comments and the persuasiveness of them.

Chairwoman VELÁZQUEZ. Commissioner, many CPAs work as apprentices before taking the CPA exam, performing most of their returns and then having a manager review it. Likewise, many law graduates or financial planners begin work while waiting to hear the results of their licensing exams. Because they are not licensed they will likely have to complete education training and testing processes increasing cost for small CPA firms and other tax professionals.

Has the IRS considered any way to differentiate for exemption purposes between professionals with advanced training from other licensed preparers with little, if any, advanced tax education?

Mr. SHULMAN. Frankly, no one has brought this specific issue about a apprentices to my attention. What we are trying to do is make sure that a lot of our licensing and registration focus was on people who are really filling out the tax return, really doing the work, that the people that American people think are providing them service and then they ship it off, someone else's name is on it and those people disappear. A lot of it has been focused on low income communities where people run these EITC mills.

Chairwoman VELÁZQUEZ. Yes.

Mr. SHULMAN. And people aren't qualified to do the work. We exempted CPAs, attorneys, enrolled agents out of this requirement because they already have a professional credential. We certainly, as we move into this, are going to have to have a bunch of discussions about this exact kind of example and make sure that it makes sense. My main goal is the people who are interfacing with the American taxpayers are qualified and provide good service. And so if there is protections built in other ways, we certainly would look at that.

Chairwoman VELÁZQUEZ. Very good.

Commissioner, the deadline for the home buyers tax credit will occur in a few weeks. Based on 2009 returns, do you have data on the number of and type of individuals who have claimed a credit? And are you able to determine if the credit boosted home sales?

Mr. SHULMAN. I think generally people think the credit boosted home sales and helped at least stabilize the housing market from its dramatic decline that was going on a year ago when it was put in place. We don't have that data parsed right now. We are trying to keep up and make sure we process credits and get refunds out quickly. And so we usually do an after-the-fact analysis to see where it is, we would be happy to work with your staff.

Chairwoman VELÁZQUEZ. At this point, you don't have any data on the number of and type of individuals who claimed the credit?

Mr. SHULMAN. I don't have it off the top of my head. We might have some more that we can get to you.

Chairwoman VELÁZQUEZ. Ranking member, do you have any other questions? Mr. Schrader? If not I ask unanimous consent that members will have 5 days to submit a statement in supporting ma-

terials for the record. Without objection so ordered. This hearing is now adjourned. Thank you.

[Whereupon, at 3:14 p.m., the committee was adjourned.]

NYDIA M. VELAZQUEZ, NEW YORK
CHAIRWOMAN

SAM GRAVES, MISSOURI
RANKING MEMBER

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STATEMENT

Of the Honorable Nydia M. Velázquez, Chairwoman
United States House of Representatives, Committee on Small Business
Full Committee Hearing: *“Entrepreneurs and Tax Day: How IRS Policies and
Procedures Impact Small Businesses”*
Wednesday, April 14, 2010

With Tax Day now just hours away, most Americans are wrapping up their paperwork, looking forward to 12 months without touching a W2. For many small business owners, however, the process is still underway. The weak economy, along with a series of new tax measures, has compounded its historic complexity, making the process of filing a small business tax return especially challenging.

This is not the first time our committee has met to discuss the tax challenges facing small firms. In the past, small businesses have told us that complexity is the most stubborn of those obstacles. With good reason—entrepreneurs face more than 200 IRS forms and schedules. The process of navigating this maze of regulations is not only complex, it is expensive and time-consuming. Businesses with fewer than 20 workers spend roughly \$1,300 per employee on tax compliance and, according to one IRS study, up to 80 hours. At a time when many businesses are struggling, every hour counts and so does every dollar.

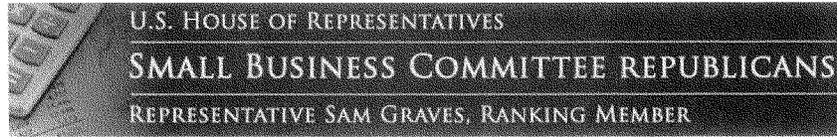
This afternoon, we will discuss the role that the IRS plays in helping entrepreneurs meet their tax obligations, and examine the agency’s management of certain Recovery Act tax incentives.

Last year, Congress passed one of the largest and most sweeping tax cuts in U.S. history. The Recovery Act incorporated \$15 billion in relief for entrepreneurs, including provisions to not only put cash back in their pockets, but to increase demand for their products, such as the first-time homebuyers tax credit. Now, we need to be asking whether or not those refunds—and their resulting economic boost—are being dispersed effectively. With the economy still struggling, it could use a fresh influx of circulating capital, and it is critical that the IRS do everything it can to stoke—rather than restrict—our economic recovery.

But as one study recently found, that isn't happening. Since 2005, the agency has increased its small business audits by 30%. Meanwhile, audits of large companies dropped 21%. I understand that, in light of our nation's fiscal constraints, closing the \$345 billion tax gap is critical to our long-term prosperity. But so are small businesses. These are the companies that create 70% of new jobs, and will play a leading role in rebuilding our economy. Any effort to increase our tax base must be done in a way that is responsible, fair and not unduly burdensome to small businesses.

Small firms should be able to look to the IRS as an ally—not an enemy. Given the myriad of available small business schedules and incentives, entrepreneurs need to know they can count on the IRS to address their concerns quickly and answer their questions accurately. The agency's move to increase staff levels within its Small Business/Self Employed program should be an important step in delivering those resources, and I was pleased to see Commissioner Shulman place a greater emphasis on small firms overall. In this afternoon's conversation, we will discuss the improvements he's made and look to see if more can be done.

Tax law operates most effectively when small businesses have certainty and stability, and now is the time for policies that deliver both. Now is the time for incentives that encourage would-be entrepreneurs to start up, and existing businesses to expand. With the proper tools, America's small firms can strengthen the economic recovery that is currently underway, and spark the job creation we are waiting to see.



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**Opening Statement for Hearing:
"Entrepreneurs and Tax Day: How IRS Policies and Procedures Impact Small
Businesses"
Sam Graves
Ranking Member
House Committee on Small Business
United States House of Representatives
Washington, D.C.
April 14, 2010**

Madam Chairwoman, thank you for calling this important hearing on tax issues affecting small businesses. Special thanks to Commissioner Shulman for testifying today.

Unemployment is hovering around 10%. New home sales are still falling. Consumer confidence is low, and our government's rampant spending could soon jeopardize the United States' AAA credit rating that keeps borrowing affordable.

The unsustainable policies of government bailouts, skyrocketing federal spending, higher taxes and record national debt have had a devastating effect on small businesses. In order to hire new workers, expand operations, and help our economy, entrepreneurs and small business owners need certainty. However, right now, the only thing that is certain for small business owners is more taxes and regulations.

Today's businesses are facing more uncertainty than ever as they try to determine the real impact that the new health care law will have on their families, their business, and their community. I am particularly concerned about who will enforce the new health care

mandates on individuals and small businesses, and how much it will cost. Estimates on this information vary, and no one seems to know the real answers. Initiating such a massive overhaul of health care without first having a clear understanding of the cost and impact is a recipe for disaster.

In addition to the health care law's \$569 billion in tax increases, employers must be wary of other tax hikes that may be just around the corner. The expiration of the 2001 and 2003 tax cuts threatens to raise the capital gains rate on dividends from the current 15% for middle class taxpayers and 20% for higher income earners to as much as much as 45%. This is not the kind of policy that will allow small business owners to expand and create jobs.

Rather than increasing taxes and unfairly punishing small businesses, one of the best steps we can take to help small business owners is simplifying the tax code. The IRS Taxpayer Advocate reported that U.S. taxpayers and businesses spend about 7.6 billion hours a year complying with filing requirements. In fact, tax complexity has been consistently ranked as the number one issue facing both taxpayers and the IRS. By making it easier for small businesses to navigate the tax code, we can save them time and the expense of hiring tax professionals.

Churchill once said that a nation trying to tax itself into prosperity is like a man standing in a bucket and trying to lift himself up by the handle. Forcing the small business owners that create the majority of private sector jobs to carry the financial burden of damaging Washington initiatives will only lead to more unemployment and fewer opportunities for Americans.

Madam Chairwoman, thank you for holding this hearing. I look forward to Commissioner Shulman's testimony.

**WRITTEN TESTIMONY
OF
DOUGLAS H. SHULMAN
COMMISSIONER OF INTERNAL REVENUE
BEFORE THE
HOUSE SMALL BUSINESS COMMITTEE
“Tax Matters Affecting Small Businesses”
APRIL 14, 2010**

Introduction

Chairwoman Velazquez, Ranking Member Graves and members of the Committee, thank you for this opportunity to testify about the Internal Revenue Service’s (IRS) continuing efforts to assist small business at a time when the economy has yet to rebound fully.

Among the key steps the IRS has taken is to show greater flexibility in dealing with taxpayers, including small businesses, who are having difficulty meeting their tax obligations. The IRS has moved swiftly during the past 15 months to implement new tax law provisions intended to help small businesses. This includes the recently enacted Hiring Incentives to Restore Employment (HIRE) Act, a law designed to provide an impetus for America’s businesses to start hiring again.

The IRS is also proceeding to publicize and administer tax provisions of the Affordable Care Act , signed into law in late March. The Act created a tax credit for qualified small businesses to support providing health insurance coverage for their employees. The IRS has already begun an outreach campaign to contact small businesses that may qualify for this important credit.

The IRS’s actions reflect our commitment to service, one of the IRS’s most important goals as it goes about its mission of administering and enforcing the nation’s tax laws. We provide world-class service to the vast majority of taxpayers trying to pay their taxes and contend with a complex tax code. Individuals and business owners just want to get the bottom line of their returns – what they owe – correct. Most taxpayers want to pay their tax liability while not missing a deduction or credit that they are due.

An example of this extended effort to reach taxpayers can be seen in the IRS’s plan to hold special Saturday open houses. The next one will be in May. Small businesses will be able to come in and work with the IRS to find ways to meet their federal tax obligations, while keeping their businesses up and running.

Excellent service by the IRS supports compliance and lessens the need for enforcement, a subject that I will say more about later in this testimony. But as I’ve said in the past, there isn’t a tradeoff between service and enforcement. It isn’t an either/or proposition. The IRS needs to do both well. As IRS Commissioner, I, and the tens of thousands of dedicated employees proudly working for the American people, remain committed both

to collecting the revenue needed to fund government and using all the tools we have available to work with small businesses, which may find themselves struggling in a difficult time.

The IRS needs to ensure fairness. Public trust requires taxpayers, regardless of size or position, pay what they owe and comply with the tax system. This same trust, however, also requires that the IRS be flexible and principled and respond appropriately to taxpayers with financial troubles. Fairness, in difficult times, requires compassion.

The small business community needs the IRS to get this aspect of service right. Too many small business owners continue to struggle to make their payroll, secure lines of credit, provide health insurance coverage, contribute to their employees' retirement plans and stay current with their taxes. As Commissioner, I have sought to give our employees the guidance and discretion they need to assist small businesses with the service they need and deserve.

Implementing New Laws Intended to Help Small Business

Beginning with the American Recovery and Reinvestment Act of 2009 (ARRA), Congress and the Administration have shown continued focus on providing valuable tools to assist small business in tough economic times. The sustained effort launched by ARRA was continued in the Worker, Homeownership and Business Assistance Act of 2009 (WHBAA) signed into law in November. Last month brought more significant action. The Hiring Incentives to Restore Employment (HIRE) Act was signed into law in mid-March, and the following week President Obama signed the Affordable Care Act.

Each of these new laws assists small businesses through important tax provisions. Each new law required the IRS to demonstrate its commitment to service through aggressive outreach and skillful administration. To do so, the IRS must update forms, write new instructions and develop guidance and administrative procedures that smooth the way for small businesses to take advantage of new deductions and credits. And the IRS must get the word out. Take for example, the laws enacted last month. These tax provisions offer an incentive to hire new workers. They offer incentives for small businesses to retain or provide health insurance coverage for employees.

The HIRE Act 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. Employers who wish to take this incentive will still need to continue withholding the employee's share of these taxes. 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 tax provisions of the HIRE Act reward small businesses who give an unemployed worker one of the best helping hands there is, a job.

Employers will be able to begin claiming this new tax incentive on their second quarter 2010 employment tax form. Information and answers to frequently asked questions have also been posted on IRS.gov to assist small businesses in using these important credits.

Help for small businesses through tax credits extends beyond the act of hiring workers. The Affordable Care Act offer billions in tax credits over ten years for small businesses to provide health insurance to their employees. These tax incentives first become available for 2010 and many small businesses and nonprofits that provide health insurance coverage to their employees now qualify for the tax credit.

The credit is designed to encourage small employers to offer health insurance coverage for the first time or maintain coverage they already have. The credit, which is effective immediately, can cover up to 35 percent of premium contributions paid by eligible small business employers and 25 percent of premium contributions paid by eligible employers that are tax-exempt organizations.

The credit especially benefits small businesses and nonprofits that primarily employ low- and moderate-income workers. It is generally available to employers that have fewer than 25 full-time equivalent (FTE) employees paying wages averaging less than \$50,000 per full-time employee per year. Because the eligibility formula is based in part on the number of equivalent full-time employees (FTEs), not the number of workers, many employers will qualify even if they have more than 25 actual workers.

The maximum credit goes to smaller employers with lower paid workers—10 or fewer FTEs with annual average wages of \$25,000 or less.

Eligible small businesses can claim the credit as part of the general business credit starting with the 2010 income tax return they file in 2011. Eligible tax-exempt organizations claim it on their quarterly payroll tax return.

An initial set of questions and answers describing the credit is now available on IRS.gov. Additional guidance will be posted on the IRS Web site over the next few weeks.

Recovery and Net Operating Losses

The American Recovery and Reinvestment Act of 2009 (ARRA) allowed certain businesses with a net operating loss (NOL) in 2008 to carry back this loss against income earned for five years instead of the normal two years. This enabled small businesses with large losses in 2008 to benefit right away, instead of waiting to carry these losses forward against future income. The benefit of this carryback is straight forward. It generates a refund of taxes paid in previous years, throwing a lifeline to businesses hard hit by the downturn, providing them with a quick infusion of cash.

Under ARRA, to qualify for this special treatment of NOLs, a small business could have no greater than an average of \$15 million in gross receipts over the three-year period that ended with the tax year of the NOL. Businesses with more than \$15 million in gross

receipts still qualified to carry back their 2008 NOL for two years. In November, however, Congress passed the Worker, Homeownership, and Business Assistance Act of 2009 (WHBAA) that broadened eligibility and included the special treatment of NOLs to include losses incurred in both 2008 and 2009.

Since ARRA's enactment in February 2009, more than 42,000 businesses have claimed NOL carryback adjustments to taxes paid in up to the prior five years. These carryback adjustments have totaled more than the \$2.6 billion on returns processed through late January 2010. With the expansion of the NOL provision in WHBAA, the IRS expects to see continued use of this important provision.

Generally, small businesses that are not corporations, including sole proprietorships filing Schedule C with their Form 1040, may accelerate a refund by using Form 1045, Application for Tentative Refund. The IRS has increased its staffing to process carryback claims from NOLs and management has closely monitored these filed claims to ensure that refunds are expedited. This process allows taxpayers to receive their refunds much faster. In most cases, taxpayers using the Form 1045 will receive their refund in 4 to 6 weeks. This has proven to be a huge help to taxpayers in these difficult economic times.

Having the right information available for small businesses, so that their managers and owners know about the special treatment of NOLs in 2008 and 2009, is critical. Questions and Answers have been posted on the IRS Web site, IRS.gov. These were updated to reflect not only the original ARRA treatment, but help businesses understand the expansion of NOL treatment in November's WHBAA.

Small businesses that file Form 1040 can also call 1-800-829-1040 with NOL questions. Corporations can contact 1-800-829-4933 with NOL questions.

ASSISTING SMALL BUSINESS TAXPAYERS

Before I turn to describe in detail what the IRS is doing to reach out to and assist small business, I wanted to assure the committee that the President's Budget meets IRS's needs and will be used to carry out the IRS's strategic and balanced agenda that includes improved service to all taxpayers, including assistance to small businesses, such as administering and publicizing recovery-related provisions discussed earlier in my testimony.

Providing quality taxpayer service is especially important to help taxpayers avoid making unintentional errors. Small businesses, from sole proprietors who file Form 1040 with a Schedule C to the owners of corporations with up to \$10 million in assets, face the task of familiarizing themselves with many complex aspects of the tax code. Some of these provisions change from year to year, so a prior year understanding may need to be revised. Assisting taxpayers with the questions before they file their returns prevents inadvertent errors and reduces burdensome post-filing notices and other correspondence

from the IRS. The President's Budget provides the resources for the staffing, outreach and service that is needed.

The Administration's legislative proposals also include a measure that will assist small business owners. Under the proposal, the percentage exclusion for qualified small business stock sold by an individual or other non-corporate taxpayer would be increased permanently to 100 percent. Further, the AMT preference item for gain excluded under this provision would be eliminated. As under current law, the stock would have to be held for at least five years and other limitations on the section 1202 exclusion would continue to apply. The proposal would include additional documentation requirements to assure compliance with those limitations.

General Outreach to Small Businesses

Getting the word out to these small businesses on changes to tax laws and the latest in filing requirements is an important part of what the IRS does. This outreach reflects the wide-spread use of tax professionals by the owners of these businesses. More than 80 percent of the small businesses and the self-employed use professional return preparers. As a result, the IRS partners with thousands of industry and small business organizations, including minority-owned business associations, tax professional and payroll associations and other government agencies to extend and amplify our outreach and education efforts.

This outreach and education involves communicating important messages ranging from how to avoid compliance problems in numerous areas of tax law to IRS burden reduction initiatives. This effort involves thousands of symposia, seminars and professional and industry meetings attended by more than 181,000 small business owners and tax professionals in Fiscal Year 2009. Nor has the IRS limited itself to getting the word out through meetings and conferences. The IRS works diligently to leverage new technology, from the use of Webinars to creating specialized small business pages on IRS.gov, to extend our ability to communicate about important developments in tax law and other changes in tax administration pertinent to small business. A fuller picture of this outreach can be found in Appendix A of this testimony.

I want to highlight one element of this outreach, an effort that reflects my emphasis on IRS help for taxpayers in tough times. We have organized taxpayer education and problem-solving days, especially for small businesses. Many small businesses and self-employed taxpayers are still in the midst of financial difficulties affecting their ability to timely meet federal tax obligations and maintain their business. At these events, IRS staff will work with small businesses and the self employed to find solutions that meet both the IRS's and small businesses' needs in an economy that is just starting to show signs of rebound.

Many of the latest developments and efforts to inform the small business community can be found on our web site. Our web site has a comprehensive section for small business and self-employed taxpayers. A wide range of video and audio presentations is available to educate small business and self-employed individuals on their federal tax

responsibilities. Archived versions of live studio broadcasts and webinars are also available. A separate section, Filing Season Central, is a one-stop resource for filing and paying business returns. This resource provides tax law change highlights, tax tips, and information on the electronic IRS.

The Virtual Small Business Tax Workshop is a new free Web application, making tax information more accessible to small businesses and tax professionals, while at the same time protecting taxpayer privacy and security. The workshop provides training to small business owners on navigating federal taxes and contains interactive features, convenience of 24/7 availability, and is updated as tax law changes take effect.

New technology increases our ability to get the word out and communicate directly with taxpayers on issues that affect them and we continue to try and identify better means of communicating to taxpayers. Through IRS.gov, the IRS leverages this ability to reach the audience it seeks, small business and the self-employed, and give these important taxpayer communities the information they need to comply with tax law and learn of new developments, such as tax credits or deductions, that may lower their tax liability.

The IRS also operates business toll-free numbers, dedicated specifically to small businesses, corporations, partnerships and trusts. These entities need information and/or help related to their business returns or business accounts. The services provided include Employer Identification Numbers, 941 series returns, 1041, 1065, 1120S, excise returns, estate and gift returns, as well as issues related to federal tax deposits.

We also offer a nationwide, toll-free, professional support line staffed by IRS representatives specially trained to handle tax practitioners' questions. This is a valuable resource practitioners may use in resolving their clients' account-related issues including business account problems, complex refunds or general information.

The dissemination of IRS published products remains a vital vehicle for agency outreach. These include tax calendars for small business, available in both English and Spanish. These calendars are filled with useful information to start and maintain a small business. Each month highlights a different tax topic, providing resources, reminders, instructions and important dates. A DVD version of the Virtual Small Business Tax Workshop is available and can be requested by small business owners, unable to attend the workshop.

Electronic publications, such as E-News for Tax Professionals, provides consolidated and localized information for tax practitioners and others on a state-by-state basis. Another bi-weekly newsletter, E-News for Small Business, provides information affecting the small business community including recent news releases, special IRS announcements, new information on IRS.gov, and tax compliance reminders.

SSA/IRS Reporter, a newsletter, is sent to more than one million business recipients each quarter. This publication is a collaborative effort between the Social Security Administration and the IRS, available in both English and Spanish. Stories support employment and business tax compliance, with an emphasis on educating and

encouraging electronic filing. The Reporter also carries general information about best payroll and employment tax practices and IRS and SSA products and services.

IRS Assistance to the Unemployed

In addition to focused efforts on small business, we also understand that economic difficulty is shared by employees as well. IRS assistance to the unemployed remains a key component of the service we provide. Times are tough for many people, and the IRS wants to do everything it can to help people who have lost their job or face financial strain. In March, I announced new steps — an expansion of efforts that began more than a year ago — to assist taxpayers. These include additional flexibility on offers in compromise for struggling taxpayers, a series of Saturday “open houses” offering taxpayers extra opportunities to work out tax problems face-to-face with the IRS, special outreach with partner groups to unemployed taxpayers and the availability of more information on a special section of the IRS Web site.

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.

Hundreds of Saturday Open Houses to Resolve Taxpayer Issues

In addition, IRS began holding hundreds of special Saturday open houses to give struggling taxpayers more opportunity to work directly with IRS employees to resolve issues. One of these “open houses” recently took place on March 27. Three additional Saturday open houses will take place in the spring and early summer. Future dates, times and locations will be announced soon.

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 American Recovery and Reinvestment 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 Your Local Office page on IRS.gov. To get to this page, select the link 'Contact IRS' at the top right of IRS.gov.

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 Web site, IRS.gov, called Tax Center to Assist Unemployed Taxpayers. 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 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 paying.
- Additional review of home values for offers in compromise in cases where real-estate valuations may not be accurate.
- 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.

IRS Compliance and Examination Program

Even with today's economic situation, even as the IRS has sought to make certain that our service to small business meets high standards, we must also carry out a rigorous enforcement program. This includes administering our examination program that helps assure that taxpayers accurately report their income, deductions or credits. This includes administering our collection program, which seeks to collect assessed tax liabilities.

We continue to run a robust examination program with an increased focus on large corporations and high-wealth individuals. For example, the number of individuals examined with income \$1 million and higher increased from 21,874 in FY 2008 to 28,349 in FY 2009. We also ensure that our examination program is well-balanced and ensure that adequate coverage is placed on all areas, including individuals, small business and flow-through entities.

In going about this work, the IRS recognizes that many small businesses still face substantial challenges. We have worked diligently to communicate to our employees the importance of recognizing that individual taxpayers and businesses being audited find themselves, trying to deal with economic hardships. As Commissioner, I have stressed that we need to take taxpayers as they come, and ensure we treat them fairly and compassionately. Toward this end, I've sought to empower our employees to be flexible and principle as they deal with taxpayers.

As part of this effort to make sure, the IRS is responding appropriately. IRS operating divisions that interact with small businesses continue their effort to coordinate issues more than ever before. Our Small Business examination group continues working with Appeals to find faster ways to resolve audit issues that may have reached an impasse. Our Fast Track Settlement initiative process allows taxpayers and their representatives to meet with both exam and appeals personnel to discuss unresolved issues, explore alternative resolutions that can achieve a mutually-agreeable resolution to disagreements. Such approaches reduce the duration of audits and can ease burden on taxpayers.

National Research Program (NRP), the Tax Gap

I would like to turn now to the tax gap. The tax gap for a given tax year is the difference between taxpayers' true total tax liability and what they actually paid on a timely basis.

In 2006, based on the work of the National Research Program, the IRS updated the estimate for the overall gross tax gap for Tax Year 2001. This figure was \$345 billion. IRS enforcement activities – examinations, collection and the receipt of late payments – is expected to recover about \$55 billion of that tax gap, leaving a net tax gap of \$290 billion for Tax Year 2001.

The updated estimates of the tax gap showed that the largest component of the gap, more than 80 percent, comes from underreported taxes. More specifically, these underreported taxes are primarily income taxes. The remainder of the tax gap consists of nonfiling and

underpayment of taxes that are reported as owed. Finding ways to get taxpayers to do a better job reporting their income would clearly help lower the tax gap.

While the latest estimates are for Tax Year 2001, the National Research Program (NRP) is in the final stages of a multi-year project on individual reporting compliance, the largest component of the tax gap, using a new approach to sampling. The method adopted should enable tax gap estimates to be updated beginning in 2011.

This approach entails using smaller annual samples of 13,000 individual returns over a rolling three-year period. The first returns of this study came from Tax Year 2006. Examinations for Tax Year 2008, the final year required before we can revise the tax gap estimate, have just begun. This individual underreporting gap involves an important component of the small business community: sole proprietors who file a Schedule C as part of their 1040, their annual income tax return.

Last fall, the IRS also began a research study on employment taxes to enable the IRS to understand problems in this area and to find ways to improve compliance. This is the first time the IRS has conducted an employment tax compliance study since the early 1980s. I know this area has been an interest of this committee. Business practices regarding employment tax issues may have changed since then, making this study necessary. This research should contribute to updating an estimate of the employment tax underreporting gap and to assisting the IRS in how best to focus its resources to address noncompliance.

Conclusion

Madam Chairwoman, I want to thank you again for the opportunity to testify today on the IRS's ongoing efforts to help small business owners as they seek to rebound economically, hire new workers and put their enterprises on a path of growth and prosperity. We have made progress in our efforts to assist small business, but more needs to be done. We look forward to working with you, the Committee and staff to see to it that small business, an engine of economic growth, can move full-speed ahead and flourish.

Appendix: Small Business Outreach and Education

To reach small businesses and self-employed taxpayers, the IRS participated in over 2,400 meetings, symposiums and seminars attended by over 181,000 small business owners and tax professionals in FY 2009. For FY10, through December, we have hosted 917 events with 112,678 direct participants. Additionally, in FY10, 482 small business workshops in 46 states have been held through partnership with other associations and agencies.

These outreach and education efforts include the following:

Small Business and Practitioner Forums

- IRS held 114 Small Business Forums with the trade and industry groups that represent small business owners in FY 2009.
- Members receive the latest small business and tax information from IRS. Topics are generated from the IRS Strategic Plan and requests from practitioner and industry partners.
- The Forum process allows partners to learn about IRS programs, policies and procedures and to alert IRS to burden issues. Systems are in place to collect and resolve systematic issues raised by practitioner and industry stakeholders.
- Topics presented in FY 2009 and FY 2010 to date:
 - ARRA and Economic Stimulus – including both Individual and Business incentives
 - Cancellation of Debt
 - Offers in Compromise
 - Online Installment Agreements
 - Report of Foreign Bank and Financial Accounts (FBAR)
 - Fast Track Settlement
 - Electronic filing and payment options, Electronic Account Resolution, and navigating IRS.gov
 - Determining when an activity is a business or hobby
- Attendees include the following organizations:
 - American Institute of Certified Public Accountants
 - National Association of Enrolled Agents
 - National Association for the Self Employed
 - National Federation of Independent Business
 - National Small Business Association
 - Small Business Administration
 - Small Business Legislative Council
 - National Payroll Consortium
 - Independent Payroll Provider Association
 - U.S. Chamber of Commerce
 - Better Business Bureau

Nationwide Tax Forums (NTFs)

- IRS sponsored six NTFs with over 14,000 participants in FY 2009.
- In 2010, six Nationwide Tax Forums will be held in cities across the U.S. These three-day symposiums provide tax professionals the opportunity to earn continuing education credits.

Problem Solving Days for Small Business and Self Employed

- Scheduled events for taxpayer to receive information on how to maintain and/or create a business and receive tax assistance with unresolved tax issues.

IRS Phone Forums

- Eleven Phone Forums and Webinars were attended by over 28,000 tax professionals and small business owners in FY 2009.
- These forums included the following topics:
 - Recordkeeping for Small Businesses
 - IRS e-File
 - Correcting Employment Taxes 2009
 - Return Preparer Penalties Under IRC 6694
 - S-Corp
 - Cancellation of Debt
 - Proper classification of workers
 - Disaster Preparedness
 - Collection Topics
 - Identity Theft
 - Form 8300
- Seven Phone Forums and Webinars attended by almost 15,000 tax professionals and small business owners so far in FY 2010.
- These forums included the following topics:
 - Homebuyer Credit
 - Electronic Interactions
 - Getting ready for the filing season.
 - EITC
 - Navigating IRS.gov
 - TE/GE 1099's
 - Employment tax issues

IRS Electronic Newsletters

- IRS offers free e-mail subscriptions to e-News for Small Business Owners that include the latest IRS news releases and announcements. This publication has about 173,000 subscribers.
- IRS offers free email subscriptions to e-News for Tax Professionals. This electronic publication has nearly 176,000 subscribers.

Small Business Tax Workshops

- IRS facilitated 1,852 Small Business Tax Workshops in FY 2009.
- These structured workshops for small business owners cover tax topics from starting up to closing down a business.

Tax Practitioner Institutes

- IRS partners with colleges and universities to provide high quality continuing education to tax professionals.
- In FY 2009, we participated in 471 events attended by 39,000 practitioners.

IRS Tax Centers

- We work with industry and tax professional partner organizations to leverage key messages and information to their members and clients. To date almost 1,700 IRS Tax Centers are established on websites providing industry-specific guidance.

IRS.gov

- Our award-winning website has a comprehensive section for small business and self-employed taxpayers.
- A wide range of video and audio presentations is available to educate small business and self-employed individuals on their federal tax responsibilities. Archived versions of live studio broadcasts and webinars are also available.
- Filing Season Central is a one-stop resource for filing and paying business returns. This resource provides tax law change highlights, tax tips, and information on the electronic IRS.
- The Virtual Small Business Tax Workshop is a new free Web application, making tax information more accessible to small businesses and tax professionals, while at the same time protecting taxpayer privacy and security. The workshop provides training to small business owners on navigating federal taxes and contains interactive features, convenience of 24/7 availability, and is updated as tax law changes take effect.

Business toll-free number

- Dedicated specifically to small businesses, corporations, partnerships and trusts who need information and/or help related to their business returns or business

accounts. Services cover Employer Identification Numbers, 94x returns, 1041, 1065, 1120S, excise returns, estate and gift returns, as well as issues related to federal tax deposits.

- Practitioner Priority Service® is a nationwide, toll-free, professional support line staffed by IRS representatives specially trained to handle tax practitioners' questions. PPS is a valuable resource practitioners may use in resolving their clients' account-related issues including business account problems, complex refunds or general information.

Published Products

- Tax Calendar for Small Business is available in both English and Spanish and is filled with useful information to start and maintain a small business. Each month highlights a different tax topic, providing resources, reminders, instructions and important dates.
- A DVD version of the Virtual Small Business Tax Workshop is available.
- SSA/IRS Reporter is sent to more than one million business recipients each quarter. This newsletter is a collaborative effort between the Social Security Administration, IRS, and others, available in both English and Spanish. Stories support employment and business tax compliance, with an emphasis on educating and encouraging electronic filing. The Reporter also carries general information about best payroll and employment tax practices and IRS and SSA products and services.



April 14, 2010

The Honorable Nydia Velázquez
 Chair
 House Small Business Committee
 2361 Rayburn House Office Building
 U.S. House of Representatives
 Washington, D.C. 20515

The Honorable Sam Graves
 Ranking Member
 House Small Business Committee
 B-363 Rayburn House Office Building
 U.S. House of Representatives
 Washington, D.C. 20515

Dear Chairwoman Velázquez and Ranking Member Graves:

On behalf of Associated Builders and Contractors (ABC), a national organization with 77 chapters representing 25,000 merit shop construction and construction-related firms with 2 million employees, we appreciate the opportunity to provide our position in response to the House Small Business Committee's hearing entitled, "Entrepreneurs and Tax Day: How IRS Policies and Procedures Impact Small Businesses." ABC strongly supports minimizing the tax burden on the construction industry to help increase the rate of capital formation, economic growth and job creation.

Tax relief is extremely important to the open shop construction industry and small businesses. One of the greatest obstacles to increased economic growth and higher standards of living is our nation's complex and ever changing tax code. The current tax code disproportionately affects small businesses, which are forced to expend significant time and resources in order to comply with the extensive, complicated and burdensome tax code.

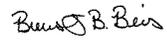
Specifically, the 1986 Tax Act required contractors to use the "percentage of completion method" of accounting and to apply "look-back" calculations to contracts lasting over one year. The "look-back" rule requires that when a contract is completed the contractor must "look-back" and substitute the actual costs and revenues for the estimated costs and revenues that were used in the percentage of completion calculations. The contractor calculates the difference between the taxes paid on the previously estimated amounts and what would have been paid on the actual amounts, as well as interest, and determines whether money is either owed or due to the Department of Treasury (Treasury).

Look-back calculations can number in the *thousands* and can take between 15 to 30 hours to complete for each job open at year-end. These calculations must be performed many times once for each year the contract is in progress, again under the post-completion adjustment rules if additional work is requested, and again if any revenue or cost results from a claim or dispute. Construction contractors pay thousands of dollars to comply with look-back requirements, while there is virtually no monetary impact on the Treasury. Also, ABC members have experienced difficulty in receiving the refund for "look-back" payments to the Department of Treasury when a payment is owed.

Additionally, small construction contractors are unable to utilize the Completed Contract Method (CCM) under Section 460 of the Internal Revenue Code if average annual gross receipts exceed \$10 million. This threshold has not been indexed for inflation, and therefore, small construction contractors are unable to use this method that more clearly reflects taxable income. CCM is the optimal method for matching contractor profits with tax payments, as the profits from the contracts are not reported until the contract is complete.

Small businesses are the backbone of our economy and give Americans a sense of pride and accomplishment in our country. In the construction industry, they provide valuable jobs and play an integral role in building communities. Lessening the tax burden on individuals will encourage small business owners and construction companies to reinvest in their businesses, thus expanding the economy. We look forward to working with you to provide tax relief to small businesses.

Sincerely,



Brewster B. Bevis
Senior Director, Legislative Affairs

