

WRITTEN STATEMENT OF

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HEARING ON

INTERNAL REVENUE SERVICE FY 2015 BUDGET REQUEST

BEFORE THE

SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

COMMITTEE ON APPROPRIATIONS

UNITED STATES SENATE

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Chairman Udall, Ranking Member Johanns, and distinguished Members of this Subcommittee:

Thank you for inviting me to submit this statement regarding the proposed budget of the Internal Revenue Service for FY 2015.¹

As you know, the IRS's budget has been cut substantially since FY 2010, and because of sequestration, the cuts last year were the most substantial to date. As a result of these resource reductions, the IRS's ability to meet the service needs of the taxpaying public has been severely impaired, and the agency has made unprecedented and disturbing changes to its delivery of taxpayer service.

The 16-day government shutdown compounded the impact of these budget cuts and affected the IRS's ability to prepare for the 2014 tax filing season. As a result, the agency delayed the start of the filing season by 10 days, requiring early filers to wait additional time to receive their tax refunds. During the shutdown, moreover, thousands of taxpayers were exposed to IRS enforcement actions but had no ability to contact IRS employees, including the Taxpayer Advocate Service, all of whose employees were furloughed and unable to assist taxpayers who experienced emergencies caused by ongoing enforcement.²

On top of all this, the revelations by the Treasury Inspector General for Tax Administration (TIGTA) that the IRS's Exempt Organizations unit had used a "Be on the Lookout" (or "BOLO") list to select applicants with the

¹ The views expressed herein are solely those of the National Taxpayer Advocate. The National Taxpayer Advocate is appointed by the Secretary of the Treasury and reports to the Commissioner of Internal Revenue. However, the National Taxpayer Advocate presents an independent taxpayer perspective that does not necessarily reflect the position of the IRS, the Treasury Department, or the Office of Management and Budget. Congressional testimony requested from the National Taxpayer Advocate is not submitted to the IRS, the Treasury Department, or the Office of Management and Budget for prior approval. However, we have provided courtesy copies of this statement to both the IRS and the Treasury Department in advance of this hearing.

² During the shutdown from October 1 through October 16, 2013, taxpayers were subject to the following compliance and enforcement actions: 3,902 levies on Social Security benefits; 5,455 levies on financial or other accounts; 7,025 wage levies; 4,099 Notices of Federal Tax Lien issued; 180,095 Automated Underreporter Statutory Notices of Deficiency; and 102,231 Collection Due Process Levy Hearing Notices issued by the Automated Collection System. Preliminary information from IRS Office of Taxpayer Correspondence, Individual Master File (IMF), and Automated Lien System.

words “tea party” and other political-sounding names for further review undermined public trust in the fairness and impartiality of the IRS, and led to multiple investigations that are still underway. Getting the IRS back on track requires not merely strong leadership within the agency, but helpful oversight and support from Congress and other key stakeholders. For that reason, I appreciate your holding today’s hearing.

In my view, the IRS is often so focused on resolving immediate crises that it is not able to devote sufficient time to setting long-term goals and developing approaches to achieve those goals. In the preface to my most recent annual report to Congress, I attempted to provide my vision of what a 21st century tax administration system should look like.³

As a foundational matter, tax administration in the 21st century should be premised on a thematic, principle-based Taxpayer Bill of Rights.⁴ If taxpayers believe they are treated, or can be treated, in an arbitrary and capricious manner, they will mistrust the system and be less likely to comply voluntarily. If taxpayers have confidence in the fairness and integrity of the tax system, they will be more likely to comply.

The good news on this front is that the Internal Revenue Code provides dozens of taxpayer rights. The bad news is that most taxpayers have no idea what their rights are and therefore often cannot take advantage of them. That is because taxpayer rights are scattered throughout the code and are not presented in a coherent way. Not surprisingly, in response to a taxpayer survey conducted for our office in 2012, less than half of all U.S. taxpayers said they believed they have rights before the IRS, and only 11 percent said they knew what those rights are.⁵

We can and must do a better job of making taxpayers aware of their rights and enabling them to assert them. Since 2007, I have repeatedly

³ National Taxpayer Advocate 2013 Annual Report to Congress [hereinafter “NTA 2013 Annual Report”], at x.

⁴ See NTA 2013 Annual Report 5-19 (Most Serious Problem: *Taxpayer Rights: The IRS Should Adopt a Taxpayer Bill of Rights as a Framework for Effective Tax Administration*); NTA 2011 Annual Report 493-518 (Legislative Recommendation: *Enact the Recommendations of the National Taxpayer Advocate to Protect Taxpayer Rights*); NTA 2007 Annual Report 478-489 (Legislative Recommendation: *Taxpayer Bill of Rights and De Minimis “Apology” Payments*).

⁵ Forrester Research Inc., *The TAS Omnibus Analysis*, from North American Technographics Omnibus Mail Survey, Q2/Q3 2012 19-20 (Sept. 2012).

recommended adoption of a Taxpayer Bill of Rights that takes the multiple existing rights embedded in the code and groups them into ten broad categories, modeled on the U.S. Constitution's Bill of Rights.⁶ Just as the Constitution's Bill of Rights sets out the relationship between the federal government and U.S. citizens and imposes limits on the federal government's power, I believe a thematic, principle-based list of core taxpayer rights would provide a foundational framework for taxpayers and IRS employees alike that would promote effective tax administration.

I am very pleased the House of Representatives passed my proposal verbatim last year, with bipartisan support, on a voice vote.⁷ While I believe a Taxpayer Bill of Rights should have the force of law, and therefore hope the Senate passes this legislation, the IRS has the authority to adopt a Taxpayer Bill of Rights on its own. I have been working with the IRS leadership to try to get agreement to do so. Particularly when resources are dear, it is important to have a set of foundational principles that guide operations and serve as a framework for effective tax administration.

In my testimony today, I will elaborate on the following key issues:

1. **Taxpayer Services and IRS Funding.** The IRS is failing badly at meeting taxpayer needs because it lacks resources.⁸ Last year, the IRS received some 109 million telephone calls on its customer service lines. The IRS could answer only 60.5 percent of calls

⁶ Congress has passed several pieces of legislation with "Taxpayer Bill of Rights" in the title. See Technical and Miscellaneous Revenue Act, Pub. L. No. 100-647, § 6226, 102 Stat. 3342, 3730 (1988) (containing the "Omnibus Taxpayer Bill of Rights," also known as TBOR 1); Taxpayer Bill of Rights 2, Pub. L. No. 104-168, 110 Stat. 1452 (1996) (also known as TBOR 2); Internal Revenue Service Restructuring and Reform Act, Pub. L. No. 105-206, 112 Stat. 685 (1998) (Title III is known as "Taxpayer Bill of Rights III" or TBOR 3). These laws create specific rights in certain instances, but they do not create a thematic, principle-based list of overarching taxpayer rights.

⁷ Taxpayer Bill of Rights Act, H.R. 2768, 113th Cong. (2013). In my 2013 report, I suggested some wording modifications, and as discussed below, the Office of the Taxpayer Advocate recently tested our proposed modifications with focus groups of taxpayers and preparers to assess whether the language accurately conveys the gist of the rights we have identified. Based on input from the focus groups, we are currently tweaking the language of a few provisions.

⁸ See NTA 2013 Annual Report 20-38 (Most Serious Problem: *IRS Budget: The IRS Desperately Needs More Funding to Serve Taxpayers and Increase Voluntary Compliance*).

seeking to reach a customer service representative (CSR) – and those taxpayers who got through had to wait an average of 17.6 minutes on hold. Initial statistics for fiscal year (FY) 2014 through April 15 indicate service has remained at low levels, with taxpayers waiting an average of slightly more than 17 minutes and tax practitioners kept on hold for nearly 27 minutes.⁹ The tax collector is rarely the government's most popular agency, but at the end of the day, IRS funding reductions do not "punish" the IRS nearly as much as they punish the nearly 150 million individual taxpayers and more than 10 million business entity taxpayers who are trying to comply with the tax laws and not receiving the help they need. When the IRS receives 109 million telephone calls, there is no substitute for the funding to hire enough CSRs to answer them. If the IRS does not receive more funding, it will be unable to assist millions of taxpayers seeking assistance from their government to comply with the tax laws.

2. **Erosion of IRS Employee Training and Skills.** To deal with a complex, constantly changing tax law and provide taxpayers with accurate and complete service, IRS employees must receive prompt and appropriate training and education. Since FY 2009, budget cuts and sequestration have led the IRS to cut its training budget by over 85 percent. The IRS has reduced its training and education programs to a bare minimum without considering the types of training employees need to perform basic job functions, protect taxpayer rights, and prevent harm to and undue burden for taxpayers.¹⁰
3. **Identity Theft and Refund Fraud.** The IRS should establish a meaningful single point of contact for taxpayers who become victims of identity theft. Today, 21 separate units handle different aspects of identity theft, and although the IRS says it has adopted a single point of contact, no employee has the authority to coordinate the entirety of the taxpayer/victim's case if, as is common, more than one of the 21 units is involved. Thus, taxpayers traumatized

⁹ IRS, Joint Operations Center, Executive Level Summary report (Oct. 1, 2013 through April 15, 2014).

¹⁰ See NTA 2013 Annual Report 40-50 (Most Serious Problem: *Employee Training: The Drastic Reduction in IRS Employee Training Impacts the Ability of the IRS to Assist Taxpayers and Fulfill Its Mission*).

by the crime of identity theft are forced to navigate the IRS by themselves, increasing their frustration and despair.¹¹ The IRS also takes much too long to resolve ID theft cases and issue refunds to legitimate taxpayers. The Taxpayer Advocate Service's experience with identity theft cases demonstrates the soundness of our recommendation that the IRS assign one employee to work with the victim from the beginning, and help coordinate resolution of the case (not merely monitor it) when it requires work by multiple units.

4. **Affordable Care Act.** As part of the Affordable Care Act (ACA), the IRS is implementing complicated health care tax provisions. I believe the IRS has acquitted itself well in meeting its initial responsibilities under the ACA. At the same time, I have concerns about the IRS's approach to addressing taxpayer questions and adequately training employees on the new provisions. In particular, the IRS is not doing enough to educate taxpayers about the importance of updating their information throughout the year with the Exchange if they are receiving a credit. Our office will continue to work with the IRS to ensure that taxpayers are treated properly and fairly in the implementation of the new law. Within TAS, we are also training our employees about taxpayer concerns they are likely to see next year, such as the impact of premium tax credit reconciliation and under- and overpayments, so they will be properly prepared to assist taxpayers.¹²
5. **Accelerated Receipt and Use of Third-Party Information Reports.** Congress should direct the IRS to develop a plan to enable it to match information return data against tax return data before paying out refunds.¹³ If the IRS could match Forms 1040

¹¹ See NTA 2013 Annual Report 75-83 (Most Serious Problem: *Identity Theft: The IRS Should Adopt a New Approach to Identity Theft Victim Assistance that Minimizes Burden and Anxiety for Such Taxpayers*).

¹² See generally National Taxpayer Advocate Fiscal Year 2014 Objectives Report to Congress 29 (*TAS Prepares for Implementation of Health Care Provisions*); IRS: *Enforcing Obamacare's New Rules and Taxes: Hearing Before the House Comm. on Oversight & Gov't Reform*, 112th Cong. (2012) (statement of Nina E. Olson, National Taxpayer Advocate).

¹³ See NTA 2013 Annual Report, vol. 2, 67-96 (Analysis: *Fundamental Changes to Return Filing and Processing Will Assist Taxpayers in Return Preparation and Decrease Improper Payments*). The National Taxpayer Advocate has been recommending this approach since 2009. See National Taxpayer Advocate 2009 Annual Report to Congress 338-345 (Legislative Recommendation: *Direct the Treasury Department to Develop a*

against Forms W-2 in a pre-refund environment, it could dramatically reduce improper payments to identity thieves and other perpetrators of refund fraud, including some improper Earned Income Tax Credit claimants. At the same time, it could make the data available to taxpayers and thereby help them prepare their returns more accurately and easily.

6. **IRS Information Technology Challenges**. The IRS's Information Technology (IT) function must be adequately funded, not only to deliver on major initiatives like the ACA and Foreign Account Tax Compliance Act (FATCA), but also to deliver on the many small but important improvements and projects that will make a positive difference for taxpayers, employees, and the public fisc. At present, the IRS is focusing its IT resources almost exclusively on the ACA, FATCA, and the 2015 filing season. All other IT requests are subordinate to these three programs. Thus, important taxpayer service and compliance initiatives are at risk because needed improvements cannot be developed or implemented, compounding harm to taxpayers. Furthermore, without dedicated funding to invest in projects that bring us into the 21st century and the digital age, the IRS will increasingly lag behind other tax administrators and the financial services sector.

I. Taxpayer Services and IRS Funding

The requirement to pay taxes is generally the most significant burden a government imposes on its citizens. For that reason, I believe the government has a practical and moral obligation to make compliance as simple and painless as possible. Yet the IRS is increasingly unable to meet the service needs of our taxpayers by phone, in person, and by mail. Consider the following:

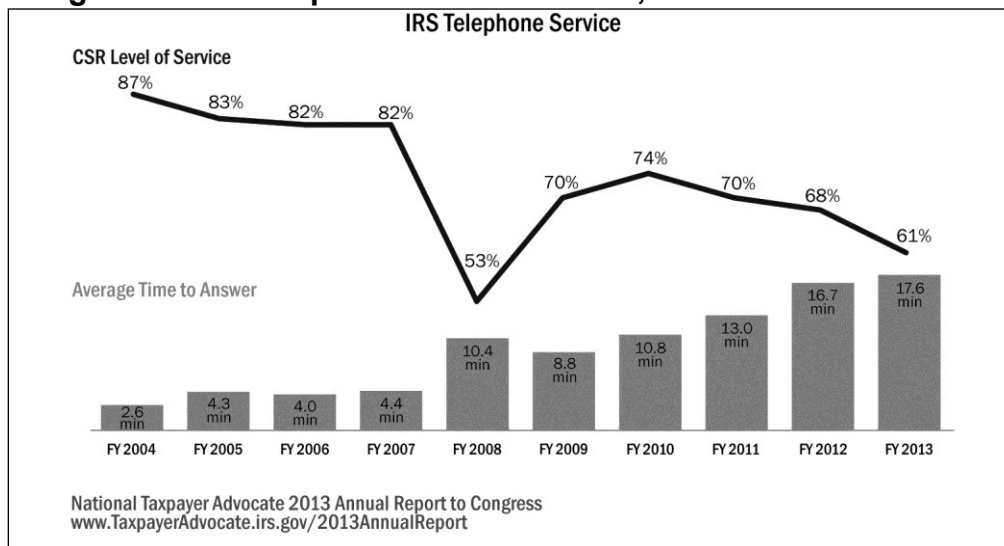
- Despite the greater availability of information on IRS.gov, the number of telephone calls the IRS receives from taxpayers on its customer service lines has been rising steadily over the past decade – from 71 million calls in FY 2004 to 109 million calls in

Plan to Reverse the “Pay Refunds First, Verify Eligibility Later” Approach to Tax Return Processing).

FY 2013, an increase of 53 percent.¹⁴

- The IRS lacks the staffing to answer these calls. In FY 2004, the IRS answered 87 percent of calls from taxpayers seeking to speak with a CSR (which, in IRS parlance, is referred to as the “Level of Service” or “LOS”). In FY 2013, the IRS answered only 61 percent of such calls, a reduction of 26 percentage points, or 30 percent, in the LOS. Among those taxpayers lucky enough to get through, hold time increased from 2.6 minutes to 17.6 minutes, a nearly six-fold rise.¹⁵

Figure 1: IRS Telephone Service Levels, Fiscal Year 2004-2013



- The IRS historically has prepared tax returns for low income, elderly, and disabled taxpayers seeking assistance at its walk-in sites (known as “Taxpayer Assistance Centers,” or “TACs”). In FY 2004, the IRS prepared 476,000 returns.¹⁶ Since that time, the IRS has imposed increasing limits on return preparation, and by

¹⁴ IRS, Joint Operations Center, *Snapshot Reports: Enterprise Snapshot* (final week of FY 2013 and FY 2004).

¹⁵ IRS, Joint Operations Center, *Snapshot Reports: Enterprise Snapshot* (final week of each fiscal year for FY 2004 through FY 2013).

¹⁶ This data was provided to TAS by the IRS Wage & Investment Division in connection with the National Taxpayer Advocate’s 2007 Annual Report to Congress 162-182 (Most Serious Problem: *Service at Taxpayer Assistance Centers*).

FY 2013, the number of returns it prepared during the filing season had declined by 59 percent as compared with FY 2004.¹⁷

- The IRS's ability to timely process taxpayer correspondence has also taken a hit. When the IRS sends a taxpayer a notice proposing to increase his or her tax liability, it gives the taxpayer an opportunity to present an explanation or documentation supporting the position taken on the return. Each year, the IRS typically receives around ten million taxpayer responses, known collectively as the "adjustments inventory."¹⁸ The IRS has established timeframes for processing taxpayer correspondence, generally 45 days. During the final week of FY 2004, the IRS failed to process 12 percent of its adjustments correspondence within its timeframes. By contrast, during the final week of FY 2013, the IRS was unable to process 53 percent of adjustments correspondence within these timeframes.¹⁹

As compared with FY 2013, the IRS's ability to assist taxpayers has suffered further declines in FY 2014:

- For FY 2014 through April 15, the LOS on the phones was 66 percent, down from 71 percent during the same period in FY 2013. Among taxpayers who got through, hold time rose from 13.3 minutes to slightly over 17 minutes. For practitioners calling the Practitioner Priority Service line, the decline was even steeper. The LOS dropped from 82 percent to 72 percent, while hold time rose

¹⁷ Government Accountability Office, GAO-14-133, *2013 Tax Filing Season: IRS Needs to Do More to Address the Growing Imbalance between the Demand for Services and Resources* 26 (Dec. 2013); GAO, GAO-11-111, *2010 Tax Filing Season: IRS's Performance Improved in Some Key Areas, but Efficiency Gains Are Possible in Others* 45 (Dec. 2010); GAO, GAO-07-27, *Tax Administration: Most Filing Season Services Continue to Improve, but Opportunities Exist for Additional Savings* 29 (Nov. 2006) (supplemented with IRS data provided to TAS for 2004 through 2006).

¹⁸ In FY 2013, receipts in the Adjustments Inventory were about 8.4 million, as compared with 10.4 million in FY 2012. We are not certain why the number declined. The Adjustments Inventory is one component of the Accounts Management function's overall Paper Inventory. In FY 2013, receipts in the Paper Inventory were about 20.8 million, and the percentage classified as overage at year-end was 47 percent. IRS, Joint Operations Center, *Account Management Information Report (AMIR) – National Summary* (week ending Sept. 28, 2013).

¹⁹ IRS, Joint Operations Center, *Adjustments Inventory Reports: July-September Fiscal Year Comparison (FY 2004 through FY 2013)*.

from 12 minutes to 26.7 minutes.²⁰

- In an effort to answer more calls, the IRS posted an announcement on IRS.gov in December that said it will answer only “basic” tax-law questions on its phone lines and in its walk-in sites during the filing season (January through mid-April).²¹ It will not answer any questions that are “more detailed” than “basic” during the filing season. Moreover, it will not answer any tax-law questions after mid-April, including “basic” questions from the millions of taxpayers who obtain filing extensions and prepare their returns later in the year.

Here are some examples of “complex” tax law questions that the IRS no longer will answer from its taxpayers:

I deliver pizzas for my employer using my car. How can I deduct my car expenses?

I received a 1099-MISC instead of a Form W-2 for my new job, how do I report this on my tax return?

Do I have to report the inheritance I received?

I have started selling some craft items I make as a hobby. Do I have to report that?

These questions are really directional questions – how should I approach this issue? When the IRS is unable and unwilling to answer questions such as these, it increases the compliance burden on its taxpayers and the risk that taxpayers will get incorrect advice from other quarters. Thus, the decision to answer only basic tax law questions through the filing season, and not answer any “complex” question at all, will have a negative effect on tax compliance.

²⁰ IRS, Joint Operations Center, Executive Level Summary reports (comparing the periods of Oct. 1, 2013 through April 15, 2014 with Oct. 1, 2012 through April 15, 2013).

²¹ IRS, e-News for Tax Professionals – Issue Number 2013-49, Item 4, *Some IRS Assistance and Taxpayer Services Shift to Automated Resources* (Dec. 20, 2013), at <http://www.irs.gov/uac/Some-IRS-Assistance-and-Taxpayer-Services-Shift-to-Automated-Resources>.

- Also to conserve resources, the IRS announced that it will no longer prepare any tax returns at its walk-in sites, even for low income, elderly, or disabled taxpayers.²²

At the risk of vast understatement, it is a sad state of affairs when the government writes tax laws as complex as ours – and then can answer nothing beyond “basic” questions from baffled citizens who are doing their best to comply.

I realize that some may find it difficult to justify increased funding for the IRS. I personally have concerns about IRS performance, and in fact, I am required by statute to be an “IRS critic” by identifying at least 20 of the most serious problems facing taxpayers in my annual reports to Congress.²³ But I must tell you that I do not see any way the agency can begin to meet the service needs of the taxpaying public without substantially more funding. Most notably, almost twenty million phone calls from taxpayers seeking to speak with a customer service representative went unanswered last year. With phone calls up about 17 percent and IRS funding down 8 percent since FY 2010, there is no way the IRS can answer all these calls without more employees.

In part because of mistakes made in the past, the agency has undergone significant leadership changes in recent months. Many policy changes have been made in response to congressional concerns, and the FY 2014 appropriations act contains new directives. If Members have continuing concerns, I encourage you to use the oversight process to try to address them. But I personally believe it is a mistake to cut the IRS’s budget and thereby preclude the agency from providing basic service to millions of taxpayers who seek help each year. When we ask our taxpayers to turn over a significant portion of their incomes to the government, we owe it to them – the constituents you represent, and the taxpayers for whom I advocate – to ensure we have the infrastructure in place to help them comply with the requirements Congress has imposed by law.

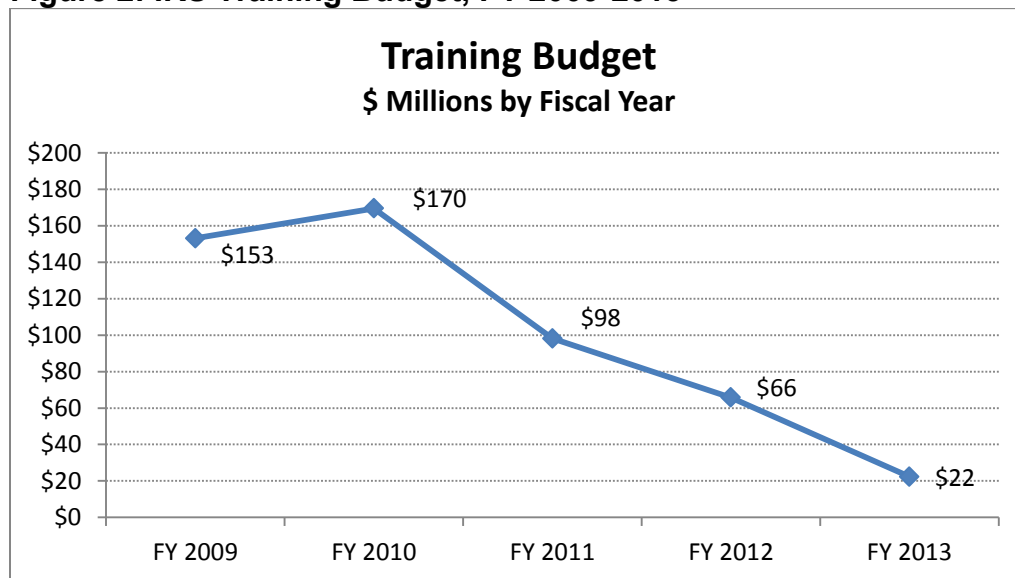
²² IRS, e-News for Tax Professionals – Issue Number 2013-49, Item 4, *Some IRS Assistance and Taxpayer Services Shift to Automated Resources* (Dec. 20, 2013), at <http://www.irs.gov/uac/Some-IRS-Assistance-and-Taxpayer-Services-Shift-to-Automated-Resources>.

²³ See IRC § 7803(c)(2)(B)(ii)(III).

II. Erosion of IRS Employee Training and Skills

The IRS mission is to “provide America’s taxpayers top-quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.”²⁴ With a complex and constantly changing tax law, it is essential that IRS employees receive prompt and appropriate training and education in order to provide taxpayers with complete and accurate assistance. However, budget cuts and sequestration have led the IRS to reduce its training budget by over 85 percent since FY 2009.²⁵ Per-employee spending dropped from nearly \$1,450 per full-time equivalent employee in 2009 to less than \$250 in 2013.²⁶

Figure 2: IRS Training Budget, FY 2009-2013



Most of the operating divisions that interact directly with taxpayers fared worse than the agency as a whole. The IRS Appeals division reduced its

²⁴ Internal Revenue Manual (IRM) 1.1.1.1, *The IRS Mission* (Mar. 1, 2006).

²⁵ IRS response to TAS research request (Nov. 22, 2013). In FY 2009, the IRS spent \$153,155,686 on training versus \$22,574,539 in FY 2013, a reduction of 85.26 percent. The IRS training budget includes both training and conferences.

²⁶ IRS, Human Resources Reporting Center, available at <https://persinfo.web.irs.gov/> (last visited Oct. 22, 2013).

training budget from nearly \$6 million in FY 2009 to about \$250,000 in FY 2013, or almost 96 percent.²⁷ During the same period:

- The Tax Exempt and Government Entities (TE/GE) division slashed its training budget by almost 96 percent, or approximately \$7 million;
- The Small Business/Self-Employed (SB/SE) division training budget declined by 93 percent;
- The Large Business and International (LB&I) division training budget fell by about 92 percent;
- The Taxpayer Advocate Service (TAS) decreased its training budget by almost 78 percent; and
- The Wage and Investment (W&I) division fared the best, with a decrease of “only” approximately 74 percent.²⁸

Not only has the IRS reduced the funding and number of hours of training for employees, it has also cut the number of courses offered and eliminated entire subject areas. In FY 2009, SB/SE offered over 2,000 different in-person and virtual learning courses to its Revenue Officers (ROs, who conduct all field collection), compared to just over 900 in FY 2013, a nearly 60 percent decrease. Other job series saw even more drastic cuts. TE/GE Tax Examiners were offered 166 in-person training courses in FY 2009 but only *three* in FY 2013, a 98 percent decrease.²⁹

We want the IRS to treat taxpayers fairly and to assess the correct amount of tax and to protect taxpayer rights in its interactions with taxpayers. After several years of continuing and drastic cuts to training, U.S. taxpayers cannot have confidence that IRS employees will be able to fulfill these expectations. IRS funding for training (and travel related to in-person training) must be restored to 2009 levels.

²⁷ IRS response to TAS research request (Nov. 22, 2013).

²⁸ *Id.*

²⁹ *Id.*

III. Identity Theft and Refund Fraud

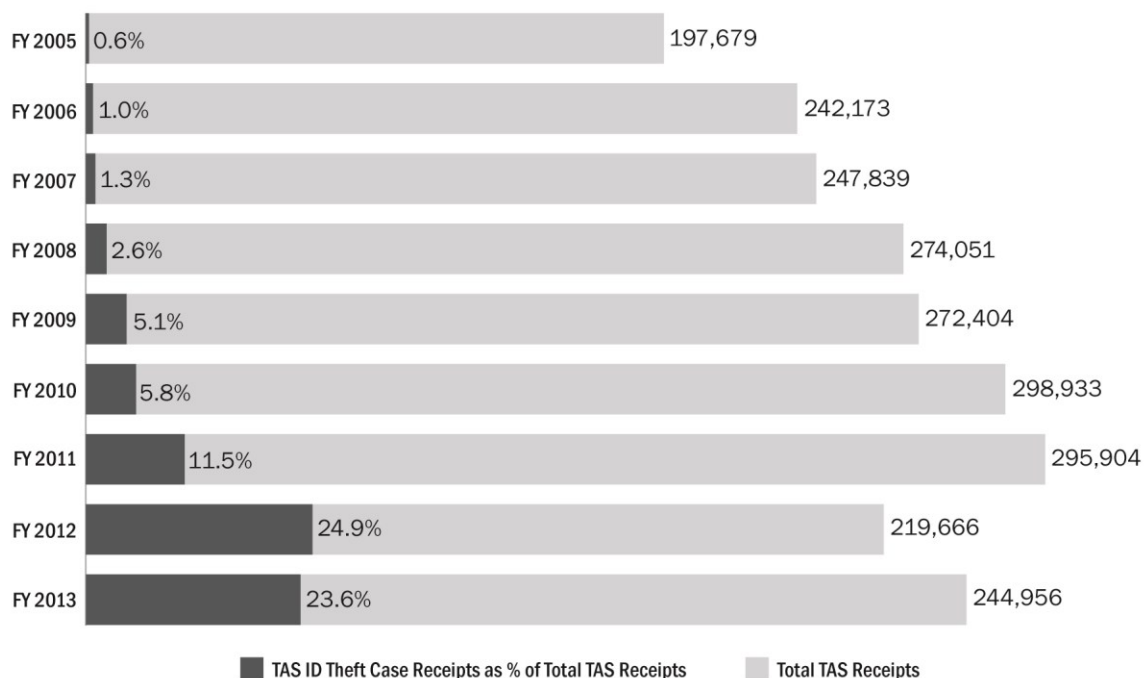
As I have written in nearly every Annual Report I have delivered to Congress since 2004, tax-related identity theft is a serious problem – for its victims, for the IRS and, when Treasury funds are improperly paid to the perpetrators, for all taxpayers.³⁰ In general, tax-related identity theft occurs when an individual intentionally uses the Social Security number of another person to file a false tax return to obtain an unauthorized refund.³¹

Within my organization, the Taxpayer Advocate Service, identity theft receipts increased sharply over the past decade, accounting for approximately one out of four cases in our inventory in recent years.

³⁰ See National Taxpayer Advocate 2013 Annual Report to Congress 75-83 (Most Serious Problem: *The IRS Should Adopt a New Approach to Identity Theft Victim Assistance that Minimizes Burden and Anxiety for Such Taxpayers*); National Taxpayer Advocate 2012 Annual Report to Congress 42-67 (Most Serious Problem: *The IRS Has Failed to Provide Effective and Timely Assistance to Victims of Identity Theft*); National Taxpayer Advocate 2011 Annual Report to Congress 48-73 (Most Serious Problem: *Tax-Related Identity Theft Continues to Impose Significant Burdens on Taxpayers and the IRS*); National Taxpayer Advocate 2009 Annual Report to Congress 307-317 (Status Update: *IRS's Identity Theft Procedures Require Fine-Tuning*); National Taxpayer Advocate 2008 Annual Report to Congress 79-94 (Most Serious Problem: *IRS Process Improvements to Assist Victims of Identity Theft*); National Taxpayer Advocate 2007 Annual Report to Congress 96-115 (Most Serious Problem: *Identity Theft Procedures*); National Taxpayer Advocate 2005 Annual Report to Congress 180-191 (Most Serious Problem: *Identity Theft*); National Taxpayer Advocate 2004 Annual Report to Congress 133-136 (Most Serious Problem: *Inconsistence Campus Procedures*).

³¹ The IRS refers to this type of tax-related identity theft as “refund-related” identity theft. In “employment-related” identity theft, an individual files a tax return using his or her own taxpayer identifying number (usually an Individual Taxpayer Identification Number or ITIN), but uses someone else’s SSN to obtain employment. Consequently, the wages are reported to the IRS under the SSN of the victim, potentially prompting the IRS to pursue the victim for additional tax on the apparent income. See IRM 10.5.3.2(4), *Identity Protection Program Servicewide Identity Theft Guidance* (Feb. 27, 2013). Unlike in 1993, when I first represented a client in an identity theft case, the IRS now has procedures in place to minimize the tax administration impact to the victim in these employment-related identity theft situations. Accordingly, I will focus on refund-related identity theft in this testimony.

Figure 3: Taxpayer Advocate Service ID Theft Cases³²
TAS Identity Theft Case Receipts, FY 2005-FY 2013



When we first started writing about tax-related identity theft in 2004, the IRS had no procedures for its employees to follow when a taxpayer claimed to be a victim of ID theft. Since then, the IRS has established a program office to develop victim assistance procedures and has adopted many of the recommendations we have made over the years. The IRS also has done a better job of developing automated filters that flag suspicious returns and delay the payout of refunds while the refund claims are scrutinized, and it has improved some of its victim assistance procedures.

³² Case receipt data obtained from the Taxpayer Advocate Management Information System (TAMIS) on February 13, 2014.

Yet, the IRS still has much room for improvement in how it addresses identity theft. First, it must recognize that the consequences for victims can be significant. Being victimized by an identity thief is a traumatic life event; when someone steals and uses your identity, it is an invasion of your person. On top of that, the victim must spend time and energy having to prove his or her identity to the IRS and must endure months of aggravation and frustration before receiving his or her tax refund, a delay that can create financial hardships for taxpayers – particularly low income taxpayers – who are expecting and depending on their tax refunds to pay basic living expenses. The IRS's current approach in many ways treats the victim as someone experiencing a minor inconvenience, instead of a frightening personal trauma.

In acknowledging that identity theft is a traumatic life event, the IRS should set up a centralized identity theft unit similar to the innocent spouse unit that assists taxpayers who are seeking relief from joint and several liability. It is important to have a centralized unit with specially trained employees who can remain on the case as a single point of contact with the victim from the beginning to full case resolution. Otherwise, the IRS would be guilty of contributing to the problem and perpetuating the trauma to the victim. When I visited the IRS Identity Protection Specialized Unit (IPSU) unit last summer, I met with front-line employees, many of whom expressed frustration about not truly “owning” a case and having to wait for other functions to take actions on these cases that the IPSU could have easily completed.

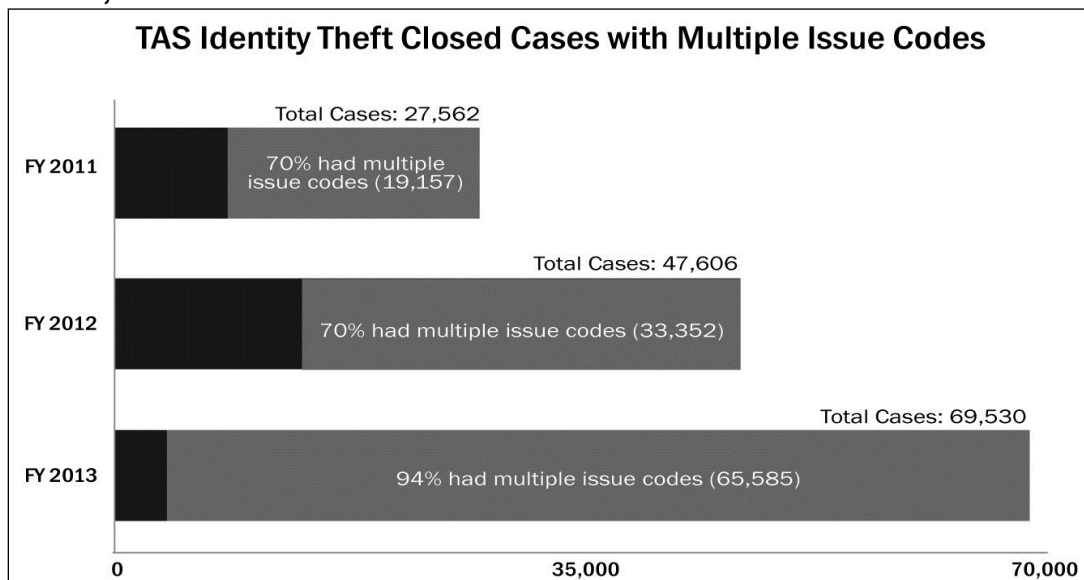
In my latest report to Congress, I recommended that the IRS designate the IPSU as the centralized function that assigns a single employee to work with ID theft victims until all related issues are resolved. In my meetings with the new IRS leadership, they have expressed willingness to revisit whether the current decentralized approach is the right one. I have offered to collaborate with the Wage and Investment division to test the effectiveness of creating a meaningful single point of contact for victims of identity theft with cases that require the involvement of multiple IRS functions (for example, where the taxpayer is not only trying to get a current year's return refund but also seeking abatement of an assessment attributable to a prior year's identity theft return).

The IRS takes much too long to resolve ID theft cases and issue refunds to the legitimate taxpayers, particularly where the case moves back and forth among IRS functions. A 2013 TIGTA report found the IRS took an

average of 312 days to work the 100 ID theft cases in the report sample.³³ This included 277 days of inactivity. In other words, though the cases lingered in various IRS units for approximately ten months, the average case in TIGTA's sample was resolved with just 35 days of direct contact.

The IRS's current approach of using more than 20 specialized units to handle discrete aspects of an identity theft victim's case is simply not working. As far as the victims are concerned, there should be *one* IRS employee who interacts with the taxpayer. That one employee should maintain control of the taxpayer's case, including all peripheral issues stemming from the identity theft. Because identity theft cases are often very complex, and can involve multiple issues spanning multiple years, too many victims fall between the cracks of the IRS bureaucracy.

Figure 4: Percentage of TAS ID Theft Cases with Multiple Issue Codes, FY 2011 - 2013³⁴



³³ See TIGTA, Ref. No. 2013-40-129, *Case Processing Delays and Tax Account Errors Increased Hardship for Victims of Identity Theft* (Sept. 26, 2013).

³⁴ The IRS does not track the number of issues in a given identity theft case because, unlike TAS, it treats each module (year/tax/issue) as a different case. Accordingly, we can provide TAS data only. This chart is meant to illustrate that the vast majority of TAS identity theft cases involve multiple issue codes. The increase in the percentage of cases with multiple issue codes from FY 2011 to FY 2013 may be due to better coding by TAS case advocates to record secondary issue codes; it does not necessarily mean that TAS identity theft cases have become more complex in recent years.

The Taxpayer Advocate Service's experience with working identity theft cases demonstrates the soundness of our recommendation that the IRS should assign one employee to work with the victim from the beginning, and oversee the case when it requires coordination among different units. Instead of taking 312 days to work an identity theft case, TAS case advocates resolve them in 87 days.³⁵ And even though identity theft cases are complex (with over 94 percent of our identity theft cases closed in FY 2013 involving more than one issue code), TAS case advocates have achieved a relief rate of 87 percent.³⁶ Furthermore, an overwhelming 94 percent of identity theft victims who came to TAS in FY 2013 have expressed satisfaction with our assistance.³⁷

The IRS also needs to do a better job of tracking identity theft case data. The IRS cannot even provide a reliable figure for the number of identity theft victims it has assisted, partly because the various specialized units use different systems to track cases. Moreover, while some IRS functions track the length of time a case is in their inventory, the IRS still cannot provide an overall cycle time from the taxpayer's perspective. For example, specialized units generally measure cycle time from the date that particular unit received the case; their cycle time measures do not reflect the time elapsed since the taxpayer attempted to file the initial return, or all of the prior interactions the victim may have had with the IRS. In my 2013 Annual Report to Congress, I recommended that the IRS develop a method of tracking cycle time *from the perspective of the victim*.

IV. Affordable Care Act

As part of the Affordable Care Act (ACA), the IRS is implementing complicated health care tax provisions that require new technology and significant rule-making.³⁸ These provisions would present a serious

³⁵ Analysis conducted by TAS Technical Analysis and Guidance of data obtained from TAMIS (Oct. 1, 2013).

³⁶ *Id.*

³⁷ Analysis conducted by TAS Business Assessment of customer satisfaction scores reported for FY 2013 (through June 2013); data obtained from TAMIS (Oct. 1, 2013).

³⁸ See Patient Protection & Affordable Care Act of 2009, Pub. L. No. 111-148, 124 Stat. 119 (Mar. 23, 2010), as amended by the Health Care & Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (Mar. 30, 2010).

administrative challenge to any agency, but for one such as the IRS, with its annual and continuing tax administration duties, the added work is daunting. To date, I believe the IRS has acquitted itself well in meeting its initial responsibilities under the ACA. Specifically, the IRS has done a good job of updating information technology (IT) systems, issuing guidance, and collaborating with other federal agencies. The IRS's actions with regard to ACA implementation demonstrate what the IRS can do when it has sufficient lead time to plan and implement a complex social benefit delivered through the tax system.

While the opening of the Health Insurance Marketplaces³⁹ on October 1, 2013, was riddled with problems, the one aspect that went better than anticipated was the role of the IRS in providing information to the Marketplace on household income and family size. Originally, the IRS agreed that queries from the Marketplace would have an average response time of less than five seconds. However the IRS has been providing an average response time of less than one second.⁴⁰ The IRS is to be commended on its ability to surpass expectations thus far.

In order to ensure that ACA design and implementation treat taxpayers – both individuals and businesses – appropriately and fairly, the Taxpayer Advocate Service has been actively involved with the IRS roll-out of the Affordable Care Act tax provisions. I personally sit on the ACA Executive Steering Committee and have staff throughout TAS on the ACA Joint Implementation Teams to ensure the provisions are implemented in a fair and equitable manner and that taxpayer rights are protected.⁴¹

ACA Taxpayer Service and Training Raise Concerns

The true test for the IRS will be in 2015, when taxpayers begin filing their 2014 tax returns. This will be the first year when individual taxpayers will have to report they have minimal essential health insurance coverage when they file their income tax returns, or that they are exempt from the

³⁹ <https://www.healthcare.gov/marketplace/individual>.

⁴⁰ This is due, in part, to a lower than anticipated volume of inquiries. Data provided verbally at ACA Executive Steering Committee on Nov. 13, 2013.

⁴¹ The Joint Implementation Teams TAS is represented on are: Customer Service Operations, Tax Return Processing, Information Return Receipt and Processing, ACA Notices and Correspondence, Compliance – Individuals, Compliance – Business, and Collection.

responsibility to have the required health insurance coverage. If the taxpayer does not have health insurance coverage and is not exempt, then he or she will need to make an individual shared responsibility payment (ISRP) when filing a return.⁴² Additionally, many taxpayers will have to reconcile the Premium Tax Credit amounts they are currently receiving with the amounts to which they are entitled based on their actual (as opposed to projected) 2014 income.⁴³

While other agencies have telephone or web chat options, the IRS has adopted a web-first strategy that acts more as a “web-only” strategy, limiting taxpayers’ access to in-person assistance with *tax-related* health care questions.⁴⁴ The IRS has specifically advised its assistors “the best service to the customer is to provide the web URLs. This is known as the ‘Web First’ strategy.”⁴⁵ In comparison, Healthcare.gov has telephone assistors trained to answer questions, as well as a live web chat option.⁴⁶

Websites alone may not meet the needs of taxpayers dealing with complicated new provisions for the first time.⁴⁷ Moreover, those who are

⁴² IRC § 5000A. The following individuals in the following categories are exempt from the ISRP: a member of a religious sect that is recognized as conscientiously opposed to accepting insurance benefits; a member of a health care sharing ministry; a person not lawfully present in the U.S.; a person incarcerated for at least one day of the applicable month in a jail, prison, or similar penal institution or correctional facility after the disposition of charges; a person who has income below the tax filing threshold; a person who lacks coverage for fewer than three months; a person who cannot afford coverage where the required contribution exceeds eight percent of household income for 2014; members of federally recognized Indian tribes; or persons who have suffered hardship as certified by an Exchange with respect to the capability to obtain minimum essential coverage (including, among others, patients of the federal Indian Health Service not enrolled in a recognized tribe). See IRC § 5000A(d) and (e).

⁴³ The Premium Tax Credit is a refundable, advanceable tax credit available to help taxpayers with moderate income purchase health insurance through a Marketplace. IRC § 36B.

⁴⁴ See Health Insurance Market Place, *Help-Center*, <https://www.healthcare.gov/help-center/> (last visited Aug. 12, 2013).

⁴⁵ IRS, *Affordable Care Act Web First Strategy: Addressing Health Care Law Inquiries*, http://win.web.irs.gov/field/fadocs/ACA_Web_First_Strat.pdf (last visited Apr. 30, 2013).

⁴⁶ See Health Insurance Market Place, *Help-Center*, <https://www.healthcare.gov/help-center/> (last visited Aug. 12, 2013).

⁴⁷ Existing IRS functions, such as Stakeholder Partnership, Education & Communication (SPEC), Stakeholder Liaison, and Taxpayer Assistance Centers may receive questions and even visits from taxpayers who want to know about the ACA. See SPEC *Outreach*

eligible for the Premium Tax Credit may not have the necessary language or computer literacy skills to obtain information in this way,⁴⁸ and those who lack Internet access still need IRS assistance through other channels. Obtaining health care is an inherently complicated and personal decision that can have a major impact on a taxpayer's life and finances. If the IRS cannot answer tax-related questions, taxpayers may unknowingly make health care choices that carry significant tax implications.

The IRS Is Not Adequately Training Assistors to Respond to Taxpayer Questions on Health Care Issues.

As discussed above, due to resource constraints the IRS already cannot answer millions of telephone calls or respond timely to volumes correspondence from taxpayers.⁴⁹ The new work caused by the ACA will compound this backlog. The IRS estimates it needs almost 2,000 new employees to handle the numerous additional calls and letters that may arrive once applicable provisions take effect.⁵⁰ Absent additional employees dedicated to the ACA, the IRS must ensure that the employees it does have – particularly in taxpayer-facing roles – are properly trained to respond to taxpayer inquiries.

Summary (Filing Season Jan.-Apr. 2013) (containing 3-pg. ACA Overview); IRS Pub. 5093, *Healthcare Law Online Resources* (1 pg. listing a half-dozen URLs for individuals & employers).

⁴⁸ Adults “living in households earning at least \$50,000 per year are more likely to have home broadband than those at lower income levels.” Pew Res. Ctr., *Home Broadband* 2013, available at <http://pewinternet.org/Reports/2013/Broadband.aspx> (last visited Sept. 17, 2013). As of 2011, only “75.6 percent of households reported having a computer,” which means almost a quarter of the nation’s households may be unable to get the information they need from the IRS’s web strategy. U.S. Census Bureau, *Computer and Internet Use in the United States*, P20-569 (May 2013) 1. See also National Taxpayer Advocate 2011 Annual Report to Congress 273, 279 (Introduction to Diversity Issues: *The IRS Should Do More to Accommodate Changing Taxpayer Demographics*) (“low income, less educated, minority, elderly, disabled, or rural populations are less likely than others to use the Internet”).

⁴⁹ See NTA 2013 Annual Report 20 (*Most Serious Problem: IRS Budget Cuts Diminish Taxpayer Service*); National Taxpayer Advocate 2012 Annual Report to Congress 34 (*Most Serious Problem: The IRS Is Significantly Underfunded to Serve Taxpayers and Collect Tax*); IRS Joint Operation Center (JOC) Snapshot Report for fiscal year 2013 (Sept. 30, 2013) and JOC Accounts Management Inventory Reports for fiscal year 2013 (Oct. 6, 2012 – Sept. 28, 2013).

⁵⁰ See IRS FY 2014 Congressional Budget Submission, Table 4.9 at 177.

The IRS has provided some general ACA information to employees but has not yet engaged in substantive training. The IRS says it is developing training for 2014, but TAS has yet to see or review its training plan. In contrast, TAS has been providing training to its employees on the Affordable Care Act since 2010, to give them time to digest and develop a basic understanding of the new provisions. TAS plans to continue this training through 2014, adding more in-depth sessions and specific case studies. It is my understanding that one of the ACA Implementation Teams is reviewing the ACA training TAS offered this year to see if it meets the needs of the ACA overview all IRS employees should receive. I encourage the IRS to use TAS's training and ensure that all IRS employees receive basic training on the new health care provisions.

IRS Outreach Does Not Alert Taxpayers to the Issues Surrounding a Change in Circumstances.

The IRS has made strides in its ACA outreach efforts. It has issued several user-friendly publications for taxpayers regarding the Premium Tax Credit, and we understand it plans similar publications for the employer provisions and Individual Shared Responsibility Payment.⁵¹ Additionally, the IRS has made efforts to improve the ACA pages on IRS.gov, including by posting new pages on the Premium Tax Credit and the ISRP⁵² as well as updated Q&As and legal guidance.⁵³ The IRS also plans to create a page on the 5000A Individual Shared Responsibility Payment. TAS will continue to work with the IRS on its outreach efforts.

However, we remain concerned that the IRS is not being proactive and educating taxpayers as early as possible on a critical issue: the importance of updating their information throughout the year with the

⁵¹ Thus far, the IRS has issued several electronic publications, including Pub. 5093, *Health Care Law Online Resources* (July 2013), Pub. 5120, *Facts About the Premium Tax Credit* (flyer) (Sept. 2013), and Pub. 5121, *Facts About the Premium Tax Credit* (brochure) (Dec. 2013). We understand that Spanish versions of the publications are in progress.

⁵² The ACA homepage is located at <http://www.irs.gov/aca>. The Premium Tax Credit page is located at <http://www.irs.gov/uac/The-Premium-Tax-Credit>. The ISRP page is located at <http://www.irs.gov/uac/Individual-Shared-Responsibility-Provision>.

⁵³ <http://www.irs.gov/uac/Newsroom/Affordable-Care-Act-Tax-Provisions-Questions-and-Answers>.

Exchange if they are receiving a credit.⁵⁴ To avoid receiving an excess credit, taxpayers must update their information with the marketplace if their incomes or other relevant circumstances change.⁵⁵ This is also important for taxpayers who may be eligible for a larger credit due to a reduction in pay or an increase in family size (such as having or adopting a child). Educating taxpayers early and repeatedly about this requirement will help prevent them from owing money to the IRS (or reducing their refunds) or receiving an additional credit amount at the end of the year that they could have received earlier.

Healthcare.gov now has a “Report Life Change” button that allows individuals to modify their health insurance plans (once they are enrolled) if they have experienced a change such as family size, moving, etc.⁵⁶ Assuming this option will also allow for a recalculation of the Premium Tax

⁵⁴ To apply for a premium assistance credit, an individual goes to an Exchange, which will attempt to verify household income with the IRS. In general, applicable taxpayers seeking health insurance and a premium tax credit through an Exchange will supply names, Social Security numbers, and income data for themselves and their dependents to the Exchange. See ACA § 1411(b), 124 Stat. 119, 224 (2010). The Exchange can verify data with HHS, which has authority under the ACA to obtain IRS data, and then disclose any inconsistency to the Exchange. See IRC § 6103(l)(21). If IRS information is inaccurate or outdated, the individual may need to present updated documentation or other evidence to HHS to establish eligibility for a premium tax credit. If a taxpayer's household status at year's end is other than anticipated – due either to a change in income or family size – the premium tax credit may be more or less than the amount advanced. Consequently, the IRS may recover the excess as a tax (above a threshold for low income taxpayers), or owe the taxpayer a refund. Section “36B(f)(2)(B) places a graduated set of caps on the additional tax liability for taxpayers with household income under 400 percent of the F[ederal] P[overty] Level]. The repayment limitation amounts range from \$600 to \$2,500 (one-half that amount for single taxpayers) depending on FPL, and are adjusted to reflect changes in the cost of living beginning in 2015.” 76 Fed. Reg. 50931, 50933-934 (Aug. 17, 2011).

⁵⁵ Income may change after submission of an application, which reflects the amount on the last tax return, *i.e.*, the one filed in the current year relating to the year that just ended. Thus, a couple of years' worth of life changes may transpire by the time of reconciliation between the advance and ultimate credit amounts. By the same token, certain changed circumstances, such as the birth of a child or a reduction in pay, may increase the credit.

⁵⁶ Amy Goldstein, *Administration will allow people to switch health-care plan to a limited degree*, Washington Post (Feb. 7, 2014) available at http://www.washingtonpost.com/national/health-science/administration-will-allow-people-to-switch-obamacare-plans-to-a-limited-degree/2014/02/07/56c8bfd2-9015-11e3-b227-12a45d109e03_story.html (last visited Feb. 18, 2014).

Credit based on these changes, the IRS can easily tie its messages about changing circumstances into this new option.

TAS worked with the IRS to prominently place language in the 2013 Form 1040, *U.S. Individual Income Tax Return*, instructions to alert taxpayers to the importance of updating their information with the marketplaces. However, the IRS still needs to be more proactive. While almost 80 percent of individual returns are refund returns and thus may offset some or all of the reconciliation amount, the IRS should be doing all it can to ensure that as few taxpayers as possible have excessive advanced premium tax credit payments and instead receive the correct amount throughout the year.⁵⁷ In addition to preventing taxpayers from owing money, this approach will reduce future costs to the IRS for collection activities.⁵⁸

I have additional concerns that other taxpayers will have their returns delayed because they claim a larger Premium Tax Credit than what they received during the year due to a change in circumstances. If the IRS flags these returns as potentially fraudulent, it may hold up legitimate refunds. TAS has seen these issues previously, especially when large dollar amounts are at stake.⁵⁹

⁵⁷ IRS Compliance Data Warehouse, Individual Returns Transaction File Tax Year 2012 (Feb. 2014).

⁵⁸ TAS looks forward to working with the IRS Office of Research, Analysis and Statistics (RAS) to try to identify the areas and populations of taxpayers most likely to have experienced a change in circumstances. This information can be used by the IRS's SPEC organization, TAS Local Taxpayer Advocates (LTAs), Low Income Taxpayer Clinics (LITCs), and other stakeholders to conduct outreach to these specific populations.

⁵⁹ National Taxpayer Advocate 2012 Annual Report to Congress 111-133 (Most Serious Problem: *The IRS's Compliance Strategy for the Expanded Adoption Credit Has Significantly and Unnecessarily Harmed Vulnerable Taxpayers, Has Increased Costs for the IRS, and Does Not Bode Well for Future Credit Administration*); National Taxpayer Advocate Fiscal Year 2012 Objectives Report to Congress 28-32; National Taxpayer Advocate 2011 Annual Report to Congress 687-689 (Case Advocacy: *Policymakers Can Learn from the Implementation of the FTHBC*); National Taxpayer Advocate Fiscal Year 2011 Objectives Report to Congress 3, 37-43; National Taxpayer Advocate 2010 Annual Report to Congress 15 (Most Serious Problem: *The IRS Mission Statement Does Not Reflect the Agency's Increasing Responsibilities for Administering Social Benefits Programs*) (Case Advocacy: *TAS Assists the IRS with the Administration of the First-Time Homebuyer Credit*); National Taxpayer Advocate 2009 Annual Report to Congress 506-509; *Hearing on Complexity and the Tax Gap: Making Tax Compliance Easier and Collecting What's Due*, Hearing Before the S. Comm. on Finance, 112th Cong. (statement of Nina E. Olson, National Taxpayer Advocate) (June 28, 2011); *Filing*

While there will always be persons trying to game the tax system, I believe the risk of fraud with respect to the PTC is much less than with many other refundable credits. With respect to the Advanced Premium Tax Credit, the credit will be paid to established insurance companies when a policy is actually in place. When a taxpayer claims the PTC on his or her income tax return, it is a *reimbursement* of amounts already paid; the taxpayer will have to provide proof of a qualified health insurance plan, which the IRS will be able to verify through third-party information reporting. This design minimizes the opportunities for fraud.

TAS is in the final stages of developing an estimator for the Premium Tax Credit that will help taxpayers and practitioners understand how changes in circumstances will impact their credit amounts. TAS hopes to have this tool online and available to the public in the next few months. We have had success with a similar estimator for the Small Business Health Care Tax Credit (SBHCTC), which we launched on the TAS Tax Toolkit in November 2012.⁶⁰ The homepage for the estimator received 5,000 page views for October 2013 and over 13,000 page views for October – December 2013.⁶¹

IRS ACA Audit and Collection Activity May Unduly Burden Low Income Taxpayers.

My concerns about the IRS's implementation of the Affordable Care Act (ACA) are similar to concerns I have raised on numerous occasions about the IRS's handling of identity theft claims. Just as the IRS does not resolve identity theft cases through a single point of contact and thereby forces taxpayers to negotiate a maze of various IRS functions to unwind the harm caused by the identity theft, the IRS may not resolve, during

Season Update: Current IRS Issues: Hearing Before the S. Comm. on Finance, 111th Cong. (2010) (statement of Nina E. Olson, National Taxpayer Advocate) (Apr. 15, 2010); The National Taxpayer Advocate's 2009 Report on the Most Serious Problems Encountered by Taxpayers: Hearing Before the Subcomm. on Oversight of the H. Comm. on Ways and Means, 111th Cong. (2010) (statement of Nina E. Olson, National Taxpayer Advocate) (Mar. 16, 2010).

⁶⁰ <http://www.taxpayeradvocate.irs.gov/Businesses/Small-Business-Health-Care-Tax-Credit-Estimator> (last visited Feb. 19, 2014). According to Weber Shandwick, which tracks statistics for the estimator, the SBHCTC estimator has received over 23,500 page views since its launch in 2012.

⁶¹ Taxpayer Advocate Service, FY 2014 1st Quarter Business Performance Review.

routine audits, issues related to the ACA. This case segmentation may prolong the length of time taxpayers must wait to fully and finally resolve their tax liabilities for a given year and burden them with additional IRS contacts. These inefficiencies, some of which appear to be attributable to programming conditions, may disproportionately affect low income taxpayers.⁶²

For example, the IRS may audit the return of a taxpayer claiming the Earned Income Tax Credit (EITC).⁶³ The taxpayer may have also claimed the Premium Tax Credit.⁶⁴ If the IRS determines the taxpayer's income exceeded the allowable threshold for claiming EITC, the taxpayer may also not be eligible for the PTC. However, under current programming conditions, the IRS would not be able to resolve both issues in the course of the audit because it plans to assess liability under the ACA using different software than it uses to process returns. Return-processing software would not recognize and manage tax liabilities arising under the ACA.⁶⁵ Consequently, the IRS would "conclude" the audit and assess additional tax because of disallowed EITC only to contact the taxpayer months later and assess additional tax due to disallowed PTC.

⁶² Programming deficiencies are evident in other, related areas of IRS operations. See letter from Sen. Grassley to Comm'r Koskinen (Apr. 21, 2014) *available at* <http://www.grassley.senate.gov/issues/upload/Grassley-to-IRS-Return-Review-Program-4-21-14.pdf>, noting that the IRS is not implementing the needed Return Review Program, a fraud detection system especially critical as the refundable Premium Tax Credit becomes available, due to budgetary constraints.

⁶³ Taxpayers who claim the Earned Income Tax Credit are more likely to be audited than taxpayers in the general population. EITC audits have historically comprised about a third of all individual taxpayer audits. See National Taxpayer Advocate 2012 Annual Report to Congress vol. 2, *Study of Tax Court Cases In Which the IRS Conceded the Taxpayer was Entitled to Earned Income Tax Credit (EITC)*.

⁶⁴ In general, a taxpayer may be eligible for the PTC if the taxpayer's household income for the taxable year is at least 100 percent but not more than 400 percent of the federal poverty level for the taxpayer's family size. IRC § 36B(c)(1). The 2014 federal poverty level for a four-person household is \$23,850. See Federal Poverty Guidelines, *available at* <http://aspe.hhs.gov/POVERTY/14poverty.cfm>. 400 percent of \$23,850 is \$95,400. For 2014, joint filers with two qualifying children must have adjusted gross income of less than \$49,186 in order to qualify for EITC. *Preview of 2014 EITC Income Limits, Maximum Credit Amounts and Tax Law Updates*, *available at* <http://www.irs.gov/Individuals/Preview-of-2012-EITC-Income-Limits,-Maximum-Credit--Amounts-and-Tax-Law-Updates>.

⁶⁵ The traditional software used by IRS Exam to conduct audits, Report Generating Software, cannot accommodate the need to assess these tax liabilities resulting from the same audit record.

Conversely, if a taxpayer inflated his or her income in order to receive a larger EITC refund and the IRS later adjusts the taxpayer's income downward and reduces the claimed EITC amount, the taxpayer might be entitled to additional PTC because of the decreased income. As a result of the audit, the IRS would assess additional tax due to disallowed EITC, but the taxpayer's final liability, determined months later after the PTC issue is addressed, may be lower. The taxpayer might receive demands for payment related to the disallowed EITC in the meantime.

Similar issues arise with respect to the ISRP. A taxpayer may claim EITC and also report liability for ISRP with respect to the same child.⁶⁶ If the IRS determines the child was not a qualifying child, it would disallow the claimed EITC and assess additional tax. If the child was also not the taxpayer's dependent, the taxpayer would not be liable for ISRP with respect to that child, but only later would the IRS contact the taxpayer with respect to the assessed ISRP and ultimately reduce the liability. In the meantime, the taxpayer might be burdened with demands for payment and enforced collection action with respect to the disallowed EITC at a time when the true amount of the taxpayer's liability had not yet been established.

The ACA prohibits the IRS from collecting ISRP liabilities through enforced collection action.⁶⁷ However, when the IRS takes enforced collection action, such as a levy, to collect non-ISRP liabilities, it may collect more than the taxpayer actually owes.⁶⁸ Once the non-ISRP liabilities have been satisfied, the IRS should refund the overpayment to the taxpayer.⁶⁹

⁶⁶ Under section 5000A(b)(3) of the ACA, the adult or married couple who can claim a child or another individual as a dependent for federal income tax purposes is responsible for making the payment if the dependent does not have coverage or an exemption.

⁶⁷ IRC § 5000A (g)(2)(B).

⁶⁸ This may occur, for example, when the IRS imposes a continuous levy on the taxpayer's wages or levies on Social Security benefits and either inadvertently does not release the levy when the tax liability has been satisfied, or releases the levy, but not before the employer or the Social Security Administration has already remitted the payment to the IRS. See IRM 5.11.2.6 (Apr. 15, 2014), noting that "Every reasonable effort will be made to release a notice of levy timely. However, sometimes surplus levy proceeds are received. Surplus proceeds are payments greater than the amount still owed for the liabilities listed on the notice of levy. Example: A refund posts after the levy source has already sent payment for the levy."

⁶⁹ See IRC § 6342(b).

However, IRS programming conditions may cause the IRS to automatically apply excess levy proceeds to ISRP liabilities. The IRS tested programming intended to prevent this refund offset, but the proposed solution was successful only if the refund offset occurred in the same cycle the levy payment was received, which occurred only 18 percent of the time.⁷⁰ Ensuring that levy proceeds are not applied to ISRP liabilities would require manual processing of these accounts.

Delays in Information Matching Show Need for Real-Time Tax System

Last year, the Treasury Department delayed the requirement for certain employers with 100 or more employees to provide coverage to their employees.⁷¹ Due to the delay in implementation, employers will not have to provide information reporting to the IRS regarding the employees they cover.⁷² This information reporting will help identify which taxpayers have coverage and which do not (and therefore have to pay a penalty). We do not yet know how the IRS plans to address this lack of information during the 2015 filing season. TAS members on the relevant Joint Implementation Team have been told it will be discussed later.

Without this information, the IRS's job is increasingly difficult. This concern underscores the need for the IRS to develop an accelerated document-matching program, as discussed immediately below.

⁷⁰ Wage and Investment Research & Analysis (WIRA) Group 2, Project #2-14-09-A-206 *Refund Offset Adjustment Due to Lien/L levy Overpayment* (April 2014) and attached spreadsheet, showing that out of 11,064 transactions in tax year 2012 in which a levy resulted in an overpayment, in only 2,039 transactions was the overpayment offset to another module in the same cycle and was therefore preventable. 2,039 out of 11,064 is 18 percent. TAS Research has not yet verified the accuracy of these findings.

⁷¹ Treasury Department Fact Sheet, *Final Regulations Implementing Employer Shared Responsibility Under the Affordable Care Act (ACA) for 2015*, available at <http://www.treasury.gov/press-center/press-releases/Documents/Fact%20Sheet%202014.pdf> (last visited April 28, 2014). The requirement was further delayed until 2016 for employers with 50 to 99 employees. Shared Responsibility for Employers Regarding Health Coverage, 79 Fed. Reg. 8544 (Feb. 12, 2014).

⁷² Transition Relief for 2014 Under §§ 6055 (§ 6055 Information Reporting), 6056 (§ 6056 Information Reporting) and 4980H (Employer Shared Responsibility Provisions), Notice 2013-45, 2013-31 I.R.B. 116.

V. Accelerated Receipt and Use of Third-Party Information Reports

Accelerated third-party information report processing and upfront document matching would protect revenue, reduce fraud, and improve taxpayer service.

Whether in the context of Premium Tax Credit reconciliation, eligibility for the Earned Income Tax Credit, or returns filed by identity thieves, the IRS faces pressure to satisfy two competing demands: protect the public fisc from erroneous refund claims and meet taxpayer expectations by issuing refunds quickly. Although the IRS has instituted many business rules and filters to identify questionable refunds, it generally matches third-party information reports with tax return data long after it has released any associated income tax refunds.⁷³

In 2009, I recommended that Congress establish a timeframe for the IRS to develop a strategy and timeline for accelerating third-party information report processing and providing taxpayers with electronic access to such data.⁷⁴ Most recently, a study in my 2013 Annual Report proposed a strategic framework and preliminary recommendations to better structure the filing season to reduce fraud and protect the interests of both the government and taxpayers.⁷⁵ This is a key component of 21st century tax administration.

The government benefits from the revenue protection aspect of accelerated third-party information report processing and upfront document matching. Third-party information reporting is a crucial element in maximizing tax compliance.⁷⁶ By enabling the IRS to match third-party

⁷³ For a more detailed discussion of the IRS's processes to review refund returns, see Nina E. Olson, *More Than a 'Mere' Preparer: Loving and Return Preparation*, 2013 TNT 92-131, Tax Notes Tax Analysts Tax Notes Today (May 13, 2013).

⁷⁴ National Taxpayer Advocate 2009 Annual Report to Congress 338-345; National Taxpayer Advocate 2011 Annual Report to Congress 284-295; National Taxpayer Advocate 2012 Annual Report to Congress 180-191.

⁷⁵ NTA 2013 Annual Report vol. 2, 67-96.

⁷⁶ Tax gap data show the importance of information reporting compliance, and how third-party reporting is essential to encourage voluntary compliance; specifically, when taxpayers have a choice about reporting their income, tax compliance rates are remarkably low. For example, workers who are classified as employees have little opportunity to underreport their earned income because it is subject to both information

data to tax return information before issuing refunds, the IRS could identify and resolve inaccurate income tax reporting soon after the return is filed and prevent the release of erroneous refunds. This system would deter tax fraud and identity theft by stopping the refund associated with a mismatch.

In addition, accelerated information report processing and upfront matching would substantially improve taxpayer service and reduce taxpayer burden by:

- Providing taxpayers with direct electronic access to the third-party information report data to assist in tax preparation and reduce inadvertent errors;⁷⁷
- Improving taxpayers' ability to answer questions about an underlying economic transaction if the IRS identifies the mismatch within months rather than a year or more after the fact;
- Avoiding IRS collection actions long after taxpayers have spent the refunds;
- Avoiding the long-term accrual of penalties and interest on unintentionally omitted or under-reported items; and

reporting on Forms W-2 and tax withholding. In fact, IRS data show that taxpayers report about 99 percent of their wages and salaries. IRS, *Tax Gap for Tax Year 2006 Overview*, Chart 1 (Jan. 6, 2012).

⁷⁷ Taxpayers will not realize the full benefits of accelerated third-party information reporting unless the IRS provides taxpayers and their preparers with the ability to access and download their third party data from an online account. To address inadvertent omissions, the IRS should provide access to real-time transcripts of third-party data to aid in return preparation. Taxpayers and preparers could refer to the transcripts to ensure they do not accidentally omit income. One step above the transcript would be to provide a platform from which taxpayers and preparers could download third-party data submitted to the IRS or the Social Security Administration directly into a commercial tax software package or even an improved version of the IRS's Free File Fillable Forms (FFFF). This second option would eliminate transcription errors and provide a one-stop-service to taxpayers who would not need to download the data separately from each third party. In addition, the government would enjoy the benefits experienced by other tax administrations through pre-filled returns, but would still encourage competition in the tax software industry. For more information on the benefits of electronic access to third-party data and the experience of international tax administrations, see National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, 67-96.

- Reducing vulnerability to identity-theft related refund fraud.⁷⁸

While the IRS has acknowledged the benefits of accelerated third-party information report processing and upfront matching, it has not made any recent progress in developing a long-term plan for such a system.⁷⁹ The IRS's lack of progress only delays the significant benefits we outlined throughout the study. Thus, we reiterated our 2009 Legislative Recommendation that Congress require the IRS and Treasury, in consultation with the Taxpayer Advocate Service, to prepare a plan and timeline to achieve an accelerated third-party report processing system. In addition, to stimulate serious consideration and discussion of the issue, we offered the following administrative and legislative recommendations to achieve a system that allows the IRS to perform upfront matching to protect government revenue and improve taxpayer service:

- Provide taxpayers with electronic access to real-time transcripts of third-party information reporting data to aid in return preparation.
- Provide a platform from which taxpayers and preparers could download third-party data directly into commercial tax return preparation software.
- To accelerate the processing of Form W-2 data, develop and implement a one-year pilot to determine whether the IRS can screen Form W-2 data as effectively as the Social Security Administration.

⁷⁸ William Hoffman, *IRS Oversight Board Brainstorms Real-Time Tax System, ID Theft Initiatives*, Tax Notes Today (May 2, 2013); IRS, PowerPoint, *Real Time Tax System Initiative, Public Meeting 1* (Dec. 8, 2011), available at http://www.irs.gov/file_source/pub/irs-utl/rtts_deck.pdf. For more information on identity-theft refund fraud, see National Taxpayer Advocate 2013 Annual Report to Congress 75-83 (Most Serious Problem: *The IRS Should Adopt a New Approach to Identity Theft Victim Assistance that Minimizes Burden to Such Taxpayers*); National Taxpayer Advocate 2012 Annual Report to Congress 42-67 (Most Serious Problem: *The IRS Has Failed to Provide Effective and Timely Assistance to Victims of Identity Theft*).

⁷⁹ For written and oral statements of panelists at the two IRS Real Time Tax System Initiative public meetings, see <http://www.irs.gov/Tax-Professionals/Real-Time-Tax-Initiative> (last visited Feb. 13, 2013).

- Because almost 98 percent of information reports are already e-filed, eliminate the March 31 deadline for e-filed information reports.⁸⁰ Thus, all information reports, whether e-filed or filed on paper, would be due at the end of February.
- Create a \$50 *de minimis* threshold for corrections, which would eliminate the need to file an amended or corrected third-party information report for any adjustments to income below \$50.
- Further increase electronic filing by reducing the 250 report threshold in IRC § 6011(e) to 50 reports and offer 2D bar code technology for those who cannot e-file.
- Issue direct deposit and other electronic refunds by April 30 and paper checks by May 31 for taxpayers who file their returns by April 15.

The proposals included in the 2013 study are meant to serve as a “conversation starter” and are based on research conducted by the Taxpayer Advocate Service, including discussions with impacted stakeholder groups and a review of international tax systems. We attempted to address all identified concerns and risks, but we acknowledge that there will be unexpected challenges and risks before a proposal along these lines is implemented. We recognize that the changes necessary to accomplish an accelerated third-party reporting system require a great deal of forethought, analysis, and stakeholder engagement.

VI. IRS Information Technology Challenges

An adequately funded, staffed, and skilled IRS Information Technology (IT) function underpins all of the activities described above. IT resources are the common denominator for performing core IRS functions, including taxpayer service, prompt issuance of refunds, selection and assignment of compliance work, and protecting taxpayers and the public from refund

⁸⁰ IRS Pub. 6961, *2013 Update: Calendar Year Projections of Information and Withholding Documents for the United States and Campuses*, Tables 2-4 (Of the 2,288,516,144 information reports received in calendar year 2012, 2,240,335,726 were received electronically).

fraud and identity theft. If the IT workforce is not appropriately skilled and staffed, the IRS will not be able to bring itself into the 21st century, much less meet its everyday work demands. Cost overruns will occur if the IRS does not have the skilled staff to undertake the necessary strategic planning or provide adequate project and contract oversight.

For FY 2014 and FY 2015, the IRS is focusing its IT resources on three main areas: implementation of the ACA; implementation of FATCA; and implementation of the 2015 filing season, including delivery of various legislative provisions and extenders. All other requests for IT resources are subordinate to these three “heavy lifts.” While I understand the importance of each of these areas to tax administration, at current funding and staffing levels the IRS will not be able to deliver on these programs and also improve or correct core processes and systems. The negative impact to taxpayers of not funding everyday improvements to IRS taxpayer service, revenue protection, and compliance activities is significant.

Moreover, because the IT workforce is stretched so thin, the already glacial pace of the IRS’s move into a 21st century technology environment is being slowed further. The IRS’s inability to digitally communicate with taxpayers places the IRS far behind other international tax administrations and the financial services sector. The slowdown or shutdown of IT support also compounds the impact of taxpayer service funding reductions by driving taxpayers to make numerous telephonic or correspondence contacts with the IRS just to get information about their accounts. It also forces the IRS to continue using archaic compliance methods like correspondence examinations, when a “virtual” face-to-face audit would bring about better and more accurate results in terms of taxpayer response, issue resolution, and taxpayer education.

The Taxpayer Advocate Service has keenly felt the impact of this IT shortfall, when work on a once-in-a generation revision of its case management system (called TASIS) stopped short on March 31, 2014, due to lack of available funds. The work stoppage was based on the IRS’s need to prioritize its IT projects and direct all available resources to the three key priorities – ACA, FATCA, and the 2015 filing season. While work will resume on this system shortly because TAS itself has transferred \$1.8 million of its operating budget to cover the shortfall, this stop-and-start approach undermines not only TAS’s ability to deliver quality service

to taxpayers experiencing significant hardship, but also the IRS's efforts in developing an enterprise case management system.

The IRS currently has about 167 case management systems used by different units. This diversity of systems is one reason it is so difficult for IRS employees and taxpayers to find out precisely what the IRS is doing when an issue crosses different IRS functional units. There is no IRS "integrated" or "enterprise-wide" case management system.

The Taxpayer Advocate Service Information System, or TASIS, was designed with this problem in mind. Over a decade ago, TAS began a major redesign effort of its case management and case assignment system, which soon expanded to include all of its activities, including systemic advocacy and research. The result is TASIS -- an integrated case, project, and work assignment system that allows for seamless movement and access to cases, projects, research, and archives. TASIS will have the following capabilities:

- TAS Intake Advocates will be able to conduct a real-time initial interview and perform related case-building, including automatically retrieving relevant information from other IRS systems.⁸¹
- TAS Case Advocates will have the ability to communicate digitally with taxpayers – both receiving and sending information and documents, and sending automated reminders to taxpayers or IRS employees as needed to keep cases on track toward resolution.
- Taxpayers will be able to submit electronic requests for TAS assistance – whether for help with an individual problem or with solving a systemic problem – and they will be able to check on the status of their cases or systemic issue online without having to call a TAS employee for an update.
- All significant materials – case files, projects, research studies, communications – will be converted to digital files, promoting ease

⁸¹ As part of our business process review, TAS created an Intake Advocate position to ensure that TAS cases would be as fully developed as possible at the first contact with the taxpayer for assignment to the appropriate case advocate and to eliminate the delays associated with reassigning cases. TAS has also developed procedures for identifying instances where, with a little guidance from the Intake Advocate, the taxpayer could actually resolve the problem him or herself.

of access and sharing, and eliminating costs of document storage, shipping, archiving, and retrieval.⁸²

- Case Advocacy employees will have an easy-to-use method to identify and elevate systemic issues they encounter in the cases;
- TAS will have a sophisticated ability to search our rich repository of information so that projects and data can be easily identified and retrieved via a library of key terms (metadata) that are applied to both cases and projects.

All of these features were designed to minimize the time spent on duplicative keystrokes and data entry, and manual retrieval or requests for information from other functions, so that TAS employees' limited time can be spent on direct communication with and advocating for taxpayers rather than on mere clerical tasks.

In summary, TISIS is a sophisticated case, project, and work assignment management system that has already been identified by the IRS's Chief Technology Officer as a potential foundation for an IRS Enterprise Case Management System, and it is of sufficient significance that the Senate Appropriations Committee has included it on its list of "major information technology project activities" about which the IRS must report quarterly to the Senate and House Appropriations Committees and the Government Accountability Office.⁸³

I write about TISIS in detail partly because of its independent significance but also to illustrate the impact of the funding shortfalls in IT more generally. Although TAS is just one small unit within the IRS, it assists taxpayers who are experiencing significant hardship as a result of IRS actions or inaction.⁸⁴ The later deployment of TISIS because of the work

⁸² Reliance on paper files and documents requires storage and handling of 50 to 60 pages for each TAS case, or approximately 12.5 million pages each year. This includes hard copies as well as records kept on employees' local hard drives. TAS incurs repeated copying and shipping costs for transfers, work reviews, and collaboration. The use of virtual documents will almost eliminate costs associated with paper document-handling and storage, allow immediate access for collaboration, and improve TAS's ability to reference the products or conduct research.

⁸³ S. Rep. No. 113-80, at 34 (2013).

⁸⁴ See IRC § 7811.

stoppage will harm those taxpayers, impeding my employees' ability to effectively communicate and advocate on their behalf. The work stoppage also will cost the IRS more in terms of shoring up an obsolete system, unproductive use of employees' direct time, and higher costs once the program is started up again. This pattern is being reproduced several times over in every business unit of the IRS.

As the National Taxpayer Advocate, I believe it is a key taxpayer need that the IRS's IT function be adequately funded, not only to deliver on major initiatives like ACA and FATCA, but also to deliver on the many small but important improvements and projects that will make a positive difference for taxpayers, employees, and the public fisc. Furthermore, the IRS needs dedicated funding to develop projects that bring us into the 21st century and the digital age. The IRS should be in the vanguard of technology, not bringing up the rear.

VII. Conclusion

In my 2013 Annual Report, I stated that the short-term crises of the past year masked the major problem facing the IRS today – unstable and chronic underfunding that puts at risk the IRS's ability to meet its current responsibilities, much less articulate and achieve the necessary transformation to an effective, modern tax agency. The issues I have discussed today clearly illustrate this situation. In this and every filing season, the IRS must carry out its core mission of collecting revenue and helping taxpayers comply with their obligations. At the same time, it must deal with threats such as identity theft, prepare for the new challenges presented by the ACA, and bring its technology into the 21st century.

I am hopeful that the new leadership of the IRS, with continued oversight and support from Congress and the involvement of the Office of the Taxpayer Advocate, can meet these goals. In particular, I believe that the IRS can improve tax administration and the fundamental fairness of the system by embracing the Taxpayer Bill of Rights I have outlined here today and using those principles to help guide the establishment of agency goals and policies. Thank you for the opportunity to submit this testimony.