

STATEMENT OF

NINA E. OLSON

NATIONAL TAXPAYER ADVOCATE

HEARING ON

IRS OVERSIGHT

BEFORE THE

SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT

COMMITTEE ON APPROPRIATIONS

U.S. HOUSE OF REPRESENTATIVES

MAY 23, 2017

TABLE OF CONTENTS

I.	Simplify the Internal Revenue Code	6
II.	The Filing Season Ran Relatively Smoothly, But Taxpayer Service Remains Below Par	7
	“Customer Callback” Technology	10
III.	The IRS's Trend Toward Heavy Reliance on Delivering Services Through Online Accounts and Away from Personal Interaction Does Not Adequately Take into Account the Widely Divergent Needs and Preferences of the U.S. Taxpayer Population	11
IV.	The IRS's Implementation of the Requirement to Hold Refunds on Returns Claiming the Earned Income Tax Credit and the Refundable Portion of the Child Tax Credit Appears to Have Gone Smoothly.....	14
V.	Tax-Related Identity Theft Appears to Be on the Decline, But Challenges Remain as the IRS Combats Refund Fraud and Large-Scale Data Breaches.....	16
VI.	The Private Debt Collection Program Threatens Taxpayer Rights	19
VII.	Charging User Fees for Services that Help Taxpayers Comply Could Be Very Costly to Taxpayers and Reduce Revenue Collection.....	22
VIII.	The IRS Requires 21st Century Information Technology (IT) Systems to Carry Out 21st Century Tax Administration.....	24
IX.	Conclusion.....	27

Chairman Graves, Ranking Member Quigley, and Members of the Subcommittee:

Thank you for inviting me to testify at your hearing today on IRS oversight.¹

As you know, I lead the Taxpayer Advocate Service (TAS), an independent organization within the IRS that advocates for taxpayers. TAS has two main functions – “case advocacy” and “systemic advocacy.” Our case advocacy operations assist more than 200,000 taxpayers each year in resolving account problems with the IRS. By law, TAS is required to have at least one Local Taxpayer Advocate available in every state, and we currently have 76 offices overall. TAS serves as a *de facto* “safety net” to help taxpayers who are experiencing financial hardships as a result of the way the IRS is administering the tax laws and to help all taxpayers whose cases are falling through the cracks of the bureaucracy. About 85 percent of TAS’s budget and personnel are dedicated to case advocacy. TAS handles congressionally referred cases, so the caseworkers in your district offices generally know our case advocates well.

On the systemic side, TAS identifies problems that are harming groups of taxpayers, and we make administrative and legislative recommendations to mitigate those problems. Any person – from inside the IRS or outside – may identify systemic problems and recommendations for us to address by submitting them online through the Systemic Advocacy Management System (SAMS).² We work many projects within the IRS, and I am required by law to submit two annual reports to Congress in which I call attention to significant taxpayer problems that we have been unable to resolve internally. It is with respect to our systemic advocacy role that I appear today.

From fiscal year (FY) 2010 through FY 2016, we estimate the IRS’s budget has been reduced by nearly 20 percent on an inflation-adjusted basis.³ That is a huge reduction for any organization, particularly a large agency that is labor-intensive like the IRS. At the same time, the IRS has been given significant new responsibilities, including implementation of the Foreign Account Tax Compliance Act (FATCA) and large portions of the Patient Protection and Affordable Care Act (ACA), which require significant resources. It has also had to confront a rising tide of stolen identity refund fraud.

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 are providing courtesy copies of this statement to both the IRS and the Treasury Department.

² Taxpayers and other stakeholders can submit issues at irs.gov/sams.

³ IRS funding is down in dollar terms by 7.5 percent since FY 2010. In FY 2010, the agency’s appropriated budget stood at \$12.1 billion. For FY 2016, its budget was \$11.2 billion. Based on the Consumer Price Index measure of inflation, costs have risen by 12 percent over the same period. Bureau of Labor Statistics, Consumer Price Index – Urban (CPI-U) (reflecting inflation from March 2010 through March 2017). Thus, the inflation-adjusted reduction is nearly 20 percent. There are multiple measures of inflation, so the use of a different measure may produce slightly different results.

The combination of reduced resources and increased work has eroded the IRS's ability to serve taxpayers and promote voluntary compliance. The additional \$290 million in funding that Congress provided in FY 2016 and that has carried over into the Continuing Resolution for this year has been very helpful, and because of it, the IRS has performed much better at answering taxpayer telephone calls than in FY 2015.

However, the IRS remains significantly resource-constrained, and there are limits to how much its performance can improve unless and until it receives additional resources. More specifically, as discussed below, the IRS deserves credit for running the best filing season in several years. But compared with historical performance, the IRS is failing to meet taxpayers' needs.

The demand for taxpayer service is enormous. Each year, the IRS receives more than 100 million telephone calls on its toll-free lines, roughly five million taxpayer visits in its Taxpayer Assistance Centers (TACs), and some ten million pieces of correspondence from taxpayers responding to proposed adjustment notices.⁴ Because taxpayers are required to file accurate and timely tax returns and face sometimes significant consequences for failing to do so, it is imperative that the IRS provide accurate and timely responses to taxpayer requests for help.

Some historical context: In FY 2004 – a high-water mark for taxpayer service – the IRS answered 87 percent of its calls, and callers waited an average of about 2.5 minutes on hold.⁵ In FY 2015 – the low-water mark for taxpayer service – the IRS answered only 38 percent of its calls, and callers waited an average of more than 30 minutes on hold.⁶ This fiscal year, the IRS projects it will answer about 64 percent of its calls and hold times will average about 15 minutes.⁷ That would represent a significant improvement as compared with FY 2015. Yet by historical standards and by any objective measure, failing to answer more than one-third of taxpayer telephone calls and requiring those who get through to wait 15 minutes on hold is poor customer service.

The combination of more work and less funding has produced substantial declines in performance in other areas well. The IRS has substantially stopped answering taxpayers' tax-law questions, victims of stolen refund identity theft continue to experience frustrating interactions with the agency and substantial delays in receiving

⁴ IRS, Joint Operations Center (JOC), *Snapshot Reports: Enterprise Snapshot, IRS Enterprise Total* (final week of each fiscal year for FY 2008 through FY 2016) (showing telephone call volumes exceeding 100 million in every year); IRS Wage & Investment Division, *Business Performance Review 7* (1st Quarter – FY 2017, Feb. 9, 2017) (showing 5.6 million visits in FY 2015 and 4.5 million visits in FY 2016); IRS, JOC, *Adjustments Inventory Reports: July-September Fiscal Year Comparison* (FY 2007 through FY 2016) (showing annual taxpayer correspondence volumes regarding potential adjustments has ranged from a low of 7.3 million letters to a high of 11.8 million letters and has averaged around ten million per year).

⁵ IRS, JOC, *Snapshot Reports: Enterprise Snapshot* (week ending Sept. 30, 2004).

⁶ IRS, JOC, *Snapshot Reports: Enterprise Snapshot* (week ending Sept. 30, 2015).

⁷ IRS Wage & Investment Division, *Business Performance Review 4*, 16 (Feb. 9, 2017).

their refunds (although the IRS has made improvements in this area), and the IRS has begun requiring taxpayers who visit its TACs to make advance appointments, a significant development when one considers that TACs were previously known as “walk-in sites.”

My message to you today is therefore two-fold:

1. The IRS needs more funding to meet the needs of U.S. taxpayers, particularly in the areas of taxpayer service and information technology systems.
2. Taxpayers would benefit from closer congressional oversight to ensure the IRS is spending its funds wisely and to rebuild trust between congressional oversight committees and the IRS’s leadership.

The IRS must be a “taxpayer service first” agency. In my most recent annual report, I expressed concern that the IRS historically has viewed itself first and foremost as an enforcement agency, and its emphasis on enforcement over taxpayer service is detrimental to both taxpayers and tax compliance. High-quality taxpayer service helps taxpayers voluntarily comply with their tax obligations and builds trust. Facilitating front-end compliance is much more cost-effective than collecting from noncompliant taxpayers one audit at a time. This is critical because more than 98 percent of all revenue the IRS collects is paid timely and voluntarily. Less than two percent is collected through enforcement actions.

There is no doubt that enforcement plays an important role in deterring noncompliance. But today the IRS spends 43 percent of its budget on enforcement and less than six percent on taxpayer outreach and education activities.⁸ I find that misguided. I believe the IRS should devote a higher percentage of its resources to taxpayer service. Not only would that make it easier for taxpayers paying the 98 percent of tax revenue to comply, but it would show that the government values U.S. taxpayers and treats them with the respect they deserve. As discussed below, for example, it is simply unacceptable that a taxpayer calling the IRS to pay a delinquent tax debt by entering into an installment agreement should have to call the IRS more than twice, on average, to get through and should then have to wait 47 minutes on hold to speak with an IRS employee. We can and should do better.

TAS has spent much of the last year taking a multi-faceted approach to learning more about taxpayer needs and preferences. I traveled the country and held 12 Public Forums on Taxpayer Needs and Preferences.⁹ Together with Members of Congress, I

⁸ Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, 129 Stat. 2242 (2015). An additional 33 percent of the IRS budget is allocated to the Operations Support account, which is used to support program activities. The balance of the budget is allocated mostly to returns processing and to the Business Systems Modernization account.

⁹ See National Taxpayer Advocate 2015 Annual Report to Congress xv. National Taxpayer Advocate Public Forums were held in the following locations: Washington, DC (Feb. 23, 2016); Glen Ellyn, IL (Mar. 9, 2016 with Congressman Roskam); Bronx, NY (Mar. 18, 2016 with Congressman Serrano);

heard directly from taxpayers and their representatives about the challenges they face in complying with the tax laws and dealing with the IRS.¹⁰ TAS also held focus groups of tax return preparers and practitioners at the IRS Tax Forums.¹¹ Additionally, TAS conducted a nationwide survey of U.S. taxpayers to hear directly what they need in the way of taxpayer service.¹² Finally, my immediate staff identified significant research on topics that have relevance for tax administration, including approaches to voluntary compliance, worldwide taxpayer service, alternative dispute resolution, taxpayer rights, fraud detection, online accounts, and the impact of geographic presence and focus.¹³

In this statement, I will provide my perspective on the recently concluded filing season and then address several areas of concern and challenges facing the IRS:

1. **Tax Reform** – The tax code, in its current state, remains the number one problem facing both the IRS and taxpayers. The complexity of the code creates enormous administrative challenges for the IRS and imposes huge compliance burdens on taxpayers. With a simpler code, the job of the IRS would be far easier.
2. **Filing Season** – The recently-concluded filing season proceeded more smoothly than during the previous two years. However, I remain concerned about the levels of service and wait times on the compliance phone lines during the filing season and all IRS phone lines during the rest of the year. I also am concerned about continuing cuts to services available at the IRS's Taxpayer Assistance Centers (TACs) and the reduction in the number of operational TACs, as well as the IRS's unwillingness to answer any tax-law questions beyond "basic" ones during the filing season and any tax-law questions at all outside the filing season. To me, it seems the IRS is simply walking away from a core responsibility of a tax administration agency.

Hendersonville, NC (Apr. 4, 2016 with Congressman Meadows); Harrisburg, PA (Apr. 8, 2016); Red Oak, IA (May 5, 2016 with Senator Grassley); Baltimore, MD (May 13, 2016 with Senator Cardin); Washington, DC (May 17, 2016); Parma, OH (Aug. 16, 2016 with Congressman Renacci); Portland, OR (Aug. 18, 2016); Los Angeles, CA (Aug. 22, 2016 with Congressman Becerra); and San Antonio, TX (Aug. 30, 2016 with Congressman Doggett).

¹⁰ For information about and full transcripts from the National Taxpayer Advocate Public Forums, see <https://taxpayeradvocate.irs.gov/public-forums> (last visited Apr. 25, 2017).

¹¹ TAS Communications and Liaison, *2016 IRS Nationwide Tax Forums TAS Focus Group Report: Preparers' Thoughts About IRS's Proposed Future State* (Oct. 2016), https://taxpayeradvocate.irs.gov/Media/Default/Documents/ResearchStudies/2016_TaxForum_FutureState_FocusGroup_Report.pdf.

¹² See National Taxpayer Advocate 2016 Annual Report to Congress, vol. 2, at 1-30 (Research Study: *Taxpayers' Varying Abilities and Attitudes Toward IRS Taxpayer Service: The Effect of IRS Service Delivery Choices on Different Demographic Groups*).

¹³ These literature reviews are published in Volume 3 of the National Taxpayer Advocate's 2016 Annual Report to Congress.

3. **Online Accounts** – I strongly support providing online account access to taxpayers, but I believe the IRS should continue to fully staff other service channels such as telephone and face-to-face service for taxpayers who want or need to interact with the IRS through personal contact. The population of the United States is large and diverse in its taxpayer service needs, and a one-size-fits-all approach is not appropriate for a tax collection agency. Moreover, voluntary compliance and trust in the tax system are best promoted by person-to-person contact. Thus, a multi-faceted service strategy based on the needs and preferences of taxpayers is required.
4. **Earned Income Tax Credit (EITC) and Child Tax Credit (CTC) Refund Holds** – To reduce improper payments, Congress enacted legislation that required the IRS this year to delay payment of any refund that includes the EITC or the refundable portion of the CTC until February 15. Although more analysis is needed, our preliminary assessment is that the implementation of this requirement went smoothly.
5. **Identity Theft and Refund Fraud** – Since 2005, I have raised concerns about the IRS's approach to assisting the victims of identity theft and refund fraud, and I have advocated for a simpler, more taxpayer-friendly procedure. The good news is that the IRS's inventory of tax-related identity theft cases has declined significantly since calendar year (CY) 2015, but more should still be done to ensure the process of identifying fraudulent returns is not overly burdensome for legitimate taxpayers whose returns are mistakenly held up. Additionally, as large-scale data breaches continue to plague both public and private organizations, the IRS must be proactive in developing strategies to protect taxpayers from becoming victims of tax-related fraud due to these breaches and not impose confusing and unnecessary requirements on persons affected by these breaches.
6. **Private Debt Collection** – Pursuant to legislation enacted in 2015, the IRS has recently begun to outsource the collection of some delinquent tax accounts to private collection agencies.¹⁴ I have significant concerns about the manner in which the IRS is administering this program, particularly with regard to the protection of taxpayer rights.
7. **User Fees** – The IRS has recently increased or proposed to increase user fees for services I consider to be central to tax administration. Because the IRS has the authority to retain and spend certain user fees, as well as the ability to spend user fee collections more flexibly than its appropriated funds, it has an extra incentive to maximize these fees. I am concerned that charging taxpayers for essential taxpayer services will have a negative effect on trust in the IRS and may promote noncompliance with the tax law.

¹⁴ IRC § 6306(c)(1).

- 8. Information Technology (IT) Needs** – The IRS is operating an aged web of computing systems that are not compatible with each other, require employees to manually transcribe information between systems, and cause the IRS to keep numerous paper files to be mailed between offices to complete everyday tasks. In the 21st century, this is an unacceptable way to do business. In my view, the IRS requires additional funding – and oversight – to upgrade and streamline its case management systems.

I. Simplify the Internal Revenue Code

At the outset, I note the need for comprehensive tax reform, including provisions relating to the taxation of individuals. The compliance burdens the current tax code imposes are overwhelming for taxpayers and the IRS alike. My staff analyzed IRS data for 2015 and determined that individuals and businesses spend about six billion hours a year complying with the tax code's filing requirements – not including the millions of additional hours they spend responding to IRS audits or notices. If tax compliance were an industry, it would be one of the largest in the United States. To consume six billion hours, the “tax industry” requires the equivalent of three million full-time workers.

The tax code, which runs several million words, contains more than 200 tax deductions, credits, exclusions, and similar tax breaks, known collectively as “tax expenditures.” In combination, the Treasury Department has estimated that tax expenditures in FY 2016 came to about \$1.4 trillion – more than the \$1.2 trillion Congress appropriated to fund the entire federal government. Put simply, Congress now spends more money each year through the tax code than it spends through the appropriations process.¹⁵

As the National Taxpayer Advocate, I believe the most effective and comprehensive way to reduce taxpayer burden is for Congress to vastly simplify the Internal Revenue Code. In my most recent Annual Report to Congress, I noted that even if comprehensive tax reform is too heavy a lift, there are numerous proposals that can be enacted in targeted areas that would bring about significant simplification and reduce taxpayer (and IRS) burden.¹⁶

¹⁵ For prior discussions of tax compliance burdens and recommendations for tax reform, see National Taxpayer Advocate 2012 Annual Report to Congress 3-23 (Most Serious Problem: *The Complexity of the Tax Code*); National Taxpayer Advocate 2010 Annual Report to Congress 3-14 (Most Serious Problem: *The Time for Tax Reform Is Now*); National Taxpayer Advocate 2010 Annual Report to Congress 365-372 (Legislative Recommendation: *Enact Tax Reform Now*); National Taxpayer Advocate 2005 Annual Report to Congress 375-380 (Key Legislative Recommendation: *A Taxpayer-Centric Approach to Tax Reform*); *Fundamental Tax Reform: Hearing Before the H. Comm. on Ways and Means*, 112th Cong. 6-38 (2011) (statement of Nina E. Olson, National Taxpayer Advocate), <https://www.gpo.gov/fdsys/pkg/CHRG-112hhrg70869/pdf/CHRG-112hhrg70869.pdf>; *Public Meeting of the President's Advisory Panel on Federal Tax Reform* (Mar. 3, 2005) (statement of Nina E. Olson, National Taxpayer Advocate), <http://govinfo.library.unt.edu/taxreformpanel/meetings/meeting-03032005.html>.

¹⁶ National Taxpayer Advocate 2016 Annual Report to Congress 305-324 (Legislative Recommendation: *Tax Reform: Simplify the Internal Revenue Code Now*); see Nina E. Olson, *Complexity Is the Root of All Evil (at Least in the Tax Code)*, W.S. Journal, Apr. 18, 2017, at A15.

II. The Filing Season Ran Relatively Smoothly, But Taxpayer Service Remains Below Par

On the surface, the recently concluded filing season was relatively successful. The IRS processed about 135 million individual income tax returns without a major hitch.¹⁷ The rate of tax returns filed electronically continued to rise.¹⁸ During the filing season, the IRS answered 79 percent of the telephone calls it received on its toll-free Accounts Management telephone lines, up from 72 percent last year.¹⁹ And wait times on the Accounts Management telephone lines dropped from 11 minutes last year to seven minutes this filing season.²⁰ In recent testimony, Commissioner Koskinen said he believes this has been the smoothest filing season the IRS has run since he became the Commissioner.²¹ In most respects, I concur with this assessment.

Concerns About IRS Customer Service

Despite improved customer service in some areas during the filing season, the IRS continues to be unable to meet the needs of U.S. taxpayers in important respects:

- **The Percentage of All Calls IRS Telephone Assistors Answered During the Filing Season Declined Slightly from FY 2016 to FY 2017.** The “official” measure of the IRS’s telephone performance is the Customer Service Representative “Level of Service” (or “LOS”) on its Account Management telephone lines. The LOS is the percentage of calls answered by telephone assistors among all calls gated to an assistor (*i.e.*, calls gated to automation are excluded from this measure). While it is true that the LOS on the Accounts Management lines was 79 percent and the wait time was about seven minutes, there are many telephone lines the IRS maintains that are not included under the “Accounts Management” umbrella. If one looks at all IRS telephone lines (the “Enterprise Total,” in IRS parlance), the LOS actually dropped slightly this filing season as compared with last year and stood at 71 percent.²²

¹⁷ IRS Filing Season Statistics for Week Ending April 21, 2017.

¹⁸ *Id.*

¹⁹ IRS, JOC, *Snapshot Reports: Enterprise Snapshot* (week ending April 22, 2017).

²⁰ *Id.*

²¹ *The 2017 Tax Filing Season: Internal Revenue Service Operations and the Taxpayer Experience: Hearing Before the S. Comm. On Finance*, 115th Cong. (April 25, 2017) (statement of John A. Koskinen, Commissioner of Internal Revenue).

²² IRS, JOC, *Snapshot Reports: Enterprise Snapshot, Enterprise Total* (week ending April 22, 2017). The LOS on all IRS telephone lines (Enterprise Total) for the filing season was 70.7 percent as of April 22, 2017, as compared with 71.3 percent as of the corresponding date in 2016.

- **The Percentage of Calls IRS Telephone Assistors Answered During the Filing Season on Compliance Lines Declined Substantially from FY 2016 to FY 2017, While Wait Times Nearly Doubled.** Most of the IRS phone lines excluded from the Accounts Management category are compliance lines (e.g., audit and collection). The telephone lines pertaining to the IRS's automated collection system received 4.2 million calls during the filing season, and the IRS answered only 44 percent – down from 64 percent last filing season. Wait times rose from 23 minutes last filing season to 42 minutes this year.²³
- **IRS Telephone Assistors Answered Only 40 Percent of Calls from Taxpayers Seeking to Make Payment Arrangements, and the Average Hold Time Was 47 Minutes.** One IRS compliance line is the "Installment Agreement/Balance Due" line. It received about 2.7 million calls during the filing season. For the most part, these calls come from taxpayers who are seeking to make payment arrangements – the sort of calls most private businesses would pick up immediately. Yet the IRS answered only 40 percent of these calls, and the average wait time among taxpayers who got through was a staggering 47 minutes. The IRS's performance on this telephone line deteriorated markedly as compared with the 2016 filing season. Last filing season, the IRS answered 76 percent of these calls, and the wait time was 11 minutes. Thus, the percentage of calls the IRS answered from taxpayers seeking to make payment arrangements on this line dropped nearly in half as compared with last year, and wait times were more than four-fold.²⁴
- **The IRS Receives More Telephone Calls Outside the Filing Season Than During the Filing Season, and Its Performance at Other Times Has Been Dramatically Lower.** While the IRS's performance during the filing season receives considerable attention, the IRS typically receives fewer than half its calls during this period. In FY 2016, for example, the IRS received 55 million calls during the filing season and 117 million calls over the course of the full fiscal year on all its telephone lines, and it received 50 million calls during the filing season and 104 million calls during the full fiscal year on its Accounts Management lines.²⁵ The IRS staffs up considerably during the filing season by hiring seasonal employees to boost its LOS, but the larger number of taxpayers who call during other points of the year don't fare nearly as well. In FY 2016, the IRS answered 53 percent of its calls on its Accounts Management lines over the full year, as compared with 72 percent during the filing season.²⁶ To average 53 percent over the course of the full year, the LOS outside the filing season was necessarily well below 53 percent. Similarly, the average wait time of 11 minutes

²³ IRS, JOC, *Snapshot Reports: Enterprise Snapshot, Consolidated ACS* (week ending April 22, 2017).

²⁴ IRS, JOC, *Snapshot Reports: Product Line Detail, Installment Agreement/Balance Due* (week ending April 22, 2017).

²⁵ IRS, JOC, *Snapshot Reports: Enterprise Snapshot* (week ending Sept. 30, 2016).

²⁶ *Id.*

during the filing season increased to 18 minutes for the full year, which means callers outside the filing season waited on hold, on average, for substantially longer than 18 minutes.

- **The IRS Now Answers Only “Basic” Tax-Law Questions During the Filing Season and No Tax-Law Questions at All Outside the Filing Season.** Citing funding reductions, the IRS sharply curtailed the scope of tax-law questions it would answer beginning in 2014. It now answers only “basic” questions during the filing season, and it does not answer tax-law questions at all after the filing season, including from the more than 15 million taxpayers who file their returns later in the year.²⁷ I consider this a significant failing. In my view, answering tax-law questions is a fundamental responsibility of a tax administration agency.
- **The IRS Is Continuing a Long-Term Trend of Scaling Back the Availability of Taxpayer Services at the Taxpayer Assistance Centers.** The IRS operates nearly 400 TACs. In the past, the IRS has served more than five million taxpayers each year in the TACs, and it provided a wide range of services, such as assisting with tax return preparation and answering tax-law questions. This year, the IRS has moved to an “appointment only” system in the TACs – a significant development given that the TACs used to be known as “walk-in sites.” On several occasions, the IRS has made important services less accessible to taxpayers and then cited the (predictable) decline in usage as a basis for making further reductions or eliminating the services altogether. For example, the IRS prepared nearly 500,000 tax returns for taxpayers in FY 2004.²⁸ Over time, it placed significant limitations on the number of returns employees could prepare, and it began to require advance appointments. As a result of making the service harder to obtain, the IRS prepared substantially fewer returns over time, reaching a low of about 125,000 during the 2013 filing season. The IRS then eliminated the service, citing low usage.

The same is true with answering tax-law-questions. The Government Accountability Office (GAO) has reported the number of tax-law questions answered by the IRS during the filing season alone dropped from 795,000 in 2004 to 110,000 in 2013.²⁹ There is no evidence that taxpayers had fewer

²⁷ During 2016, the IRS received nearly 137 million tax returns by April 22 and nearly 153 million by December 30, indicating that nearly 16 million returns were received after the filing deadline. See IRS Filing Season Statistics (weeks ending April 22, 2016 and Dec. 30, 2016).

²⁸ See National Taxpayer Advocate 2014 Annual Report to Congress 3, 21 (Most Serious Problem: *Taxpayer Service: Taxpayer Service Has Reached Unacceptably Low Levels and Is Getting Worse, Creating Compliance Barriers and Significant Inconvenience for Millions of Taxpayers*) (and GAO data cited therein).

²⁹ GAO, 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-07-27, *Tax Administration: Most Filing Season Services Continue to Improve, but Opportunities Exist for Additional Savings* 29 (Nov. 2006) (supplemented with more precise IRS data provided to TAS by the IRS Wage & Investment Division for 2004 through 2006).

questions. Rather, the IRS reduced TAC staffing and reduced the scope of questions it was willing to answer, and wait times became unreasonably long. As it became harder and harder to get answers to tax-law questions, taxpayers became deterred from asking. The IRS's decision to restrict employees from answering tax-law questions was based partly on this "reduced demand."

The IRS says that taxpayers are visiting the TACs less frequently because when they call for appointments, telephone assistants are frequently able to address their questions, obviating the need to visit. To some degree, that is undoubtedly true. But many taxpayers with tax problems still want to talk to an IRS employee face-to-face. If the IRS's current trend continues, they soon may not have that opportunity. The IRS has already reduced the number of TACs from 401 to 376 since 2011.³⁰ In addition, 22 TACs have no staff, while 95 have only one employee,³¹ and it is considering closing a significant number of additional TACs through FY 2018. Because of its new "appointment only" policy, the IRS is projecting that the number of taxpayers visiting a TAC will decline from about 5.6 million in FY 2015 to 3.5 million this year.³² I encourage the subcommittee to require the IRS to conduct a more in-depth study of taxpayer preferences for face-to-face assistance, in conjunction with studies by my office, the GAO and the Treasury Inspector General for Tax Administration (TIGTA), before any additional TACs are permitted to close.

"Customer Callback" Technology

Many private businesses and federal agencies, including the Social Security Administration and the Department of Veterans Affairs, have deployed customer callback systems that allow callers to choose between waiting on hold and electing to be called back when their place in the telephone queue is reached.³³ We believe a customer callback system would improve the taxpayer experience at a reasonable cost.

In the President's FY 2015 and FY 2016 budgets, the IRS proposed this initiative and estimated it would cost about \$3.3 million.³⁴ In November 2015, Commissioner Koskinen said that although the customer callback technology itself would cost about

³⁰ In 2011, the IRS operated 401 TACs. IRS response to TAS information request (Dec. 23, 2014). As of December 31, 2016, the IRS operated 376 TACs, a reduction of six percent. IRS response to TAS fact check (Dec. 20, 2016).

³¹ IRS response to TAS fact check (Dec. 20, 2016).

³² IRS Wage & Investment Division, *Business Performance Review 7* (Feb. 9, 2017).

³³ See GAO, GAO-17-140, *Financial Audit: IRS's Fiscal Years 2016 and 2015 Financial Statements* 116-117 (Nov. 2016).

³⁴ IRS, Congressional Justification for Appropriations accompanying the President's FY 2015 Budget at IRS-20 (2014); IRS, Congressional Justification for Appropriations accompanying the President's FY 2016 Budget at IRS-22 (2015).

\$3.5 million, the IRS had determined its phone system would need to be upgraded at a cost of about \$45 million in order to allow the customer callback technology to run.³⁵

Even if that is accurate, we think customer callback technology would be a prudent investment. For context, the IRS's FY 2016 budget proposal requested about \$186 million to increase the Level of Service (LOS) on its toll-free lines to 80 percent.³⁶ The significant majority of that funding would have paid for additional customer service representatives and other costs that recur annually. By contrast, the deployment of a customer callback system would essentially be a one-time cost, and it would permanently improve the IRS's LOS.

It should be emphasized that a high percentage of taxpayers who don't reach the IRS on their first attempt keep calling until they get through. As noted above, the LOS during FY 2016 averaged 53 percent, and those taxpayers who managed to reach an IRS telephone assistor had to wait an average of 18 minutes on hold.³⁷

With customer callback technology, unsuccessful calls would be substantially reduced – as would hold times. Most taxpayers would only have to call the IRS one time. Thus, this one-time cost would improve taxpayer service and substantially increase the LOS for years into the future.

Accordingly, I recommend that Congress direct the IRS to take the following action:

- Complete a study of “customer callback” technology and submit a report to Congress describing its costs and benefits.

III. The IRS's Trend Toward Heavy Reliance on Delivering Services Through Online Accounts and Away from Personal Interaction Does Not Adequately Take into Account the Widely Divergent Needs and Preferences of the U.S. Taxpayer Population

The reduction in current taxpayer service outlined above is occurring in conjunction with the IRS's increasing attempts to move taxpayers from person-to-person interaction toward online interaction with the tax agency. This shift is often justified as a movement toward less costly service options. However, I believe these planned shifts are only superficially less costly, because digital interaction is not appropriate for certain populations, nor is it suitable for taxpayers with intensely factual and specific matters (which is what all but the most simple tax transactions are). Migrating taxpayers toward

³⁵ See Lisa Rein, *IRS Customer Service Will Get Even Worse This Tax Filing Season, Tax Chief Warns*, Washington Post.com, Nov. 3, 2015.

³⁶ See IRS, Congressional Justification for Appropriations accompanying the President's FY 2016 Budget at IRS-22 (2015).

³⁷ IRS, Joint Operations Center, *Snapshot Reports: Enterprise Snapshot – Accounts Management* lines (week ending Sept. 30, 2016).

self-help and less personalized service channels may benefit the IRS in the short term; however, if taxpayers face too many obstacles in their attempted interactions with the IRS, their frustrations will mount and they may become less willing to comply voluntarily in the future. In particular, once a taxpayer faces enforcement action, it is imperative that the IRS assist the taxpayer by learning the taxpayer's particular facts and circumstances to help bring him or her into compliance and to educate the taxpayer on how to avoid making similar mistakes in the future.

I believe the online account application is a beneficial addition to the IRS's service offerings as long as it is only one component of a multi-channel service strategy. In fact, I have advocated in the past that the IRS develop the online account.³⁸ Despite the utility of the online account application, research and experience has shown that a significant percentage of taxpayers cannot access the online account application. Specifically, approximately 33 million U.S. taxpayers have no broadband access.³⁹ Taxpayers with internet service connections slower than broadband will likely experience delays when attempting to access large files or complex web pages. In addition, we estimate 14 million U.S. taxpayers have no Internet access at all.⁴⁰

For taxpayers who do have online access, there are significant concerns about being able to pass e-authentication screens. As of April 22, 2017, of the approximately 1.3 million account registration attempts since the application launched, only about 20 percent were successful.⁴¹ I am not suggesting that the IRS reduce its security protections. I believe protecting the security of taxpayer information is absolutely essential. However, the IRS must recognize that providing necessary security has implications for how many taxpayers will be able to access online accounts and how many will need to use other service channels, such as telephones or TACs.

The automation of IRS services ignores the fact that the United States is geographically large, with a diverse population and many local micro-economies and distinct regional cultures. In order to provide meaningful service to taxpayers nationwide, the IRS must establish a geographic presence in the states. This geographic footprint will enable IRS employees to understand the unique challenges and situations facing the culturally and geographically diverse population of taxpayers. Unfortunately, the IRS has reduced its

³⁸ See, e.g., National Taxpayer Advocate 2013 Annual Report to Congress, vol. 2, at 67-96 (Research Study: *Fundamental Changes to Return Filing and Processing Will Assist Taxpayers in Return Preparation and Decrease Improper Payments*).

³⁹ See National Taxpayer Advocate 2016 Annual Report to Congress, vol. 2, at 1-30 (Research Study: *Taxpayers' Varying Abilities and Attitudes Toward IRS Taxpayer Service: The Effect of IRS Service Delivery Choices on Different Demographic Groups*).

⁴⁰ *Id.* TAS survey research also found that such vulnerable groups as low income, seniors and taxpayers with disabilities are less likely to have broadband access at home.

⁴¹ IRS, Wage and Investment Division, JOC, *Online Account External Launch Weekly Report* (week ending April 22, 2017). The registration rate increased to 24 percent in April 2017.

geographic presence since 2011. Figure 1 illustrates the reduction in IRS geographic presence and employees between 2011 and 2016.⁴²

Figure 1, Locations with Specified Employees in the Last Pay Period of the Fiscal Year

Number of Locations, Employees, or Visitors	2011	2012	2013	2014	2015	2016
IRS Offices (Cities)	541	523	510	499	479	470
Appeals Officers (AOs)	1,129	1,058	958	881	795	739
Revenue Officers (ROs)	4,402	4,035	3,703	3,441	3,191	3,072
Revenue Agents (RAs)	11,959	11,258	10,502	9,776	9,090	8,871
Stakeholder Liaison Outreach Employees	137	123	119	110	105	98
Stakeholder Partnerships, Education and Communication Outreach Employees	522	475	444	405	386	365
Taxpayer Assistance Centers (TACs)	401	401	398	382	378	376
TAC Service Reps	1,639	1,515	1,484	1,520	1,423	1,267

Twelve states have no Appeals Officers stationed within their boundaries,⁴³ and 14 states have no IRS liaisons to Small Business and Self-Employed taxpayers.⁴⁴ In fact, according to IRS data, the agency dedicates only 98 employees to conduct outreach and education to the roughly 62 million Small Business and Self-Employed taxpayers (*i.e.*, taxpayers who are self-employed or own small businesses), and only 376 employees to conduct outreach and education to the nearly 125 million Wage and Investment taxpayers (*i.e.*, taxpayers who are classified as “employees”). Meanwhile, the IRS has over 3,000 revenue officers (who conduct field collection activities) and over 8,800 revenue agents (who conduct field audit activities).⁴⁵

Despite this imbalance, the IRS budget request for FY 2017 sought an increase of 7.2 percent in enforcement funding, as compared with an increase of just 3.1 percent in

⁴² National Taxpayer Advocate 2016 Annual Report to Congress 86-97 (Most Serious Problem: *Geographic Focus: The IRS Lacks an Adequate Local Presence in Communities, Thereby Limiting Its Ability to Meet the Needs of Specific Taxpayer Populations and Improve Voluntary Compliance*).

⁴³ The 12 states that lack a permanent Appeals Officer are Alaska, Arkansas, Delaware, Idaho, Kansas, Montana, North Dakota, New Mexico, Rhode Island, South Dakota, Vermont, and Wyoming. There is also no Appeals Office in the territory of Puerto Rico. IRS Office of Appeals response to TAS information request (June 6, 2016).

⁴⁴ The 14 states are Alaska, Delaware, Hawaii, Kentucky, Mississippi, Montana, North Dakota, Nebraska, New Hampshire, South Dakota, Vermont, West Virginia, Wisconsin, and Wyoming. There also is no liaison in the District of Columbia. IRS response to TAS fact check (Dec. 15, 2016); IRS Human Resources Reporting Center, *Report of Small Business/Self-Employed (SB/SE) Job Series 0526, Stakeholder Liaison Field Employees as of the week ending October 1, 2016* (Dec. 1, 2016).

⁴⁵ IRS response to TAS fact check (Dec. 16, 2016).

taxpayer services funding.⁴⁶ This proposal to increase enforcement funding by more than twice the rate of taxpayer services funding was made against a backdrop in which the agency has been unable to meet basic taxpayer needs.

Accordingly, I recommend the following:

- The IRS, in collaboration with TAS, should undertake a comprehensive study of taxpayer needs and preferences by taxpayer segment, using telephone, online, and mail surveys, focus groups, town halls, public forums, and research studies. These initiatives should be designed to determine *taxpayer* needs and preferences, and not be biased by the IRS's own desired direction.
- Congress should consider directing the IRS and the National Taxpayer Advocate to jointly report on the results of this comprehensive study.

IV. The IRS's Implementation of the Requirement to Hold Refunds on Returns Claiming the Earned Income Tax Credit and the Refundable Portion of the Child Tax Credit Appears to Have Gone Smoothly

The Earned Income Tax Credit (EITC) was enacted as a work incentive in the Tax Reduction Act of 1975.⁴⁷ It has become one of the government's largest means-tested anti-poverty programs.⁴⁸ In tax year (TY) 2015, over 27 million taxpayers received about \$67 billion in EITC benefits.⁴⁹ Unlike traditional anti-poverty and welfare programs, the EITC was designed to have an easy "application" process by allowing an individual to claim the benefit on his or her tax return. This approach virtually eliminates the significant costs associated with up-front eligibility verification in traditional social welfare programs, but results in a high improper payment rate.⁵⁰ To address the EITC improper payment rate, Congress included a directive in the Protecting Americans from Tax Hikes (PATH) Act that requires the IRS to delay payment of any refund that

⁴⁶ U.S. Department of the Treasury, *Internal Revenue Service FY 2017 Budget-in-Brief 1*, <https://www.irs.gov/pub/newsroom/IRS%20FY%202017%20BIB.pdf>.

⁴⁷ Pub. L. No. 94-12, § 204, 89 Stat. 26 (1975).

⁴⁸ Congressional Budget Office, *Federal Means-Tested Programs and Tax Credits – Infographic* (Feb. 11, 2013), <https://www.cbo.gov/publication/43935>.

⁴⁹ IRS, *About EITC*, <https://www.eitc.irs.gov/EITC-Central/abouteitc>.

⁵⁰ An improper payment is defined as "any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments) under statutory, contractual, administrative, or other legally applicable requirements" and "any payment to an ineligible recipient." Improper Payments Elimination and Recovery Act of 2010, Pub. L. No. 111-204, § 2(e) (2010) amending Improper Payments Information Act of 2002, Pub. L. No. 107-300 (2002) by striking § 2(f) and adding (f)(2). The IRS estimates that for FY 2016, between 22.2 percent (\$15.5 billion) and 25.9 percent (\$18.1 billion) of the total EITC program payments of \$69.8 billion were improper. Department of Treasury, *Agency Financial Report Fiscal Year 2016* 49 (Nov. 2016).

includes the EITC or the refundable portion of the Child Tax Credit (CTC) until February 15 of each filing year.⁵¹

Based on an analysis of IRS data from filing season 2017, it appears that all computer-generated freezes related to the PATH Act released as anticipated. Furthermore, TAS compared the number of EITC refunds issued week-by-week in filing season 2016 to the comparable period in filing season 2017. We found that by the third week of filing season 2016, the IRS had issued 13.6 million refunds. In comparison, by the third week of filing season 2017 (the first week in which EITC refunds were issued), the IRS had issued refunds to slightly more than 11.3 million taxpayers. See Figure 2.

Figure 2, Comparison of Refunds Issuance Dates on Returns Receiving EITC Between Filing Seasons 2016 and 2017

Cycle (week)⁵²	2016 Filing Season Count	2016 Filing Season Cumulative	2017 Filing Season Count	2017 Filing Season Cumulative
4th	855,083	855,083		
5th	6,569,700	7,424,783		
6th	3,679,630	11,104,413		
7th	2,523,418	13,627,831	11,261,003	11,261,003
8th	1,905,990	15,533,821	2,107,633	13,368,636
9th	1,462,160	16,995,981	1,898,720	15,267,356
10th	1,170,029	18,166,010	1,426,186	16,693,542
11th	968,727	19,134,737	1,123,215	17,816,757
12th	836,918	19,971,655	962,178	18,778,935
13th	741,827	20,713,482	860,784	19,639,719

⁵¹ Protecting Americans from Tax Hikes (PATH) Act of 2015, Pub. L. No. 114-113, Division Q, Title II, § 201(b), 129 Stat. 2242, 3076 (2015) (codified at IRC § 6402(m)). The freeze on refunds involving EITC or the refundable portion of the CTC applies to refunds made after December 31, 2016. The National Taxpayer Advocate previously made a similar recommendation. *The National Taxpayer Advocate's 2014 Annual Report to Congress: Hearing Before the H. Subcomm. on Government Operations* (2015) (statement of Nina E. Olson, National Taxpayer Advocate).

⁵² The cycle equates to the week of the calendar year. For example, the fourth cycle equates to the fourth week of the calendar year. For 2017, the IRS delayed the refunds of returns claiming EITC until February 15, the seventh cycle of the year. Refunds were not delayed for taxpayers claiming the EITC last year, and the IRS had issued refunds to taxpayers claiming EITC by the fourth week of 2016.

TAS also compared the period of time between when a return posted and when the refund was issued in filing seasons 2016 and 2017. For filing season 2016, about 239,000 taxpayers had to wait two weeks or more for the IRS to issue their refunds after their returns posted. This number climbed to over seven million taxpayers in filing season 2017 (a 2,858 percent increase).⁵³ However, the increase in waiting time declined as filing season 2017 progressed. For taxpayers who had delays of four weeks or more, there was a 31 percent increase between filing seasons 2016 and 2017 (over 108,000 taxpayers in filing season 2016 compared to over 141,000 taxpayers in filing season 2017). The average delay was about a week longer in 2017 than 2016 (through the end of March 2017).

The number of frozen EITC returns between filing seasons 2016 and 2017 increased by nearly 260 percent (from about 41,000 to 148,000), and EITC dollars frozen increased by about 225 percent (from \$147 million to \$479 million).⁵⁴ The dollars frozen in filing season 2017 constitute a 2.1 percent decrease in improper payments from filing season 2016 to 2017.⁵⁵ This is not surprising because although income misreporting is the most frequent source of EITC errors, it does not account for the largest dollar amount of EITC errors.⁵⁶ Because EITC noncompliance is attributable to multiple causes, there is no silver bullet; instead, it will take multiple approaches to bring down the improper payment rate. Upfront W-2 matching is an important step, and as discussed later in this testimony, it provides additional benefits in the area of identity theft and other refund fraud.

V. Tax-Related Identity Theft Appears to Be on the Decline, But Challenges Remain as the IRS Combats Refund Fraud and Large-Scale Data Breaches

Tax-related identity theft is an invasive crime that has significant impact on its victims and the IRS. For years, I have highlighted the need for the IRS to establish or improve procedures to assist victims of identity theft.⁵⁷

⁵³ TAS review of Individual Returns Transaction File and the Individual Master File.

⁵⁴ *Id.* Data includes taxpayers whose TY 2015 refunds were processed by March 2016 and whose Tax Year 2016 returns were processed by March 2017 and scheduled to receive EITC after IRS math error processing, but prior to audit.

⁵⁵ This percentage is calculated as the additional \$332 million of EITC not refunded divided by the FY 2015 lower bound EITC improper payment estimate of \$15.5 billion.

⁵⁶ IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* (Pub. 5162, Aug. 2014); see National Taxpayer Advocate 2016 Annual Report to Congress 325-357 (Legislative Recommendation: *Tax Reform: Restructure the Earned Income Tax Credit and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden*).

⁵⁷ See National Taxpayer Advocate 2015 Annual Report to Congress 180-87; National Taxpayer Advocate 2014 Annual Report to Congress vol. 2, 44-90; National Taxpayer Advocate 2013 Annual Report to Congress 75-83; National Taxpayer Advocate 2012 Annual Report to Congress 42-67; National Taxpayer Advocate 2011 Annual Report to Congress 48-73; National Taxpayer Advocate 2009 Annual Report to Congress 307-17; National Taxpayer Advocate 2008 Annual Report to Congress 79-94; National Taxpayer Advocate 2007 Annual Report to Congress 96-115; National Taxpayer Advocate 2005

Decline in Identity Theft Cases

During CY 2015, the IRS received nearly 700,000 identity theft cases in which the taxpayer needed victim assistance.⁵⁸ In CY 2016, the IRS received about 376,000 identity theft cases – a decline of about 46 percent.⁵⁹ As of January 2017, the IRS-wide inventory of identity theft cases was under 30,000 – less than half of the inventory two years ago.⁶⁰

We are seeing a similar decline in identity theft cases within TAS. In FY 2017 (through March), TAS had identity theft case receipts of 11,314 – less than half the 24,491 identity theft cases we received by the same point in FY 2016.⁶¹

Potential Reasons for Decline in Tax-Related Identity Theft

I believe that a significant factor in the decline of tax-related identity theft is the impact of the accelerated due dates for certain information reporting. As part of the PATH Act enacted in December 2015, the due date for filing Forms W-2, *Wage and Tax Statement*, and Forms 1099-MISC, *Miscellaneous Income*, with the Social Security Administration (SSA) was moved up to January 31.⁶² Prior to 2017, the due dates for these information reporting forms were the last day of February (or March, if filed electronically).

The accelerated deadline allows the IRS to verify the legitimacy of tax returns by comparing the return data against the data on Forms W-2 filed by employers **before** paying out refunds. Prior to the enactment of the PATH Act, the IRS received W-2 data from the SSA after the filing season, when the majority of refunds had already been issued, and began data matching in the summer.

By the end of week 12 in CY 2017, the IRS had received 222 million Forms W-2, a nearly 30 percent increase from the 171 million received by the same point in 2016.⁶³ Similarly, there was a big increase in the number of Forms 1099-MISC the IRS received in 2017 as compared with 2016. By week 12 of CY 2017, the IRS received 31

Annual Report to Congress 180-91; National Taxpayer Advocate 2004 Annual Report to Congress 133-36.

⁵⁸ IRS, *Global ID Theft Report* (Jan. 2017). Part of the decline in identity theft cases may be attributable to the IRS's decision to modify the criteria for counting cases included in the "Identity Theft Taxpayer Impacted" inventory.

⁵⁹ *Id.*

⁶⁰ *Id.*

⁶¹ Data obtained from Taxpayer Advocate Management System (TAMIS) (Apr. 1, 2016; Apr. 1, 2017).

⁶² PATH Act of 2015, Pub. L. No. 114-113, Division Q, Title II, § 201(a), 129 Stat. 2242, 3076 (2015) (codified at IRC § 6071(c)).

⁶³ IRS Compliance Data Warehouse, Information Returns Master File (as of cycle 201712).

million Forms 1099-MISC, more than 2.5 times the 12 million received by the same week in the prior year.⁶⁴ (Forms 1099-MISC are used to report non-employee compensation.)

In addition to the PATH Act provisions, there are other reasons why tax-related identity theft is on the decline. The IRS is doing a better job of collaborating with state tax agencies and with the tax software industry to develop some very effective safeguards against refund fraud.

- **Driver's License Verification.** In an ongoing effort to protect taxpayers from identity theft, the IRS, state tax agencies, and the tax software industry have worked together to request information from taxpayers contained in a driver's license (or state-issued identification) when they e-file. Failure to provide such information, while not mandatory to file a federal return, may delay processing of the return.
- **W-2 Verification Code.** Many taxpayers (about 50 million) received a Form W-2 with a 16-character "verification code" in 2017.⁶⁵ These taxpayers will be prompted to enter this code in the tax software; without it, the return will be rejected. This safeguard allows the IRS to verify the authenticity of the W-2 data.
- **Identity Protection Personal Identification Number (IP PIN).** Victims who have had their identity and address verified by the IRS may have been issued a six-digit IP PIN. The IP PIN is a single-use number; a new IP PIN is issued each December prior to the filing season. Taxpayers who have received an IP PIN must use it when filing a return.

High False Positive Rates Undermine Effectiveness of Fraud Filters

The IRS has developed numerous filters, rules, and data mining models to combat refund fraud. For example, the Taxpayer Protection Program (TPP) identifies suspicious tax returns and notifies the taxpayer that there was a problem processing the return. As of April 13, 2017, 1.3 million suspicious tax returns were selected by the TPP, down from 1.5 million returns selected by the TPP over the same period in 2016.⁶⁶

The IRS's fraud detection systems have a history of high false positive rates. In CY 2016, the false positive rate for TPP ID theft filers was 53 percent, meaning that of all returns flagged as potentially fraudulent, more than half turned out to be legitimate.⁶⁷

⁶⁴ *Id.*

⁶⁵ IRS, *IRS Tests W-2 Verification Code for Filing Season 2017*, <https://www.irs.gov/individuals/w-2-verification-code> (last visited Apr. 25, 2017).

⁶⁶ IRS Return Integrity & Compliance Services (RICS), *Update of the Taxpayer Protection Program (TPP)* (Apr. 19, 2017); IRS RICS, *Update of the Taxpayer Protection Program (TPP)* (Apr. 20, 2016).

⁶⁷ IRS Wage & Investment Division, *Business Performance Review 9* (Feb. 9, 2017).

High false positive rates can lead to significant downstream consequences for both the IRS and taxpayers. For example, these over-inclusive filters unnecessarily delay refunds of legitimate taxpayers, possibly placing these taxpayers in a financial hardship; create unnecessary work for IRS employees, needlessly draining the IRS's limited resources; and potentially damage taxpayers' willingness to voluntarily comply with their tax obligations.

I continue to support the use of data-driven models to detect suspicious tax returns. However, the IRS has an obligation to sufficiently test these filters. A year ago, the IRS agreed to track and monitor its false positive rates. While that is a positive development, it is still unclear how the IRS is using the information and whether the information will be used to adjust IRS filters in real time.

Data Breaches

Hackers that infiltrate the cybersecurity of a large corporation can gain access to thousands of taxpayer names and associated personal identifying information that can be used to file falsified tax returns. One such breach involved the Free Application for Federal Student Aid (FAFSA) website, where hackers may have accessed the tax information of applicants for federal student aid. The IRS has started mailing notification letters to approximately 100,000 potentially impacted taxpayers and has offered a year of free credit monitoring.⁶⁸

As large-scale data breaches become more prevalent, the IRS should carefully consider how to assist victims. For example, should it create a marker that would lock down the taxpayer identification number for victims of a data breach and issue an IP PIN or require authentication in person? I believe the IRS should try to find less intrusive ways to provide extra scrutiny to tax returns filed under the taxpayer identification number of victims of large-scale data breaches.

VI. The Private Debt Collection Program Threatens Taxpayer Rights

From 2006 through 2009, the IRS operated a program in which it contracted with private debt collection agencies to collect certain delinquent tax debts. The IRS discontinued the program after concluding it was not effective. In 2015, Congress enacted legislation directing the IRS to resume outsourcing certain inactive tax receivables.⁶⁹ Although I believe that tax collection is an inherently governmental function, my obligation is to ensure the IRS adheres to the law and that it implements a private debt collection

⁶⁸ IRS, *Questions and Answers: Mailings About Suspicious Activity Related to the DRT and FAFSA*, <https://www.irs.gov/uac/newsroom/questions-and-answers-mailings-about-suspicious-activity-related-to-the-drt-and-fafsa> (last visited Apr. 25, 2017).

⁶⁹ Fixing America's Surface Transportation Act, Pub. L. No. 114-94, Div. C, Title XXXII, §§ 32102, 32103, 129 Stat. 1312, 1733-36 (2015) (FAST Act) (redesignating subsections (c), (d), (e), and (f) as (e), (f), (g), and (k) and adding new subsections (c), (d), (h), (i), and (j) to IRC § 6306).

(PDC) program effectively, efficiently, and in accordance with taxpayer rights.⁷⁰ I am concerned that the IRS, in an effort to run this program “on the cheap,” is implementing it in a way that will harm taxpayers.

Congress has carefully delineated the extent to which private collection agencies (PCAs) may engage in collection activities. Based on the program documents my staff has reviewed, I am concerned that the IRS is allowing PCAs to exceed those limits. For example, Congress authorized PCAs only to request full payment or offer installment agreements (IAs) not to exceed five years, and, if the taxpayer says he or she cannot pay the liability in full within five years, to collect financial information from the taxpayer.⁷¹ Because analyzing financial information is clearly an inherently governmental function, the financial information collected by PCAs from taxpayers in the previous iteration of the PDC program was sent to a group of IRS employees (known as a “Referral Unit”) for further consideration. Now, however, the IRS will:

- Not require or even allow PCAs to request financial information from taxpayers;
- Allow PCAs, if they obtain IRS approval of proposed IAs in excess of five years, to monitor and receive commissions on payments taxpayers make pursuant to those “streamlined” IAs;⁷² and
- Allow PCAs to “restructure” IAs an unlimited number of times in the event of nonpayment.⁷³

In addition to concerns about the legality of these arrangements, I question whether they are good business decisions. An analysis of financial information may increase the number of successful IAs and reduce subsequent noncompliance. For example, taxpayers were more likely to maintain their IAs in good standing under TAS’s procedures, which require analysis of the taxpayer’s financial information, as compared

⁷⁰ Under the Federal Activities Inventory Reform Act of 1998 (FAIR Act), any activity that requires the “exercise of discretion in applying Federal Government authority” is “inherently governmental” and must be performed solely by Federal Government employees. Pub. L. No. 105-270, § 5(2)(B) 112 Stat. 2382, 2384-2385 (1998).

⁷¹ IRC § 6306(b)(1).

⁷² Streamlined IAs may be for up to six years in duration, are generally available for individual taxpayers when the total tax liability is \$50,000 or less, and do not require a financial statement. See IRM 13.1.4.2.3.9, *Installment Agreements* (Oct. 31, 2004); IRM 5.14.5.2, *Streamlined Installment Agreements* (Dec. 23, 2015). The IRS is currently conducting a pilot under which taxpayers with liabilities of more than \$50,000 and up to \$100,000 may enter into IAs of up to seven years without the need for a financial analysis. For details, see <https://www.irs.gov/businesses/small-businesses-self-employed/streamlined-processing-of-installment-agreements>.

⁷³ In contrast, IRM 5.14.11.5, *Considerations After Default or Termination, Including Reinstatement* (Jan. 1, 2015) provides for reinstatement of an IA without managerial approval or financial information only where, among other requirements, default was caused by an additional liability. Otherwise, “financial statement analysis is required to re-evaluate the taxpayer’s ability to pay.”

to taxpayers the IRS placed in IAs, where often no financial data is considered.⁷⁴ Additionally, the taxpayers TAS assisted were less likely to incur subsequent liabilities for two years after the IA was initiated.⁷⁵ These findings indicate the IRS's "streamlined" IA procedures place some taxpayers into IAs they cannot afford.⁷⁶ This problem will grow worse when PCAs, driven by the prospect of earning commissions, are allowed not only to place taxpayers into IAs, but also to "restructure" IAs, all without ever gathering financial information for the IRS to consider.

Unlike in the prior PDC initiative, the IRS has not designated a Referral Unit to act as liaison or intermediary between taxpayers and PCAs. The IRS will now assign and recall cases directly to PCAs by means of electronic data exchanges. There are no mechanisms to trigger IRS assistance in determining, for example, whether a taxpayer should be treated as unable to pay. This is especially troubling considering that, according to the IRS's own estimate, almost 80 percent of the debts to be outsourced belong to taxpayers with incomes at or below 250 percent of the federal poverty level.⁷⁷ TAS Research identified almost 380,000 taxpayers who, as of November 2016, had debts required to be assigned to PCAs.⁷⁸ Of these taxpayers, more than 273,000 (about 72 percent) filed a recent tax return.⁷⁹ The median reported income was about

⁷⁴ National Taxpayer Advocate 2016 Annual Report to Congress, vol. 2, at 53-66 (Research Study: *The Importance of Financial Analysis in Installment Agreements in Minimizing Defaults and Preventing Future Payment Noncompliance*).

⁷⁵ *Id.*

⁷⁶ National Taxpayer Advocate 2016 Annual Report to Congress 230-238 (Most Serious Problem: *The IRS Is Failing to Properly Evaluate Taxpayers' Living Expenses and Is Placing Taxpayers in IAs They Cannot Afford*).

⁷⁷ Letter from Nina Olson, National Taxpayer Advocate, to Sen. Ron Wyden, Chairman, Committee on Finance; Sen. Orrin G. Hatch, Ranking Member, Committee on Finance; Rep. Dave Camp, Chairman, Committee on Ways and Means; Rep. Sander Levin, Ranking Member, Committee on Ways and Means; Rep. Charles W. Boustany, Jr., Chairman, Subcommittee on Oversight, Committee on Ways and Means; Rep. John Lewis, Ranking Member, Subcommittee on Oversight, Committee on Ways and Means 8 (May 13, 2014). The letter states that in analyzing the proposed legislation, the IRS prepared a preliminary estimate of the percentage of individual taxpayers with incomes at or below 250 percent of the federal poverty level whose delinquent accounts seemingly fell within the definition of statutory term "inactive tax receivables." After analyzing collection data for FY 2013, the IRS concluded that 79 percent of the cases that fall into the "inactive tax receivables" category involve taxpayers with incomes below the threshold.

⁷⁸ There were 379,576 such taxpayers. IRS Accounts Receivable Dollar Inventory (ARDI), Compliance Data Warehouse (CDW) (data accessed Nov. 28, 2016).

⁷⁹ IRS, ARDI, Individual Returns Transaction File (IRTF), Information Returns Master File (IRMF), CDW (data accessed Nov. 28, 2016) (showing there were 273,105 such taxpayers). Recent returns include those for TY 2014 or later. Not all taxpayers whose debts are required to be assigned to PCAs had a 2015 filing requirement. See, e.g., IRC § 1; IRS Publication 501, *Exemptions, Standard Deduction, and Filing Information 2* (2015). For example, a single person under age 65 at the end of 2015 was not required to file a 2015 return unless his or her gross income was \$10,300 or more.

\$32,000,⁸⁰ and more than one-third of the returns reported incomes of less than \$20,000.⁸¹

Accordingly, I recommend that the IRS:

- In assigning debts to PCAs, identify taxpayers who have incomes at or below 250 percent of the federal poverty level;
- Require PCAs to gather financial information from these taxpayers;⁸² and
- Where this information indicates the taxpayer cannot pay within five years, require the PCAs to refer the case back to a newly created IRS referral unit for analysis and resolution.

VII. Charging User Fees for Services that Help Taxpayers Comply Could Be Very Costly to Taxpayers and Reduce Revenue Collection

Most services the IRS offers to assist taxpayers in paying their tax liabilities are provided without charge. However, the IRS has determined that some services provide a “special benefit” that justifies, or requires, the payment of a “user fee.” For example, a financially struggling taxpayer who cannot pay his tax bill in full when it is due but is doing his best to be compliant may enter into an IA to pay the liability, plus interest charges, over a period of years. This should be encouraged because it will keep the taxpayer in compliance and save the agency the costs of taking expensive enforced collection action. Yet the IRS currently charges taxpayers a fee for this “special benefit” and it has proposed to increase the fee to up to \$225.

Indeed, the IRS recently increased, or proposed to increase, the fees for IAs,⁸³ offers-in-compromise (OICs),⁸⁴ pre-filing agreements (PFAs),⁸⁵ and private letter rulings

⁸⁰ IRS ARDI, IRTF, CDW, data accessed Nov. 28, 2016, showing that median income reported on these returns was \$31,842.

⁸¹ *Id.*, showing that 38 percent of these returns reported income of less than \$20,000.

⁸² Under the current PCA contracts, the PCAs are compensated only by commissions computed as a percentage of funds they collect. If PCAs begin to collect financial information that they pass along to the IRS for IRS action, they should be compensated with flat fees for their work on those cases.

⁸³ *User Fees for Installment Agreements (IAs)*, T.D. 9798, 81 Fed. Reg. 86955 (Dec. 2, 2016), <https://www.regulations.gov/document?D=IRS-2016-0036-0007> (increasing the IA fee from \$120 to \$225).

⁸⁴ *User Fees for Offers in Compromise (OICs)*, Notice of Proposed Rulemaking (NPRM), 81 Fed. Reg. 70654 (Oct. 13, 2016) (proposing to increase the OIC fee from \$186 to \$300). For the National Taxpayer Advocate’s comments, see National Taxpayer Advocate Memo to Associate Chief Counsel (Procedure and Administration), *Comments on User Fees for Offers in Compromise* (Nov. 28, 2016), <https://www.regulations.gov/document?D=IRS-2016-0038-0003>.

(PLRs).⁸⁶ The Independent Offices Appropriation Act of 1952 generally requires federal agencies to establish user fees at “full cost” for services that convey “special benefits,” unless the Office of Management and Budget (OMB) grants a waiver.⁸⁷

Unlike most federal agencies, however, the IRS has an extra incentive to raise fees because it may retain and spend certain user fee revenue.⁸⁸ It also has more flexibility in how it spends user fees than in how it spends its appropriation. While the IRS submits its user fee spending plan to Treasury and OMB for approval, it does not need congressional approval.⁸⁹ Not surprisingly, in 2016 the IRS proposed increasing the fees for IAs and OICs because of “constraints on IRS resources.”⁹⁰

It is illogical and counterproductive to charge increased user fees to taxpayers who don’t have enough funds to pay their tax liabilities. Unlike services provided by other agencies, fundamental tax services generate tax revenue or reduce enforcement costs because they promote voluntary tax compliance. When the IRS charges user fees to taxpayers who can’t even pay their taxes, it deters some taxpayers from voluntarily entering into IAs. And when fees deter taxpayers in this way, total revenue collection may actually be lower.⁹¹

In addition, IA and OIC applicants are not “special beneficiaries” in the sense that they are in a specific industry or are getting a service that is unavailable to others. Rather, any taxpayer, at any point in time, might need an OIC or an IA to pay his or her taxes, whether because of a business downturn, the death of a spouse, or a medical condition. Do we really want a system where only those who are willing and able to pay a fee can

⁸⁵ Rev. Proc. 2016-30, § 10, 2016-21 I.R.B. 981, 987 (increasing the PFA fee from \$50,000 for requests before June 3, 2016 to \$218,600 for requests after January 1, 2017).

⁸⁶ Rev. Proc. 2015-1, App’x A(3), 2015-1 I.R.B. 1, 79 (2015) (increasing the general PLR fee from \$19,000 to \$28,300). Previously, the fee for PLRs involving exempt organizations was \$10,000. Rev. Proc. 2014-8, § 6.08, 2014-1 I.R.B. 242, 247 (2014).

⁸⁷ 31 U.S.C. § 9701; OMB Circular A-25.

⁸⁸ Compare 31 U.S.C. § 3302(b) (requiring agencies to return user fee receipts to the Treasury) with Pub. L. No. 103-329, § 3, 108 Stat. 2382 (1994) (allowing the IRS to retain certain user fee receipts) and Pub. L. No. 109-115, § 209, 119 Stat. 2396, 2439 (2006) (same).

⁸⁹ GAO, GAO-17-492T, *2016 Filing Season* 4 n.7 (Mar. 8, 2016), <http://www.gao.gov/assets/690/683246.pdf>. Congress increased the IRS’s appropriation for taxpayer services from FY 2013 to FY 2016. TIGTA, Ref. No. 2017-40-013, *Analysis of Resources Allocated to Taxpayer Services* 5 (Dec. 2017), <https://www.treasury.gov/tigta/auditreports/2017reports/201740013fr.pdf>. In FY 2015, however, the IRS diverted fee revenue from taxpayer service to operations support, primarily to implement various legislative mandates. *Id.*

⁹⁰ See, e.g., *User Fees for IAs*, 81 Fed. Reg. 56543, 56544 (Aug. 22, 2016); *User Fees for OICs*, 81 Fed. Reg. 70654, 70655 (Oct. 13, 2016).

⁹¹ When the IRS first imposed a \$150 OIC user fee, OIC submissions declined even among those who were exempt from the fee. See TIGTA, Ref. No. 2005-30-096, *The Implementation of the Offer in Compromise Application Fee Reduced the Volume of Offers Filed by Taxpayers at All Income Levels* (June 2005).

get an IA or OIC to pay their taxes? Finally, there is no principled distinction between the services subject to a fee and those that are free, such as entering into a closing agreement, visiting a taxpayer assistance center, calling the IRS, receiving a communication (e.g., a call, letter, or notice), making a payment, submitting a tax form, or using the “where’s my refund” website.

I believe the best approach is for Congress to decide what kind of tax administrator it wants. If it wants a proactive administrator that provides services to help taxpayers comply before resorting to enforcement, then it should provide the IRS with the funds to provide that assistance and limit the IRS’s ability to charge user fees, at least for IAs and OICs. Encouraging the IRS to impose fees on IRS services that help taxpayers comply will discourage taxpayers from being proactive in paying their taxes.

Accordingly, I recommend that Congress:

- Provide the IRS with funding to offer fundamental taxpayer services for free;
- Consider reducing the incentive for the IRS to charge for them;⁹² and
- Require the IRS to weigh the costs against the benefits of any proposed fee increase – including the effect of the proposed increase on voluntary compliance, enforcement costs, and taxpayer rights – and to consider public comments on its analysis before raising any fee.

VIII. The IRS Requires 21st Century Information Technology (IT) Systems to Carry Out 21st Century Tax Administration

The IRS’s IT systems, and particularly its case management systems, require a significant investment of funding to promote efficiency gains and improve taxpayer service. An adequately funded, staffed, and skilled IRS IT function underpins all core tax administration activities, including taxpayer service, prompt issuance of refunds, selection and assignment of compliance work, and protection of taxpayers and the public from refund fraud and identity theft. The current state of IRS technology substantially limits the IRS’s ability to carry out effective tax administration. The IRS currently possesses the two oldest information system databases, each nearly six decades old, in the entire federal government.⁹³

⁹² Section 504 of S. 3471 would generally prohibit further increases of the installment agreement fee and waive the fee for certain low-income taxpayers. H.R. 4885 would limit the IRS’s authority to spend user fee revenue without authorization from Congress.

⁹³ See GAO, GAO-16-468, *Information Technology: Federal Agencies Need to Address Aging Legacy Systems* (May 2016) (discussing aging IT systems throughout the government and listing the IRS’s Individual Master File (IMF) and Business Master File (BMF) as the two oldest investments or systems at 56 years old each).

The IRS has identified 63 separate case management systems to include in its enterprise case management (ECM) project. The age, number, and lack of integration across these systems, as well as the lack of digital communication and record keeping, cause waste and delay, and make it difficult for IRS employees, including those in TAS, to perform their jobs efficiently and provide quality service to taxpayers. This causes frustration for taxpayers and IRS employees alike.

The IRS's current case management system structure requires employees to retrieve data from many systems manually, which requires maintaining both paper and electronic records. Employees transcribe or otherwise import information from paper and other systems into their own case management systems, and ship, mail, or fax an estimated hundreds of thousands, if not millions, of case management files and supporting documents annually within or between business functions for activities such as case work, management approval, quality review, and responses to Appeals and Counsel.

To ameliorate these problems, ECM requires a significant investment of both time and money to promote productivity and efficiency gains, and to improve taxpayer service. Indeed, success of the ECM project is critical to establish online accounts to effectively serve taxpayers and their representatives. I am encouraged by the IRS's most recent approach to ECM, including the addition of new leadership and search for the appropriate ECM platform, but I am frustrated that the process has been so drawn out.

In addition, I have recently learned the IRS does not plan to complete the Taxpayer Advocate Service Integrated System (TASIS), which was halted in March 2014 after \$20 million was spent on it. TASIS was a versatile case management system that would have replaced the Taxpayer Advocate Management Information System (TAMIS), TAS's current antiquated system from the 1980s. Since 2013, Congress had identified TASIS as a major IT system and required quarterly IRS reporting on it.⁹⁴ While I understand and appreciate the IRS's reason for not moving forward with TASIS as it is seeking an ECM solution and platform that will work across the IRS, I am concerned that the time, effort, and \$20 million spent in developing TASIS not go to waste. As I discussed in my Annual Report last year, TAS worked over several years to develop the business requirements for TASIS, and ultimately developed more than 4,500 such requirements.⁹⁵ It is critical that the extensive business requirements development and process design work that went into TASIS not be for naught and that the IRS leverage it as it endeavors to find an ECM solution. The IRS can also use the

⁹⁴ The Senate Appropriations Subcommittee on Financial Services and General Government has repeatedly included TASIS on a list of six "major information technology project activities" about which it has directed the IRS to submit quarterly reports. See S. Rep. No. 114-280, at 40 (2016); S. Rep. No. 114-97, at 39 (2015); S. Rep. No. 113-80, at 34 (2013). In 2014, a similar provision was included in the Senate Appropriations Committee's draft report, but the draft report was not adopted for that year.

⁹⁵ See National Taxpayer Advocate 2016 Annual Report to Congress 117 (Most Serious Problem: *Enterprise Case Management (ECM): The IRS's ECM Project Lacks Strategic Planning and Has Overlooked the Largely Completed Taxpayer Advocate Service Integrated System (TASIS) As a Quick Deliverable and Building Block for the Larger ECM Project*).

lessons learned from the development of TASIS in its current ECM effort to reimagine its business processes and make them more efficient and user friendly, thereby enabling it to thrive technologically in the 21st century.

TAS is committed to working with the IRS to develop an ECM solution and is willing to assist with the testing of new products as the IRS designs and programs the new ECM system. For example, the IRS may wish to test a solution to electronically submit and track Operations Assistance Requests (OARs),⁹⁶ which would benefit taxpayers, TAS, and the IRS by reducing delays in case resolution. It would also produce resource savings by eliminating many of the current costs, including shipping, time spent by employees manually inputting and tracking OARs, and time spent physically printing and scanning OARs into other IRS tracking systems.

It is also vitally important that the IRS take steps to address its aging legacy systems while it develops an ECM system, which could take several years. In the meantime, the IRS requires funding, which I recommend that Congress provide, to maintain its current aging case management systems, many of which desperately need upgrading to provide effective tax administration and quality service to taxpayers. For example, TAS's antiquated TAMIS case management system requires upgrades to allow TAS's case advocates to effectively do their jobs and assist taxpayers.

Although the IRS requires substantially more funding for IT in general and ECM specifically, it must articulate a clear strategy that will assure both Congress and taxpayers that this money will be spent appropriately. I encourage Congress to monitor the IRS's IT spending closely and not simply hand the IRS a blank check.

Accordingly, I recommend that Congress:

- Provide the IRS with additional IT funding to develop an effective enterprise case management system once the IRS has developed and presented a detailed ECM plan.
- Direct the IRS to work with TAS to make use of the design elements previously developed for TAS's TASIS system and include TAS in any pilots of ECM products.
- Provide the IRS with adequate funding to maintain its current IT systems while it develops an ECM system.

⁹⁶ An OAR is the form that TAS uses to request the IRS to take action on a case when TAS lacks the statutory or delegated authority to perform the action.

IX. Conclusion

The IRS faces major challenges in meeting the service needs of taxpayers. Some of these challenges are due to limited resources and others are a result of the way the IRS chooses to allocate the resources it currently has. Several incidents over the last few years have reduced the confidence of many Members of Congress in the leadership of the IRS. Largely as a result of that reduced confidence, Congress has cut the IRS budget to the point where the agency is now struggling to meet basic taxpayer needs.

The failure to adequately fund the IRS harms U.S. taxpayers, not the IRS. It means taxpayers do not receive the service, education, and assistance they need to comply with their tax obligations, and it means that those who want to game the laws and evade their tax obligations will find it easier to do so.

We cannot continue with the current state of affairs. To break the cycle of distrust, the IRS must show Congress that it can wisely and appropriately spend funds and allocate resources. In turn, it is imperative that Congress continue to hold oversight hearings on tax administration to understand how the IRS is spending its appropriations and gain greater confidence in the IRS. These steps will enable Congress and the IRS to work together to ensure that the IRS can be a service first organization going forward.