

NOMINATION OF DOUGLAS H. SHULMAN

HEARING

BEFORE THE

**COMMITTEE ON FINANCE
UNITED STATES SENATE**

ONE HUNDRED TENTH CONGRESS

SECOND SESSION

ON THE

NOMINATION OF

DOUGLAS H. SHULMAN, TO BE COMMISSIONER,
INTERNAL REVENUE SERVICE

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JANUARY 29, 2008
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CONTENTS

OPENING STATEMENT

	Page
Baucus, Hon. Max, a U.S. Senator from Montana, chairman, Committee on Finance	1

ADMINISTRATION WITNESS

Shulman, Douglas H., nominated to be Commissioner, Internal Revenue Service, Washington, DC	3
---------------------------------------------------------------------------------------------------	---

ALPHABETICAL LISTING AND APPENDIX MATERIAL

Baucus, Hon. Max:	
Opening statement	1
Grassley, Hon. Chuck:	
Prepared statement	25
Salazar, Hon. Ken:	
Prepared statement	26
Shulman, Douglas H.:	
Testimony	3
Prepared statement	28
Biographical information	30
Responses to questions from committee members	37
Responses to follow-up questions from Senator Grassley	132

**NOMINATION OF DOUGLAS H. SHULMAN
TO BE COMMISSIONER OF THE
INTERNAL REVENUE SERVICE**

TUESDAY, JANUARY 29, 2008

U.S. SENATE,
COMMITTEE ON FINANCE,
Washington, DC.

The hearing was convened, pursuant to notice, at 10:05 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Max Baucus (chairman of the committee) presiding.

Present: Senators Wyden, Schumer, Salazar, Grassley, Hatch, Smith, and Sununu.

**OPENING STATEMENT OF HON. MAX BAUCUS, A U.S. SENATOR
FROM MONTANA, CHAIRMAN, COMMITTEE ON FINANCE**

The CHAIRMAN. The hearing will come to order.

Thomas Jefferson once said, "Taxation is the most difficult function of government." Today we consider the nomination of Doug Shulman to carry out that job. In that job he will face many difficulties, but each difficulty is also an opportunity.

Let me tick off a few of the difficulties awaiting him: the tax gap, improving customer service at IRS, IRS's outdated computers, the challenges in the global economy, an aging IRS workforce, fundamental tax reform, and implementing stimulus this year.

Mr. Shulman, you have your work cut out for you. Good luck! It is almost as if you have added new meaning to the term "masochism" in wanting this job. [Laughter.]

First, the tax gap. That is the difference between the taxes legally owed and the taxes paid on time. It is estimated to be at least \$345 billion each year. IRS Commissioner Charles Rossotti called this the "free rider tax." That is because those who do not comply with our Nation's tax laws ride on the backs of those who do. IRS's Taxpayer Advocate says that the tax gap amounts to \$2,600 in additional burden for each honest American taxpayer.

Last year, I insisted that Treasury and IRS develop a comprehensive and credible plan to reduce the gap, a plan with baselines, timelines, and measures. They delivered the plan in August, and I intend to hold Mr. Shulman accountable for implementing the plan and regularly keeping me apprised of his progress.

Second, to customer service. Providing top-notch customer service must be a priority for the IRS. Many of our tax laws are complex and difficult to understand. I call on Mr. Shulman to follow

through on the IRS's taxpayer assistance blueprint. He needs to ensure that taxpayers receive the service they deserve.

I might say at this point, Mr. Shulman, IRS has made that taxpayer assistance blueprint, and the plan is waiting for you to oversee it and implement it. I might say, though, the IRS has conducted lots of plans and often does not follow through, partly because of staff turnover, turnover at the top. There is just not follow-through. That has to change. There has to be follow-through, even when people change. The plans themselves have to be followed through.

Third, IRS computers. Mr. Shulman will be faced with the major overhaul of IRS's information technology. The IRS still uses computer systems built in the 1960s. I cannot, for the life of me, believe that here in the United States of America the IRS still uses those little tapes and does not have the more up-to-date drives, with CDs, or the new technology, but still has the old tapes. Most countries do not. Most companies do not have the old, outdated system. We still have the old, outdated system.

What does that mean? It means that various systems cannot talk to each other. For example, a person's unemployment, a 944 form, cannot be matched with whether or not he or she paid income taxes. They cannot talk to each other. That is just one example where they cannot talk to each other. It is an outrage, frankly. An absolute outrage. Mr. Shulman, that is something that you have to change.

Information technology is more than outdated, it is in the Dark Ages. This limits the Agency's ability to process information or detect scams. Taxpayers who are accustomed to doing all their business online should be able to meet their tax obligations electronically without additional costs.

Fourth, an increasingly global economy affects our Nation's tax system. The IRS needs to keep pace with multinational corporations, sophisticated financial products, and offshore tax schemes.

Fifth, the IRS workforce is aging. Skilled public servants who have dedicated their professional careers to tax administration are retiring in increasing numbers. Mr. Shulman needs to act aggressively to retain skilled technicians and hire high-quality workers to replace those who retire.

Sixth, tax reform. This year I intend to hold a series of hearings to explore options for fundamental tax reform. As Congress works on changes to our tax laws, I expect Mr. Shulman's commitment to help us formulate changes and actively implement those changes. I would like your assistance, Mr. Shulman, again on designing changes, and also your assistance in implementing those changes.

Seventh, Congress will be enacting the stimulus package soon. The IRS review of the 2001 rebate program found that this success was due in large part to the commitment of the Commissioner to ensure that the Agency devoted adequate resources to the rebate program. I expect Mr. Shulman to provide his full support to successfully administering a stimulus payment program that will boost our Nation's economy.

These are just some of the difficulties that you face. As I said, they are also opportunities. Let me just highlight both of those

points: huge difficulties and huge opportunities. You have, basically, the opportunity, Mr. Shulman, to turn this around, finally. It is going to take a lot, a lot of work, but you will have the cooperation of this committee because, clearly, that is in the best interests of the country.

Let me now turn to our witness, Mr. Shulman. Before we go any further, do you have any family you would like to introduce?

Mr. SHULMAN. Yes, I do, Mr. Chairman. My wife, Susan, is here with me, as well as my son, Ben, and my daughter, Eve. They are 4 years old, so they may not stay for the whole hearing.

The CHAIRMAN. Would you all stand up, please, so we can recognize all of you? This is a joint, team, family effort here. That is great. Thank you very much.

[Applause.]

The CHAIRMAN. Thank you. I know you are all very proud of Doug, and I hope you see him more—I hope you see him. [Laughter.]

Mr. Shulman, we have three questions we customarily ask of all of our nominees, and I will ask of you right now. Is there anything that you are aware of in your background that might present a conflict of interest with the duties of the office to which you have been nominated?

Mr. SHULMAN. No.

The CHAIRMAN. Do you know of any reason, personal or otherwise, that would in any way prevent you from fully and honorably discharging the responsibilities of the office to which you have been nominated?

Mr. SHULMAN. No.

The CHAIRMAN. And do you agree, without reservation, to respond to any reasonable summons to appear and testify before any duly constituted committee of Congress, if you are confirmed?

Mr. SHULMAN. Yes.

The CHAIRMAN. Good. I might say, too, besides oral questions that we in the committee might ask you, members of the committee might provide you with written questions. In order to expedite the committee's consideration of your nomination, we ask that you respond to these written questions as soon as possible.

We also recognize our newest member of the committee who is here. You are giving us a very good—how can I say this? It is a good precedent for our new member to be here attending our committee hearings. It is a good example for other members of the committee to follow. So I recognize our newest member, Senator Sununu from New Hampshire. Welcome, Senator, in joining our committee.

Senator SUNUNU. Thank you.

The CHAIRMAN. Mr. Shulman, why don't you proceed?

STATEMENT OF DOUGLAS H. SHULMAN, NOMINATED TO BE COMMISSIONER, INTERNAL REVENUE SERVICE, WASHINGTON, DC

Mr. SHULMAN. Thank you, Mr. Chairman, members of the committee. My name is Doug Shulman. I am currently vice chairman of the Financial Industry Regulatory Authority. It is truly an honor

to be here today as you consider my nomination to be Commissioner of the Internal Revenue Service.

Mr. Chairman, the importance of the Internal Revenue Service cannot be over-estimated. How the IRS approaches its work and interacts with taxpayers greatly affects both the functioning of the Federal Government, as well as Americans' overall view of their government. The IRS touches every adult, every business, and every nonprofit organization in America. For many citizens, it is the only Federal agency with which they will have contact in a given year.

Never has thoughtful leadership and direction at the IRS been more critical as the Federal Government's responsibilities to its citizens have grown. As you know, the IRS collects the vast majority of the revenue needed to run the government, from protecting the environment, to defending the homeland, to improving educational opportunities, to increasing access to health care services. It is truly an awesome responsibility to lead such an agency. Because I recognize the enormous challenge, if I am confirmed, I have given a lot of thought as to how I would approach the job.

Since I have been nominated, many people have asked me if I would emphasize service or enforcement. I actually believe this is a false choice. In order to execute its mission, the IRS must do both. For taxpayers who pay their taxes willingly and on time, which is the great majority of Americans, there must be clear guidance, accessible education, and outstanding service. Our aim should be to make it as easy as possible for them to pay the correct amount of taxes in the most efficient and least burdensome manner possible.

For taxpayers who intentionally evade paying their taxes, there must be rigorous enforcement programs. But whether servicing taxpayers or enforcing the law, it is absolutely essential that Americans believe the IRS is fair and that it respects the rights of all taxpayers.

Thanks to Commissioners Rossotti and Everson, there are important initiatives currently in place that, if confirmed, I would anticipate continuing. But I would also bring a fresh set of eyes to the position and ensure that the Agency continues to evolve as circumstances change.

Any effort to improve service must include a commitment to IRS modernization. IRS employees must have timely access to taxpayer data so assistance is quick and accurate. This will require focusing on, and investing in, IRS processes as well as IRS's information technology. This would be a priority for me, if confirmed.

The IRS must also continue its rigorous enforcement programs. It must deter those who may be inclined to evade their legal tax obligations and pursue those who engage in evasion. As members of this committee already know, in recent years a number of significant steps have been taken to shut down tax shelters and other abusive transactions that were created for no other reason than to avoid taxation. I support these efforts, and I would anticipate continuing them.

I also believe that it is essential for the IRS to work closely with the practitioner community, including lawyers, accountants, and tax preparers who are all a vital part of our Nation's tax compli-

ance system. The IRS must use all of the tools at its disposal—dialogue, education, service, and enforcement—to ensure that these important members of the tax community are partners in our efforts to see that all individuals and institutions meet their tax obligations.

Finally, if confirmed, I plan to focus on leadership and employee development during my tenure as Commissioner. I have been extremely impressed by the leadership and the dedicated and talented workforce of the IRS. However, as you mentioned, Mr. Chairman, like other Federal agencies, many experienced and knowledgeable IRS employees will be approaching retirement eligibility in the coming years. It is critical that the next Commissioner devote significant attention to recruiting, training, and grooming the next generation of IRS leaders.

Mr. Chairman, it is an honor to have been nominated by the President to be the next Commissioner of the IRS. I recognize that, if confirmed, it will be a very demanding and difficult job, which I see as an opportunity. As Commissioner, I would do everything in my power to ensure that the Nation's tax laws are administered in a fair and efficient manner. Essential to my success would be a close partnership with members of Congress on both sides of the aisle, and you have my commitment to work closely with this committee.

Thank you for letting me make these brief opening statements, and I am happy to respond to your questions.

The CHAIRMAN. Thank you, Mr. Shulman.

[The prepared statement of Mr. Shulman appears in the appendix.]

The CHAIRMAN. I would like your thoughts on implementing the stimulus rebate program that clearly is going to pass the Congress and be signed by the President in the next couple of weeks, at least. As you well know, the GAO analysis of the 2001 rebate program found "one of the primary reasons the program worked well was because the IRS Commissioner made it a top priority and communicated that to IRS leadership and rank-and-file employees." Your thoughts on how well you can administer sending out the stimulus rebate checks.

Mr. SHULMAN. It is an important question. I can assure you, Mr. Chairman, that it will have my full attention, if I am confirmed. I think, a few observations. One, we are in the middle of filing season. Refunds are going out, which is an important part of the overall tax administration process.

I am obviously not privy to the inner discussions, given that I am currently a private citizen. But you have my assurance that, if I am confirmed, I recognize the importance of this to the entire government, and I would do everything in my power to ensure that checks went out as quickly as possible.

The CHAIRMAN. It is also even more important to the people we work for, the public.

Mr. SHULMAN. Absolutely.

The CHAIRMAN. They are our employers. We are just the hired hands. We are just the employees here. We are just making sure that our employers get what they expect, and that is very efficient distribution of rebate checks.

The second, the tax gap issue. As you well know, I have spent a lot of time on this. In fact, I held up an Assistant Secretary's nomination until we got a plan from the Treasury and IRS on how to solve the tax gap problems. I would like to have 90-percent compliance by the year 2017, and I am curious as to the degree to which you think we can accomplish that. Right now, I think it is 83-percent compliance. I would like your commitment that we get up to 90-percent compliance.

Mr. SHULMAN. We have had the opportunity to talk about the tax gap. I agree with you 100 percent that this large a number of taxes that are uncollected is a problem. I think it is a problem on its face for the Treasury. I think it also has the potential, as you mentioned before, to undermine the system where there is a large percent of the population paying their full share of taxes and there is a percentage of the population that is not. So, you have my absolute commitment to work with you on it.

I have looked at the report closely and have followed your statements and analysis of it, Mr. Chairman. I think it is clear there are two causes. There are the unintentional causes and unintentional mistakes, and I think there service—telephone, in-person, technology, and the website—needs to continue to be improved so that people understand their obligations and meet their obligations. Then there are clearly the intentional issues. As we have had a chance to talk about, it seems like one of the keys to the tax gap is third-party reporting.

All of the statistics that I have seen show that when there is third-party reporting, compliance rates are very high. When there is not third-party reporting and the IRS has to go in with more burdensome-type audits and does not have a way of verifying, compliance rates are lower. I think that is a discussion that I will look forward to having with the committee about exactly what to do about that, and look forward to working in close partnership.

Regarding the percentage, we had a little chance to talk about this. I do not know enough about all the levers now to know exactly where I think we can get with compliance, but I am 100-percent committed to working with you to increase compliance and help to close that gap.

The CHAIRMAN. I think we can get to 90 percent, frankly. I am going to stick with this issue. So, virtually every time you come back before this committee, you can expect a question from me as to how far along are we in closing that gap. I am going to keep asking that question and expect you to show progress—significant progress—every time I ask that.

One final question before I turn to other Senators. I am quite concerned about the development of very complex financial products and the degree to which IRS is able to understand them and know how our tax code fits in with them, that is, the degree to which there is any taxable income in exchange of those products, or in some way involve those products, whether they are SIVs, CDOs, or whatever they may be.

Let me put it this way. I am told by 1991 there was about \$10 trillion in American bank deposits; now there is about \$10 trillion in American bank deposits. There was \$20 trillion developed over that period of time in complex financial products; \$43 trillion in

credit default swaps. Who knows what they are? Who knows? Banks do not know the value of them, frankly. So my question to you, and my time has expired, is what will you do at the IRS to keep abreast of these products, and in your role as Commissioner, in what to do about them?

Mr. SHULMAN. That is a great question. As you know, Mr. Chairman, in my current role as vice chairman of the Financial Industry Regulatory Authority, we have regulatory responsibility to oversee brokerage firms that do business with the public. I have had the opportunity to track these issues. I think the financial industry is innovating really at an exponential pace.

I think keeping track of these products is a challenge, frankly, for financial service regulators, and I think it is going to be an important challenge for the IRS to be up to. Some of the things that I did in the past, I tried to bring people in from those industries to work inside the Financial Industry Regulatory Authority, people who had spent time on trading desks, had done product development with those kinds of products, so we had people who really understood the thinking that went on.

I think making sure people at the IRS, and in my case now the Financial Industry Regulatory Authority, actually went out to desks and went to those financial institutions and made sure they were in dialogue and understood not just what products are on the shelf, but what products are in development, and really having a focused group, would be my instinct.

The CHAIRMAN. I appreciate that. My time has expired. But I expect you, as Commissioner, to be fully aware of and abreast of all of these developments and understand them in your role as Commissioner.

Senator Grassley, I might ask if you have an opening statement that you may want to make.

Senator GRASSLEY. Yes, but I am just going to put that in the record.

The CHAIRMAN. All right. Thank you.

[The prepared statement of Senator Grassley appears in the appendix.]

Senator GRASSLEY. I want to follow on, but on a very narrow part of the tax gap and how the Private Debt Collection Program might work in with it. We have the Taxpayers Advocate report that gross accounts receivable increased by 5 percent for 2006. Then I want to give you a quote: "The number of taxpayers with unpaid accounts in the inventory of unassigned collection cases—or queue as it is called—and the amount owed on these accounts increased to 10-year highs."

The IRS, before last year's political attack on the program, established a realistic range for collections of these accumulated debts to the government of somewhere between \$88 million to \$124 million, a rather modest sum considering that the IRS currently has over \$110 billion of very collectable receivables eligible for this program.

So I am going to ask a few questions, but they all come around to this. What role do you see the Private Debt Collection Program playing in the efforts to close the tax gap? Given that this program is estimated to collect more than \$1 billion over 10 years that oth-

erwise would not be collected, how do you plan to utilize and expand this cost-effective program to further reduce the tax gap?

Then I am asking for a commitment to the full implementation of the program as set out by IRS executives in December, 2006. I ask, with the understanding that these goals are relatively modest—I am going to stop there with those questions I have just asked you.

Mr. SHULMAN. Yes. Thank you, Senator, for the question. This is an important issue that I know has gotten quite a bit of attention, both at the IRS and here on Capitol Hill.

Let me just say, if I step back just a little bit—if you will permit me—that I think the job of the Commissioner to do an overall resource allocation for the Service is one of the important jobs. To make sure there are the right people, the right technology, the right funding, the appropriate use of contractors, whether it be in the technology arena or in an arena like this. I also would say I think there is quite a large number of very talented and able IRS workers who do a lot of this work.

I have some guiding principles around any program, including this one, for the IRS. One would be to ensure that taxpayer rights are respected. Two would be that taxpayer privacy and the privacy of their data is safeguarded and adhered to. Three is that there are proper oversight and safeguards for any program.

My understanding of this private debt collection program is that these are cases that otherwise would not be worked by the IRS, and that Congress has actually authorized—there has been quite a bit of debate, and Congress has authorized it. I have been assured by the team at the IRS, after we had a chance to talk, that they are actually pursuing this program aggressively. As long as it is authorized and Congress has debated it and made the decision to move forward, I would anticipate this, like every other program, running well and running in the spirit of doing the best we can.

Senator GRASSLEY. I have trouble reconciling what I am hearing from the IRS versus what I am hearing from the Treasury Department. I hear from the IRS that more employees are needed to enforce the tax code, while I hear from the Treasury Department that the amount of time devoted by IRS employees to work for their union is greater than the average of the entire Federal Government. How do you reconcile these observations, and how will you ensure that those who work for the IRS actually do work for the IRS before asking for more funding for staff?

Mr. SHULMAN. Yes. It is a great question. I think, clearly, I am going to have to, if confirmed, get my hands around the number of employees, the budget, the resource allocation. It is clearly something that I will go and try to get a handle on and come back.

What I will tell you is, my belief is, as Commissioner, my job would be to be the leader of every single person at the IRS: union, non-union, management, rank and file. I would do everything I could to ensure people are treated with dignity, that they are motivated to do their job, that they are focused on getting the job done, that they feel accountable to the American taxpayer to do a good job.

Senator GRASSLEY. The expensive problem the IRS has had in modernizing its computer system is well known. It is a great source

of frustration for me. In fact, as far back as 10 years ago—and you will remember this very well—the fact that the IRS used many separate computer systems that did not communicate with each other was recognized as a serious problem, and it still remains a serious problem. So as new Commissioner, what is your plan to succeed where others have not truly succeeded, and then modernize the computer system used by the IRS?

Mr. SHULMAN. It is an incredibly important question for the IRS, how to really move forward with modernization. I think that modernization is actually essential to meeting service goals, meeting enforcement goals, and meeting workforce productivity goals. My experience, where I oversee large technology operations for a Wall Street regulator, is that a lot of technology projects fall down when the right requirements are not developed and everyone has not agreed on exactly what we are trying to get done.

So the first thing I would do is go in and make sure that everyone, from the contractors working on it, to the leadership, all have the same goal. I think the goal is real-time access to taxpayer information by the people providing service and enforcement so that when a taxpayer calls they see an accurate record. That record can be updated so that when someone is going out to do an IRS audit, they actually have the same information. So being crystal clear and focused on the goal is the first thing that I will ensure.

The second thing is to make sure there is the right accountability in structure and governance. A lot of times the technologists get sent off into a hole to develop something and it comes out and it is not necessarily what the entire workforce needs. So, making sure that there is true joint accountability between the people using the system and the technology folks who build the system.

Finally, it is making sure there are the right resources, both the talented people, the people who understand what they are doing in all aspects of development, and that the funding is there. So, this will get my full attention.

The CHAIRMAN. Thank you.

Senator Wyden, you are next.

Senator WYDEN. Thank you, Mr. Chairman.

Mr. Shulman, in December the Bush administration criticized the Congress, saying that even a few days of Congressional debate on a temporary fix for the Alternative Minimum Tax would make it tough for the IRS to print and mail the new forms. Now the administration says it can send rebate checks to 113 million households within 60 days—in effect making this claim just a few weeks after the Congress was criticized for overwhelming the IRS with a much simpler challenge relating to updating the AMT forms.

My question to you is, it is obvious that the IRS is being put right in the center of the political debates in this country. What do you intend to do to make sure that the IRS, on your watch, is not used as a political tool?

Mr. SHULMAN. That is a great question. I believe that it is incredibly important that the IRS is seen as fair, is seen as non-political and nonpartisan, and that it really is a public service organization. I would be a public servant, serving all American taxpayers, and really the government.

I think specifically the issues you mentioned, and the Chairman asked before about, the stimulus package and the rebate checks, you have my assurance that I would approach the job as a non-political position, trying to follow and implement the policies that were set forth by the Congress, and would do everything under my power to do it. I think what I could do as Commissioner is send a clear signal that that is the job of the IRS, to actually implement what the policymakers decide.

Senator WYDEN. Let me ask you a couple of questions again about the process relating to this stimulus package and how it is going to be implemented. We had the CBO Director, Director Orszag, before us who talked about the difficulties in getting the checks out. His concern was that the checks' stimulus benefits really would not arrive until the second half of the year.

We have been informed about the various challenges involving hiring extra workers to reprogram the computers, entering new data, answering calls; the list goes on and on. I am going to do my best to advance tax reform. I think we ought to be going back to what Ronald Reagan and Bill Bradley talked about, about broadening the base and making the code simpler.

Is part of what we are seeing in this discussion about the stimulus package not a reflection on the fact that the biggest challenges for our country, such as right now getting this stimulus package implemented quickly, a lot of those challenges would be easier if the tax code were simpler. Is that not correct?

Mr. SHULMAN. Clearly the IRS, the programming, getting the forms out, et cetera, is exacerbated by a complex tax code. Clearly, tax administration would be easier in this country with a simpler tax code.

On the stimulus package, I am not close enough, really to—I mean, I know what I read in the papers. I am not privy to the conversations. What I will say, though, is I do know that one of the impacts for mailing the checks for stimulus is the fact that we are in the middle of filing season. There is a lot of work that has to be done around what is already a complex code.

Senator WYDEN. I am not going to belabor this simplification issue. I think the tax code is broken. It has gotten to the point now where practitioners tell me they cannot even get a regional office at the IRS to give a consistent opinion within the office. We used to have problems, for example, say, with Denver disagreeing with Los Angeles. Now we have one of the regional offices not even able to agree among themselves on a difficult issue.

I am going to be trying to advance a bipartisan tax reform effort. I have already proposed a Fair Flat Tax proposal. I hope that on your watch you will be a champion, consistent with your pledge to be nonpolitical, to help us work for tax reform. It is time to drain this swamp. I am impressed with your candidacy. I particularly appreciate your pledge this morning to keep politics out of the Agency. We have seen that, regrettably, just in the last few weeks, the effort to bring the Agency, in my view, into these political debates. I am glad you want to take a different approach.

Mr. Chairman, thank you for this time this morning.

The CHAIRMAN. Senator Hatch, you are next.

Senator HATCH. Thank you, Mr. Chairman.

Welcome to the committee. We are proud of you, and certainly appreciative of your willingness to take on what really is a very daunting task and assignment.

Now, in your position as vice chairman of the Financial Industry Regulatory Authority, you have been responsible for strategy, services, and operations. Now, can you outline for us how, in your view, this is going to help you as you run the IRS?

Mr. SHULMAN. Well, it is a good question, and I have answered it throughout. I think the Financial Industry Regulatory Authority—most of my career it was actually called NASD and oversaw the broker/dealer industry—has a lot of parallels to the IRS. It runs large computer systems. It has to service both the industry as well as individual investors. We conduct examinations. We write rules, have an examination program, and have an enforcement program. So, I am familiar with the intersection of policy and administration.

I was also overseeing very similar difficulties. We have had to wrestle with some of the international challenges that the Chairman referred to in his opening statement, with the globalization of the financial services world: where did our jurisdiction end, how did we ensure that American investors were protected? We had to update and modernize computer systems. We had to bring some new computer systems online as trading was becoming quicker and quicker than ever before. We wrestled with all the very difficult issues of workplace planning and employee planning, and put in place leadership development programs.

As the financial industry was innovating, we had to bring people into the Financial Industry Regulatory Authority who would understand those innovations so we could keep speed with business. So I think, clearly, the IRS would be a huge challenge for me if I am confirmed. I will not sit here and tell you I will not make mistakes, but I think that piece of my background really gave me an opportunity to run a large regulatory-type operation that had both enforcement and services.

Senator HATCH. And the computer systems you worked with actually handled billions and billions of items every year. It seems to me that this is one of the things we really have to upgrade. We are having enough of a rough time trying to upgrade our legal enforcement systems in the country at the FBI and elsewhere with computerized services.

But also, with any organization, the most valuable resource the Service has, of course, is its people. We have a large IRS facility out in Ogden, UT which has won awards for its effectiveness and productivity. I have been very proud and have been out there to see them. However, I hear complaints from some of my constituents about low morale and poor management practices. What would you say are the Service's top human resources challenges, and how do you intend to address them?

Mr. SHULMAN. I think that getting the entire employee base—management and rank and file—motivated and focused is one of the top priorities that any leader needs to have. I mean, in many ways, if you can get the organization focused and the people motivated, the organization runs pretty well. If you do not do that, organizations do not run well. Clearly, there is a lot of turnover, and

the IRS, like other agencies, has a lot of people reaching retirement age.

So, I think we are going to have to work on the underlying recruitment and getting the pipeline filled, as well as grooming the senior management, the next generation of senior management, to take over as this group approaches retirement age.

I really think that I will spend a significant amount of time, if confirmed, on this, first setting the right tone at the top, second, making sure the senior management team is all aligned around goals and there is clear buy-in around goals, and then making sure those goals are pushed down and there is accountability throughout the organization, and communicating both from a central place in Washington and making sure that all the regional offices are all marching to the same drumbeat, all have the same priorities and are trying to deliver for the American people.

Senator HATCH. That is great. In my view, two of the most important changes made in the 1998 Restructuring Act were the establishing of the IRS Oversight Board and the enhancement of the National Taxpayer Advocate. How do you assess the effectiveness of these entities, and how do you think they can be improved? Do you think the top management of the IRS is taking their recommendations seriously enough?

Mr. SHULMAN. I have not had a chance to work with either of these bodies.

Senator HATCH. Sure.

Mr. SHULMAN. I have reached out and spoken with them. I believe that good ideas can come from lots of different places. They do not have to come from the people who work at an agency. I also believe in partnership and good dialogue with all constituencies. So I view both the Oversight Board and the National Taxpayer Advocate as assets to the IRS and would treat them as such.

Senator HATCH. Well, thank you.

Mr. Chairman, my time is up. Thank you.

The CHAIRMAN. Thank you very much.

Senator Schumer is next.

Senator SCHUMER. Thank you, Mr. Chairman.

I want to thank you, Mr. Shulman, for appearing here and for your desire to do public service, which I think is a very fine and noble undertaking. I have heard good things about you and expect to support your nomination, but I have some questions.

My first is on the issue of RALs, the refund anticipation loans, which you may know I have been quite active with. There is legislation that I have sponsored with a few others to restrict these loans. I hope it will be marked up by the Finance Committee this year. I know the IRS has proposed some new rules in this area as well that might take effect next year.

But the bottom line is, we know that millions of Americans are looking forward to receiving the stimulus checks that are the lion's share of the package that our committee is marking up tomorrow. The American people are getting a boost from us and need that check. In fact, many families are so cash-strapped that I am worried they may not even wait for the IRS to send them a check, but instead turn to a RAL or similar product.

You have seen the ads. You sign a form with your tax preparer when you file your taxes. You pay a fee and walk out with cash against your coming refund check. But tax preparers often charge interest rates that can run, on an annualized basis, into triple figures. It is usurious under many State laws but not under others, and it is just disgraceful. That is all for the privilege of getting the money a few days or a few weeks earlier. There is not very good disclosure here. A lot of people do not know what they are getting into. The IRS actually helps reduce their refunds by alerting loan providers to any claims against refund loan applicants' refunds.

So, I think many of these loans are a scam. They are targeted at working-class Americans. It is an outrageous rate for a very short-term loan, which is very low-risk to the lender—and an even lower risk because the IRS helps the preparer flag who is going to present a risk.

So I am worried that tax preparers or payday loan vendors will try to use the RAL model to advance Americans' the rebate we are providing as a way of speeding up the process and getting a smaller rebate check into the hands of families sooner.

For instance, for someone expecting a \$1,600 check in May and a RAL provider or a loan vendor promising to give them a \$1,400 check in March, that is an 87-percent annualized interest rate.

So what I would like to get today from you is your assurance that the IRS will do everything in its power to make sure this does not happen. I would like to know what the IRS can and will do under your leadership to ensure that this rebate is provided as quickly as possible, knowing that delays do give lenders the opportunity to offer high-interest loans and steal this money out of the pockets of American families.

What rules can the IRS put in place to ensure that unscrupulous lenders or scam artists do not try to take advantage of the rebate process? Does Congress need to include explicit prohibitions in the legislative language of the stimulus package?

Mr. SHULMAN. That is a great, great question. Let me just give you my general thought about RALs and then get to your question. I mean, one is, I just think it is unfortunate that taxpayers have to avail themselves of loans and that there are a lot of lower-income families who are in a position where they cannot wait 10 days to get their refund and have to pay high interest rates. I think that is an unfortunate situation. In my current job at the Financial Industry Regulatory Authority we spend a lot of time on financial literacy. I think a goal for the Nation is to have people manage their money in a more prudent fashion.

What the IRS can do on RALs—there are a number of things. One is to actually keep working on the computer system so there is a shorter time between filing and rebates so they will not be as necessary; educate people about their withholding so refund checks are not as large in the regular tax filing season; and then there are these proposals that are out for comment.

I must tell you, I had not thought about the issue of the refund checks. I really do not know the levers that the IRS has on this or whether we need to come back to you and say that it is needs to be done legislatively. So, if you would let me get back to you on that, I would appreciate it.

Senator SCHUMER. But can I have your assurance you will do everything within the power of the IRS to limit these kinds of RALs or payday loans when it comes to the rebate checks, if you are in office at that time?

Mr. SHULMAN. Yes. If I am in office, if you would let me just come back to you on this. It does not sound like that would be a great situation. It is clearly not what the policymakers are intending. I do not know enough about—

Senator SCHUMER. No. I am not asking you to stop them. I would like you to do that. But I am just asking you to do everything within your existing power to try to limit these to be reasonable and prudent. Do you have a problem with that?

Mr. SHULMAN. No.

Senator SCHUMER. Thank you.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator.

Senator Salazar?

Senator SALAZAR. Thank you very much, Chairman Baucus. I have a statement that I will submit for the record, and I have some questions for you, Mr. Shulman.

[The prepared statement of Senator Salazar appears in the appendix.]

Senator SALAZAR. Let me just say, first of all, congratulations to you and to your family for this appointment. I very much enjoyed the discussion that we had in my office yesterday. I have several questions; we will see how far we get.

The first question has to do with land conservation easements. In my State of Colorado, for the year 2003, there were a number of conservation easements that were put into place to try to protect some of our open spaces, our ranch lands, our wild places. And of all the audits that the IRS is conducting from 2003 on conservation easements—there are a total of 500; 375 of those audits are in Colorado. As I spoke to you about this issue yesterday, I very much believe that we need to crack down on those who are abusing the tax system, and if there are fraudulent transactions out there, we need to make sure that we deal with them.

Second, we need to make sure that as we move forward with that regulatory action, that we also are not having a chilling effect on what is a really good program. For me, in Colorado, I have worked on land conservation for most of my life. We do not want Colorado to become quite another Florida or California, so we do not want us to have a chilling effect on this major program which has now been in effect for so long. Colorado and Virginia really lead the Nation.

We need to figure out a resolution to the pending cases, but also as importantly, moving forward with guidelines that will make sure that those who are putting their lands in conservation programs have a sense of reliability with respect to the program.

So my question to you is, are you willing to help us deal with that issue and get it addressed as expeditiously as possible within the IRS?

Mr. SHULMAN. Yes. As we had a chance to talk yesterday, I think these land conservation easements are a wonderful way to preserve natural beauty and historic architecture. My goal would be to make

sure that it is administered in a way that actually promotes that land preservation, which means having clear guidance, education, and standards for those who are making conservation easements, as well as punishing those who are abusing it. So as we talked yesterday, you have my commitment to look into this matter quickly, if I am confirmed.

Senator SALAZAR. Senator Allard and I have written to the IRS several times on this subject, so we will place this as a very high-priority item that we would like to have resolved as soon as possible.

Second, just the issue of timeliness. There is a charitable organization in Colorado that had applied for a determination by the IRS on an exemption. Senator Allard—actually, Senator Grassley as well—had a colloquy on this a couple years ago. We sent a couple letters in to the IRS. It just does not seem to get determined, whatever the determination is. It seems that this charitable organization has been hanging out for a long time.

So would you just very quickly describe what your approach would be to dealing with these kinds of issues as they come before you so that you have, hopefully, a timely response to them?

Mr. SHULMAN. Yes. I think it's an important question for really any regulatory agency, which is, how do you balance having enough time to do a thorough job, with timeliness that allows the taxpayer to get on with its work and allows the organization to free up resources to get to the next issue?

So I have a bias towards—we serve the American people. We need to make sure we thoroughly investigate any issue where we think there is potential wrongdoing or that there is an issue and get to the bottom of things, but we should also try to do it as expeditiously as possible so that there is some certainty in people's lives so they can keep moving forward. So, I am obviously not familiar with this specifically—but I would focus on, in these kinds of programs, trying to get that balance right.

Senator SALAZAR. Thank you, Mr. Shulman.

One final question. Senator Grassley has made a major issue of charitable religious tax issues. In my view, one of the reasons that abuses that may occur within the religious context are not dealt with effectively, and frankly address part of the tax gap that Senator Baucus was addressing, is that there is a fear sometimes of the power of these organizations. I applaud Senator Grassley for his leadership in terms of wanting to make sure that the tax code is being applied fairly to those organizations.

What is your general view?

Mr. SHULMAN. My view, first off, is that this committee has done excellent work in the nonprofit sector and shining a light on this. I think, akin to my other approach, there needs to be clear education, guidance, and lots of communication so people understand where the boundaries are, and there needs to be some enforcement presence where people think they are breaking the boundaries.

I think this gets into sensitive issues. I think in this area, as well as all others, but especially this area, the IRS has to be seen as fair, consistent, and impartial. So I think it is appropriate to have a presence there, but as you said, it needs to be a very consistent, fair approach and has to have no politics involved.

Senator SALAZAR. And is this something you are willing to work on with Senator Grassley, and perhaps other members of the committee who are interested in this issue?

Mr. SHULMAN. Yes.

Senator SALAZAR. Thank you very much, Mr. Shulman.

The CHAIRMAN. Thank you, Senator.

Before recognizing the next Senator in line, Senator Sununu, I may note that Senator Sununu is the 12th Senator from New Hampshire to sit on the Finance Committee. His predecessors have included Chairman Charles Atherton and Chairman Daniel Webster. Although Webster really was from New Hampshire, he officially represented Massachusetts at the time.

Senator Sununu is the first New Hampshire Senator on the committee in nearly half a century, since Senator Norris Cotton in 1960. As I said, New Hampshire has had more Senators on the Finance Committee than any other State but three. Only New York, Pennsylvania and Kentucky have had more members.

So, Senator Sununu, we look forward to your contribution and to your questions.

Senator GRASSLEY. And live up to the expectations. [Laughter.]

Senator SUNUNU. Thank you very much, Mr. Chairman and Mr. Ranking Member. Montana and Iowa may not be on that list, but that just goes to show, it is quality, not quantity that really counts in the Senate.

Mr. Shulman, there is a saying of which I am very fond that goes: be careful what you wish for, you just might get it. I think, to a certain extent that may apply here given your service for the Bipartisan Commission back in 1996 and 1997. I think we called that Kerry-Portman. Were those the two that were involved? Senator Kerry and Congressman Portman.

That led to, as I recall, being in the House at the time, fairly significant legislation that worked its way through both chambers and was signed into law. I imagine, from your biography, you were fairly involved in the construction of the legislation.

Is it your sense, your recollection, that most of the principal recommendations of the committee ultimately were contained in the legislation that made it to the President's desk?

Mr. SHULMAN. A lot of them were, yes.

Senator SUNUNU. What in your recollection, your personal opinion, were the most significant changes or departures, if any, from the recommendations?

Mr. SHULMAN. Departures from the recommendations?

Senator SUNUNU. Yes.

Mr. SHULMAN. You know, I have told some of the people I have had the opportunity to talk to in the Service, it was a long time ago that I was involved in this and I do not pretend, going in, to have all the answers at the IRS, or even to know the organization intimately. I have a lot of familiarity with it from that time. I think maybe I can answer it on the positive side. One of the reasons I think I am sitting here is that I have made my career in management and leadership, not necessarily in tax. That is one of the recommendations, is that a professional manager be appointed to the Commission. I think that—

Senator SUNUNU. Were you looking 10 years into the future when you said that? [Laughter.]

Mr. SHULMAN. Absolutely not. I thought that was where you were going.

Senator SUNUNU. It would be great to have someone who is psychic, so I just thought I would ask.

Mr. SHULMAN. The Commission basically set out a framework that said there needs to be high-quality service, as well as tough enforcement at the IRS. It waded into tax simplification, because I think anyone trying to say, how do you get the tax administration to work better, simplification just becomes something that is quite clear.

I think the last two commissioners since then, and having the 5-year term for the Commissioner so that there is continuity of management and follow-through, were important parts of that recommendation. If I am confirmed, I will go in and, as you said, I will learn what we recommended that worked and what did not work. I will have to live with a little bit of my own cooking.

Senator SUNUNU. Are there any other specific recommendations or components of the legislation that you think, again, from your perspective in the private sector, have had a positive impact or a particularly positive impact? Do you have certain opinions about which of the recommendations were the most important changes in the way they do business?

Mr. SHULMAN. I have a hard time answering that. Maybe if we got an opportunity, once I was in there—I mean, I was a staff member. These were the recommendations of a broad commission. I think this whole notion of focusing on taxpayer rights, focusing on service, focusing on appropriate enforcement, all of those pieces really drove through and were implemented at the IRS.

A lot of those had been implemented before, so I cannot really speak to it. But I think a lot of the same issues are on the table, as the Chairman said in his opening statement. Modernizing the computers, getting good service, focusing enforcement resources, are all things that are going to continue to be important to the IRS.

Senator SUNUNU. Have you had the opportunity to speak with any of your predecessors about the position and the challenges?

Mr. SHULMAN. I have.

Senator SUNUNU. What did they highlight as the things that you need to be most cognizant of, or perhaps be most prepared to deal with, entering the role?

Mr. SHULMAN. My predecessors were relatively consistent in telling me that it is an incredibly talented and dedicated workforce who really are looking for leadership, from not just the Commissioner, but the entire senior team. They emphasized the non-political nature, not being viewed as partisan, and really making decisions based on your own best abilities in implementing the tax code as fairly as possible. They all focused on getting the computer modernization moved forward.

They focused on the importance of some of the work that really was done in the last 5 years around tax shelters and enforcement as important to have a close dialogue/partnership, and, when needed, push the practitioner community to make sure that they are doing the right thing by taxpayers and the government.

Senator SUNUNU. Thank you very much.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator.

Senator Smith?

Senator SMITH. Thank you, Mr. Chairman.

Mr. Shulman, good to see you again. Thank you for being here. Many of us have mentioned the issue of computers and the need to modernize that. Since we met in my office, I wonder if you have had any further thoughts about that, if you were putting in the budget request with OMB to make sure you have the resources to actually modernize them.

Mr. SHULMAN. Yes. I am not privy to any budget discussions, being a private citizen right now and not employed by the government and part of the administration. So that, I have not had a chance to look at. I think my thoughts are similar to what we talked about. The computer systems need focus. We need to make sure there is clarity around the goal, and, if I understand the goal, it is getting real-time information into the hands of the people at the IRS so they can service taxpayers well and focus their enforcement resources. We need to make sure that there is the right scope of projects, the right funding, as you said, for the projects, and that there are the right people in place and they are governed properly.

A lot of it is—big technology operations are difficult. Technology is evolving at a very rapid pace. I have seen a lot of major financial services organizations struggle with upgrading their technology in the private sector. It looks like the IRS has actually matured its processes quite a bit since I was last there, but it is going to need a lot of focus and attention.

Senator SMITH. I have noticed in a number of the presidential campaigns that the IRS continues to be the bogeyman, and some even want to abolish it. I suppose there is some inevitability that the IRS is not one of the most loved agencies of the Federal Government. But I wonder if you think the IRS has a PR problem, and are there things that can be done that you will do to address it?

Mr. SHULMAN. Well, I have thought about this some. I mean, clearly the IRS is one of the most recognized brands in America. I think it clearly has a job to do that not everybody likes. I think the real focus, and I would not think of it as PR for the IRS, but the important thing, I think, is that the IRS be seen as competent, it be seen as fair, it be seen as impartial. So my belief is, there is no major marketing that needs to be done. It is really continuing to engage the entire workforce so that their interactions with the American people are viewed as such.

Senator SMITH. Do you think it is viewed as fair and competent or is there room for improvement on that score?

Mr. SHULMAN. My philosophy in life is, I would like to always be better tomorrow than I am today. There is always room for improvement in any operation. That is how I approach my work and that is how I expect my colleagues to approach their work. So, I am sure there is room for improvement at the IRS.

Senator SMITH. I am interested in any thoughts you might have upon the issue of the aging of our population and the concern, as someone in the securities industry as you have been, with the retirement savings rates of Americans, and I wonder if you have any

thoughts on what we might be able to do to help spur it below the negative that it is now to a positive.

Senator Bingaman and I have proposed automatic payroll deposits in IRAs, those kinds of things. Automatic enrollment has been shown to help, and potentially reverse, this trend. Do you have any other ideas that we ought to be pursuing to help improve America's savings rate?

Mr. SHULMAN. You asked about retirement. We have spent a lot of time focused on really the baby boomer generation retiring and needing to take care of its retirement. There is a lot of work we have done at the Financial Industry Regulatory Authority. Clearly there are a lot of provisions of the tax code designed to encourage retirement savings. I would have to think more about this and probably defer to tax policymakers. But it is an interesting issue that I would love to be engaged with you on, if I am confirmed.

Senator SMITH. All right.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator.

Mr. Shulman, I intend to hold, as I mentioned in my statement earlier, some fairly lengthy hearings on tax reform. I would like to have your commitment that you will clearly work with us by devising some new changes that you think would make the code simpler and easier to understand and work with, and then work with us to help implement them.

Mr. SHULMAN. Yes.

The CHAIRMAN. That means working with your staff, and not just some off-the-top commitment, but to definite effort where our staffs, committee staffs, and your staff are working step-by-step to make some changes here.

Mr. SHULMAN. Yes, you have my commitment. I mean, as we have had a chance to talk, I think the intersection between policy-making and policy administration is incredibly important. So I think it is very important to have a very close relationship and a deep dialogue between the IRS and the tax policymakers.

The CHAIRMAN. Last year, a prisoner told this committee how easy it is to steal identities and file false tax returns. It was stunning, frankly, how easy it is. Commissioner Everson testified that identity theft cases under \$40,000 would not be prosecuted due to lack of resources. I would like your views on prosecution of identity theft cases.

Mr. SHULMAN. I think identity theft, data security, and computer security are major issues for every government and private organization that is handling sensitive data right now. I am aware of that hearing. I think getting the right balance between making service quick and easy through the computers, but also making sure there is security in those computers is always a difficult issue for commercial financial services firms and for the government.

I think identity theft is a horrendous crime that should be prosecuted. I am not aware of how IRS now triages its cases and does resource allocations, so I do not know exactly where they are in the queue. But as a matter of principle, I think identity theft should not be tolerated.

The CHAIRMAN. Well, this is clearly a very, very high priority. Obviously you cannot answer it very precisely right now, but you

know it is such a high priority. It is certainly a high priority of this committee.

Next, a couple of questions about globalization. I am just concerned, with all the complexity, that the IRS just frankly is getting behind the curve. It is not getting ahead of the curve, what is going on in the world. I am not talking so much now about the tax gap, although that is a large part of it, that is, taxes legally owed but not collected. In addition to taxes legally owed but not collected, it is misusing and abusing loopholes and other provisions of the law which on the surface are legal, but clearly are being used in a very abusive way.

I must say, and Senator Grassley and I went down to IRS and talked to the Commissioner and talked to people down there, I just came away with the impression that we just are not ahead of the curve with all the new complexities that are being developed worldwide. Your thoughts. Can you just comment on that a little bit, please, and what you think is going on? In your current job—your current/previous—you have some insight into all of this. Your thoughts on how we could get the Commission ahead of the curve.

Mr. SHULMAN. Yes. Absolutely. I think it is an issue of huge import right now. Between technology, communication, the workforce, it has all allowed businesses to become global operations. Clearly, the IRS needs to keep pace, as does every regulatory agency.

At the Financial Industry Regulatory Authority, it is actually quite interesting. When I showed up 7 years ago and first started a little over 7 years ago, trading desks in the U.S. would have responsibility to trade just equities, so they would trade New York Stock Exchange stock only on a specific desk; that is what they were responsible for. Over the next couple of years they started trading stocks and bonds and eventually started trading derivative products, and they were putting together much more complex trades.

Recently, desks have been trading all of those and then moving the book around the world. So one day you are trading with the firm's money for a set of customers in New York. When you are done trading in New York, it may move to London. In London, the same firm, the same problem they are trying to solve, the same trades they are trying to get off, they are happening at the London desk, and then the Tokyo desk, and the book can just move around the world. What ends up happening is, we have authority for U.S. broker/dealers, but we need to think about how we are protecting the customers where the trading is occurring on behalf of those customers in another jurisdiction.

What I will tell you is, these are not easy answers. They involve sovereignty of regulators. For us, we are not a government organization. We are under the auspices of the SEC, the Financial Industry Regulatory Authority is. Treaties are incredibly important to have the proper information sharing and, when necessary, actually having joint efforts going on. So I think, actually, for my term as Commissioner, if I am confirmed, these global issues around tax administration are going to be some of the most important, complicated ones that we are going to have to focus on getting a handle on.

The CHAIRMAN. Senator Grassley?

Senator GRASSLEY. My first, is a comment. The nexus for it is based upon Senator Salazar's question about nonprofits. Then a reminder that when you and I talked in my office, one of the problems we have—not with IRS any more than any other government agency—but they do not answer our letters all the time. Well, I guess Senator Salazar made that clear.

But anyway, on this nonprofit stuff, a recent hearing in the House about abuse of money that people contribute to veterans organizations is one example, a tremendous waste of money in the money-raising process, I guess it is, and things of that nature. We cannot take for granted the review of these organizations and policing them and all that sort of thing. The only thing I am asking you is, I do not know how long ago, but we have some letters down there at IRS that have not been answered yet on this subject, and I wish you would dig those out and respond to those.

Then the second point I want to make is about IRS hiring veterans. But before I ask my question, I think it is safe to say that the President made clear last night, maybe more on health than on a general approach to veterans, that we need to do all we can for our veterans. So, it is about the IRS hiring veterans. The Nation is seeing a significant number of veterans, many of whom are disabled, returning from Iraq and Afghanistan. These are extraordinary young men and women, and our country is honored by their service. There is no question that these men and women are extremely capable. I think it is important for the Federal Government to do all that it can to hire these returning veterans.

It is clear that the IRS offers many opportunities to service men and women, particularly the disabled. These veterans will bring to the IRS a good deal of much-needed youth, a fresh outlook and experience, and most importantly, a can-do attitude that is much needed. The IRS would greatly benefit from these veterans joining the ranks.

So I wanted to ask you, when you are hiring new employees, I would like to raise with you the goal of hiring 1,000 Iraq and Afghanistan veterans this fiscal year, with a particular emphasis on those who are disabled.

So please provide me information on how you would seek to implement this goal, including outreach, job classification, reclassifications, notification, working with veterans' organizations, working with the Department of Veterans Affairs and the Department of Defense. In addition, if there are any legislative changes that would assist this effort, please identify them. However, I am confident that the IRS has significant authority at hand to accomplish this goal.

So for me it is not a question of when, it is a question of why not hire these people, and have a real aggressive effort on the part of the IRS to do it.

Mr. SHULMAN. Yes. Senator Grassley, I think you bring up an important point. Let me assure you, I share your goal, and I share the sentiment of the importance of making sure that veterans and American service men and service women are treated well when they come back to America after fighting on our behalf and are given all the opportunities that we can afford them.

I must tell you, I am really not familiar with what the IRS hiring process is and their ability, et cetera, but you have my commitment to work with the administration and all the agencies you said to try to work towards a goal such as that.

Senator GRASSLEY. Yes.

My last question is, though you are not considered by some to be a tax person in a technical sense, how will you establish your managerial authority such that it is recognized and respected throughout the IRS? How can you assure this committee that you will take a hands-on approach with the Office of Chief Counsel?

Mr. SHULMAN. Yes. It is a good question. It is clear to me that, if I am confirmed, I will be accountable for administering the Nation's tax laws. When I am accountable for something, I view that I need to have the authority to meet that accountability. My general approach to working with all my colleagues, including the Chief Counsel, is that person will be my chief legal advisor. They will be responsible for giving me the best advice and counsel possible.

I will work towards having a transparent, open dialogue and relationship with them, and I will expect them to bring exactly what information I need, as I will expect of everyone I work with, and I will do the same for my colleagues. At the end of the day, because I will view myself as accountable for tax administration in the country, I will make sure I am deeply involved in whatever issues I feel I need to be involved in.

Senator GRASSLEY. Thank you.

The CHAIRMAN. Thank you, Senator.

Thank you, Mr. Shulman. I listed several very key sort of points that you are going to have to address as Commissioner, and other Senators have asked lots of questions along the same lines, and added other issues as well. I want to say this. You know, I have been here a few years. Some of these problems have just been festering. They are just developing. They are not being solved. Personally, I am getting a little frustrated.

I am here, just as long as I am on this committee, either Chairman or Ranking Member or whatnot, I am going to do all I possibly can to help you keep your eye on the ball in solving those problems. Very often this body, this Congress, is guilty of what some of us charge the Service and other government agencies of being guilty of, namely, inadequate follow-up, inadequate follow-through. Very often in this town people raise an issue and there are headlines, then people tend to forget about it. Some intentionally want to forget about it, others just have other business and forget about it.

But we are not going to forget about it. I am not going to forget about it. Every time you come before this committee, I am going to be going down that list of issues again. I expect you to come up with answers that are not platitudinous, not generalizations, but actual demonstrations of progress.

To me, that means baselines, quantifications. You have to quantify each of these problems so that you know whether you are making progress or not, so you can demonstrate to this committee whether you are making progress or not.

I will be very upset if I just hear generalizations, "We are making progress, we are working on that." I have had enough of that.

The American people have had enough of that. These problems that you are facing are tremendous. Let us start with the computer problems, for example. That is just one out of many.

I wish you good luck. I wish you well. Thank you for the service you are providing. But we have a job ahead of us, and I am going to do my part to help make sure that, together, we resolve it. But you are the person on the line there, so you know what the solutions are more than do I. It is more my responsibility to make sure that you solve the problems and that you have the resources necessary to solve all these problems.

So I wish you luck.

Mr. SHULMAN. Thank you very much.

The CHAIRMAN. Thank you very much.

The hearing is adjourned.

[Whereupon, at 11:21 a.m., the hearing was concluded.]

APPENDIX

ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

United States Senate
Committee on Finance



Sen. Chuck Grassley · Iowa
Ranking Member

<http://finance.senate.gov>
Press_Office@finance-rep.senate.gov

Statement of Sen. Chuck Grassley
Committee on Finance Hearing on the Nomination Douglas Shulman as IRS Commissioner
Tuesday, Jan. 29, 2008

Thank you, Mr. Chairman, for holding this hearing so quickly. The position of IRS Commissioner is very important and it is vital that the position be filled as quickly as possible, given a thorough review by this Committee. I am eager to hear Mr. Shulman's testimony so I will keep my remarks short. Although he doesn't have in-depth tax expertise, Mr. Shulman brings a strong managerial background with him, and he will need all of his talents to succeed as IRS Commissioner.

I have a few basic yet significant concerns I want to touch on. The problems the IRS has with computers are legendary as well as a source of great consternation and government spending. The next Commissioner must do more to modernize the computer system used by the IRS, and spend the money to do it more effectively than has been done in the past.

Next, it is important that the IRS Commissioner be seen to be in charge of his agency, and this means that he take a hands-on approach to the Office of General Counsel. Additionally, I'm sure it will surprise no one to know that I am concerned about the tax gap, and that I consider the Private Debt Collection program an excellent way to work to close the tax gap. It is important that IRS management continues to support this valuable program. Finally, I am concerned about information I have received, that while there are not enough IRS personnel working to enforce the tax laws, the amount of time devoted by IRS employees to work for their union is greater than the average for the entire federal government.

These will be important issues for the next Commissioner. Finally, I want to mention that my staff reminds me that I have several outstanding letters to the IRS and Treasury. I am sure we will be able to work together to resolve these requests in a timely manner. Thank you again, Mr. Chairman. I look forward to hearing from Mr. Shulman.

**Opening Statement
Senator Ken Salazar
January 29, 2008**

Thank you, Chairman Baucus and Ranking Member Grassley, for holding today's hearing on the nomination of Douglas Shulman to be Commissioner of the Internal Revenue Service.

I also want to thank Mr. Shulman for appearing before the Committee today. Congratulations on your nomination.

The Commissioner of the IRS has a vital role to play with respect to a number of critical issues, including efforts to close the tax gap and overseeing the development and issuance of important guidance for taxpayers, businesses, and other organizations to help them comply with the laws we pass here in Congress.

While I appreciate the work that Kevin Brown and Linda Stiff have performed in their role as Acting Commissioner since Commissioner Everson resigned last year, it is nice to finally have the opportunity to create certainty with respect to who will be overseeing the duties and responsibilities of the IRS in the coming months and years.

Given that the next IRS Commissioner is likely to serve in that role for some time, I am interested this morning in hearing Mr. Shulman's views on some of the big picture issues that Congress and the Administration are dealing with in terms of tax administration and taxpayer assistance.

I also want to raise two specific matters that are of particular importance to my state of Colorado. Your views on these matters will be integral in informing my approach to your nomination.

The first is an issue that many of us are familiar with, but that has had a disproportionate impact on Colorado – the IRS's ongoing efforts to investigate and address alleged abuses of charitable contributions to conservation easements. Several hundred of these easements have been under investigation by the IRS in my state, and these investigations have serious implications with respect to both the need to prevent abuses and the importance of allowing legitimate easements to go forward.

Let me emphasize that I strongly support the effort to identify and deal with abusive transactions and with those who promote them. Landowners who have violated the law and abused the system must be held accountable. Neither I nor the conservation community in Colorado wants these abusive practices to stain the long history and stellar record of the conservation movement in our state.

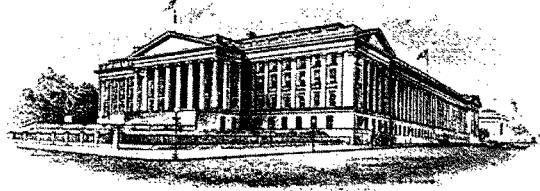
Additionally, I want to see a swift and just resolution to the pending investigations into conservation easement donations in Colorado. I understand that some of these audits deal only with questions over the valuation of the easements under investigation, and that the IRS has pledged to work to resolve these cases expeditiously and fairly.

I strongly urge you to uphold that commitment.

The second issue I want to raise today has less to do with Mr. Shulman than it does the agency he has been nominated to oversee, and that is the application by a charitable organization in Colorado – the Reisher Family Foundation – for an exemption from a specific provision in the Pension Protection Act of 2006. The Foundation, which provides invaluable assistance to low-income students in Colorado who want to attend college, has now been waiting for over a year for a determination from the IRS.

Given that the Foundation appears to have met all the necessary criteria to receive an exemption, this delay is extremely troubling. I am extremely eager to see this matter resolved as soon as possible.

Thank you again, Mr. Shulman for being here today. I look forward to hearing your views on these and other matters.



U.S. TREASURY DEPARTMENT OFFICE OF PUBLIC AFFAIRS

**TESTIMONY OF DOUGLAS H. SHULMAN BEFORE THE SENATE FINANCE
COMMITTEE ON NOMINATION TO BECOME THE COMMISSIONER OF
INTERNAL REVENUE**

Washington, D.C.--Good morning, Mr. Chairman, Ranking Member Grassley and Members of the Committee.

My name is Douglas Shulman and I am currently the Vice Chairman of the Financial Industry Regulatory Authority. It is an honor to appear before the Committee today as you consider my nomination to become the Commissioner of Internal Revenue.

I appreciate your giving me the opportunity to make a brief opening statement before taking your questions. I would also like to take this opportunity to introduce my wife, Susan, and my two children, Benjamin and Eve.

Mr. Chairman, the importance of the Internal Revenue Service (IRS) cannot be overestimated. How the IRS approaches its work, and interacts with taxpayers, greatly affects both the functioning of the federal government, as well as Americans' overall view of their government.

The IRS touches every adult, every business and every non-profit organization in America. For many citizens, it is the only federal agency with which they will have contact in a given year.

Never has thoughtful leadership and direction at the IRS been more critical, as the federal government's responsibilities to its citizens have grown.

As you know, the IRS collects the vast majority of the revenue needed to fund our government and the services it provides, from protecting the environment to defending our homeland to improving educational opportunities and increasing access to health care services. It is an awesome responsibility to lead such an agency. And because I recognize the enormous challenge of the position, I have given a lot of thought as to how I would approach the job.

Since I've been nominated, many people have asked me if I would emphasize service or enforcement. But to be forced to choose between the two is a false choice. In order to execute its mission, the IRS must do both.

For taxpayers who pay their taxes willingly and on time, which is the great majority of Americans, there must be clear guidance, accessible education, and outstanding service. Our aim should be to make it as easy as possible for them to pay the correct amount of taxes in the most efficient and least burdensome manner possible. For taxpayers who intentionally evade paying their taxes, there must be rigorous enforcement programs. But whether serving taxpayers or enforcing the law, it is absolutely essential that Americans believe the IRS is fair and that it respects the rights of all taxpayers.

Thanks to Commissioners Rossotti and Everson, there are important initiatives currently in place that I confirmed I would anticipate continuing. I would also bring a fresh set of eyes to the position, and ensure that the agency continues to evolve as circumstances change.

Any effort to improve services must include a commitment to IRS modernization. IRS employees must have timely access to taxpayer data so assistance is quick and accurate. This will require focusing on and investing in IRS processes, as well as the IRS's information technology systems. If confirmed as Commissioner, I would make this one of my top priorities.

The IRS must also continue its rigorous enforcement programs. It must deter those who may be inclined to evade their legal tax obligations and pursue those who engage in evasion. And as Members of this Committee already know, in recent years a number of significant steps have been taken to shut down tax shelters and other abusive transactions that were created for no other reason than to avoid taxation.

I also believe that it is essential for the IRS to work closely with the practitioner community, including lawyers, accountants, and tax preparers – a vital part of our nation's tax compliance system. The IRS must use all the tools at its disposal – dialogue, education, service and enforcement – to ensure that these important members of the tax community are partners in our efforts to see that all individuals and institutions meet their tax obligations.

Finally, if confirmed, I plan to focus on leadership and employee development during my tenure as Commissioner. I have been extremely impressed by the current leaders of the IRS and its dedicated and talented workforce. However, like other federal agencies, many experienced and knowledgeable IRS employees will be approaching retirement eligibility in the coming years. It is critical that the next Commissioner devotes significant attention to the recruitment, training and grooming of the next generation of IRS leaders.

Mr. Chairman, it is an honor to have been nominated by the President to be the next Commissioner of the IRS. I am under no illusion that, if confirmed, it will be a very demanding and difficult job.

As Commissioner, I would do everything in my power to ensure that the nation's tax laws are administered in a fair and efficient manner. Essential to my success would be a close partnership with Members of Congress on both sides of the aisle, and you have my commitment to work closely with this Committee.

Thank you and I would be happy to respond to your questions.

**SENATE FINANCE COMMITTEE
STATEMENT OF INFORMATION REQUESTED OF NOMINEE**

A. BIOGRAPHICAL INFORMATION

1. Name: (Include any former names used.)
Douglas H. Shulman
2. Position to which nominated:
Commissioner, Internal Revenue Service
3. Date of nomination:
4. Address: (List current residence, office, and mailing addresses.)
Home:
Office: FINRA, 1735 K St, NW, Washington, DC 20006
5. Date and place of birth:
May 10, 1967; Dayton, OH
6. Marital status: (Include maiden name of wife or husband's name.)
Married to Susan Lynn Anderson
7. Names and ages of children:

8. Education: (List secondary and higher education institutions, dates attended, degree received, and date degree granted.)
 - Georgetown University Law Center, 1996-1999, JD 2000
 - Harvard University, John F. Kennedy School of Government, 1995-1996, MPA 1996
 - Williams College, 1985-1989, BA 1989
 - Oakwood High School, 1981-1985, High School Diploma 1985
9. Employment record: (List all jobs held since college, including the title or description of job, name of employer, location of work, and dates of

employment.)

- Financial Industry Regulatory Authority (known as FINRA, formerly the NASD),
Currently Vice Chairman (hired as Executive Vice President; promoted to
President, Markets, Services and Information; promoted to Vice Chairman),
Washington, DC, 2000-Present
 - FoundryOne, Inc., Co-Founder, San Francisco, CA/Washington, DC, 2000
 - Darby Overseas Investments, Ltd., Vice President, Washington, DC, 1998-2000
 - National Commission on Restructuring the IRS, hired as Senior Policy Advisor,
promoted to Chief of Staff, Washington, DC, 1996-1997
 - Share New York, Executive Director, New York, NY, 1992-1995 (also served as
consultant in 1995 and 1996)
 - Bronx Regional High School (New York City School System), Substitute Teacher,
New York, NY, 1991
 - Teach For America, Inc., Co-Founder, New York, NY, 1990-1991
 - AT Kearney, Inc, Analyst/Consultant, New York, NY, 1989-1990
10. Government experience: (List any advisory, consultative, honorary, or other part-time service or positions with Federal, State or local governments, other than those listed above.) NA
11. Business relationships: (List all positions held as an officer, director, trustee, partner, proprietor, agent, representative, or consultant of any corporation, company, firm, partnership, other business enterprise, or educational or other institution.)
- Currently member of Board of Directors of Depository Trust and Clearing Corporation (DTCC)
12. Memberships: (List all memberships and offices held in professional, fraternal, scholarly, civic, business, charitable, and other organizations.) N/A
13. Political affiliations and activities:
- a. List all public offices for which you have been a candidate. N/A
 - b. List all memberships and offices held in and services rendered to all political parties or election committees during the last 10 years. N/A
 - c. Itemize all political contributions to any individual, campaign organization, political party, political action committee, or similar entity of \$50 or more for the past 10 years.
 - \$500 to the Democratic National Committee
 - \$50 to Rob Portman for Congress

- \$150 to Rob Portman for Congress

14. Honors and Awards: (List all scholarships, fellowships, honorary degrees, honorary society memberships, military medals, and any other special recognitions for outstanding service or achievement.)
Fellowship for partial tuition at Harvard University, John F. Kennedy School of Government
15. Published writings: (List the titles, publishers, and dates of all books, articles, reports, or other published materials you have written.) N/A
16. Speeches: (List all formal speeches you have delivered during the past five years which are on topics relevant to the position for which you have been nominated. Provide the Committee with **two** copies of each formal speech.)
Speeches not relevant
17. Qualifications: (State what, in your opinion, qualifies you to serve in the position to which you have been nominated.)

I have extensive experience managing and leading organizations in both a regulatory and business environment. As Vice Chairman of the Financial Industry Regulatory Authority (FINRA, formerly NASD), I am a senior executive of an organization that has many parallels to the Internal Revenue Service. FINRA, like the IRS, must execute the following functions at a world-class level: customer service; data analysis and security; technology development and operations; examinations and enforcement; policy development; strategic planning; and human resource management. I know how to drive change and lead an organization that has immense operational and management challenges, but operates in the public spotlight.

Given the immense technology challenges and opportunities that confront the IRS, it is important that I have a proven track record overseeing technology development and operations. Together with a team I recruited, I orchestrated the modernization of FINRA's technology portfolio, which processes billions of trades annually, monitors much of the US capital markets, delivers over 275,000 annual tests to industry professionals, and processes the paperwork of over 650,000 broker/dealer employees annually. We placed particular emphasis on developing new systems that leveraged innovations in technology to better interface with customers and constituents, improve employee productivity, and manage and analyze data.

I am also passionate about management and leadership development and have made that a priority during my tenure at FINRA. Among many other management initiatives, two times a year I led full-day sessions with key organizational leaders to discuss priority setting and goals, navigating change, balancing short and long term objectives, and managing employees. I understand how to motivate a large employee base, and bring out the best in a workforce.

In 1996-1997, I served as Senior Policy Advisor and subsequently Chief of Staff of the National Commission on Restructuring the IRS (the Commission). The bipartisan Commission, which was comprised of Members of Congress from tax writing committees, representatives of the Administration, senior executives from large corporations, and tax experts, was charged with making recommendations to bolster the public trust in the IRS and ensure that it performed optimally for the American taxpayer and the federal government. The Commission studied the operations and governance of the IRS and made recommendations to improve the effectiveness of the IRS through the use of taxpayer education, modern customer service practices, and effective law enforcement techniques. These recommendations served as the foundation for legislation subsequently enacted by Congress.

As Senior Policy Advisor, my role on the Commission staff was to study the administration, operations, and governance of the IRS; formulate recommendations for the Commission to consider; and build consensus among Commissioners for recommendations. As Chief of Staff, a position I held after the release of the Commission report, my role was to work with Members of Congress and their staff to turn the Commission report into legislation for consideration by Congress. As a result of my work on the Commission, I have a history with the IRS, and through my role at FINRA and the Commission, I have intimate knowledge of the intersection of policy formulation and policy administration and implementation.

B. FUTURE EMPLOYMENT RELATIONSHIPS

1. Will you sever all connections with your present employers, business firms, associations, or organizations if you are confirmed by the Senate? If not, provide details. Yes, however I will receive 6 months continuation of salary after leaving my employment with FINRA per an Employment Agreement.
2. Do you have any plans, commitments, or agreements to pursue outside employment, with or without compensation, during your service with the government? If so, provide details. No
3. Has any person or entity made a commitment or agreement to employ your services in any capacity after you leave government service? If so, provide details. No
4. If you are confirmed by the Senate, do you expect to serve out your full term or until the next Presidential election, whichever is applicable? If not, explain. Yes

C. POTENTIAL CONFLICTS OF INTEREST

1. Indicate any investments, obligations, liabilities, or other relationships which

could involve potential conflicts of interest in the position to which you have been nominated. N/A

2. Describe any business relationship, dealing or financial transaction which you have had during the last 10 years, whether for yourself, on behalf of a client, or acting as an agent, that could in any way constitute or result in a possible conflict of interest in the position to which you have been nominated. N/A
3. Describe any activity during the past 10 years in which you have engaged for the purpose of directly or indirectly influencing the passage, defeat, or modification of any legislation or affecting the administration and execution of law or public policy. Activities performed as an employee of the Federal government need not be listed.

During my employment with FINRA, I have been actively engaged in broker/dealer and capital markets policy issues. FINRA is overseen by the Securities and Exchange Commission, and I frequently had interaction with that agency to discuss FINRA proposals and policy issues. I also testified before Congress on two occasions:

- >3/03: Testimony before the House of Representatives, Financial Services Committee, Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises, regarding Internet disclosure of information about financial services personnel.
- >6/04: Testimony before the Senate Committee on Banking, Housing and Urban Affairs, regarding regulation of bond markets.

4. Explain how you will resolve any potential conflict of interest, including any that may be disclosed by your responses to the above items. (Provide the Committee with **two** copies of any trust or other agreements.) N/A
5. **Two** copies of written opinions should be provided directly to the Committee by the designated agency ethics officer of the agency to which you have been nominated and by the Office of Government Ethics concerning potential conflicts of interest or any legal impediments to your serving in this position.
6. The following information is to be provided only by nominees to the positions of United States Trade Representative and Deputy United States Trade Representative:

Have you ever represented, advised, or otherwise aided a foreign government or a foreign political organization with respect to any international trade matter? If so, provide the name of the foreign entity, a description of the work performed (including any work you supervised), the time frame of the work (e.g., March to

December 1995), and the number of hours spent on the representation.

D. LEGAL AND OTHER MATTERS

1. Have you ever been the subject of a complaint or been investigated, disciplined, or otherwise cited for a breach of ethics for unprofessional conduct before any court, administrative agency, professional association, disciplinary committee, or other professional group? If so, provide details. No
2. Have you ever been investigated, arrested, charged, or held by any Federal, State, or other law enforcement authority for a violation of any Federal, State, county or municipal law, regulation, or ordinance, other than a minor traffic offense? If so, provide details. No
3. Have you ever been involved as a party in interest in any administrative agency proceeding or civil litigation? If so, provide details.

I have not been involved as a party in interest in any administrative agency proceeding, however in my capacity as the FINRA representative to the Board of Directors of the Depository Trust and Clearing Corporation (DTCC), I was named in the following two civil actions:

A. Nutek, Inc., etc. et al. v. Ameritrade, Inc., et al.
CV-S-03-0321-JCM-RJJ was filed in Nevada district court in or about March 2003.

In April 2004, DTCC filed a motion to dismiss as against all DTCC Defendants on various jurisdictional and substantive grounds. Plaintiffs voluntarily dismissed the DTCC Defendants (including me) from the action.

B. Williamson v. Goldman, Sachs & Co, CV-N-03-0057-HDM-VPC was filed in the District Court of Nevada, in Reno, in or about January 2003.

The DTCC Defendants were never served in this action and the case was dismissed in March 2004.

4. Have you ever been convicted (including pleas of guilty or *nolo contendere*) of any criminal violation other than a minor traffic offense? If so, provide details.
No
5. Please advise the Committee of any additional information, favorable or unfavorable, which you feel should be considered in connection with your

nomination. None that I can think of

E. TESTIFYING BEFORE CONGRESS

1. If you are confirmed by the Senate, are you willing to appear and testify before any duly constituted committee of the Congress on such occasions as you may be reasonably requested to do so? Yes
2. If you are confirmed by the Senate, are you willing to provide such information as is requested by such committees? Yes

**RESPONSES TO QUESTIONS
FOLLOWING THE TESTIMONY OF DOUG SHULMAN, NOMINEE FOR IRS
COMMISSIONER, BEFORE THE SENATE FINANCE COMMITTEE**

**Chairman Max Baucus
Questions for Douglas Shulman**

VISION

Question 1

The IRS' mission statement says, "Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all."

- a. Describe how you will enable the IRS to more effectively fulfill its mission statement.**

Answer

I believe that the job of a leader is to communicate a clear vision and direction, insist on a culture of integrity and accountability, support the employees of an organization as they work towards its mission, and be personally involved in important issues. I also believe that in a public setting, an effective leader communicates with and engages a wide range of stakeholders. If confirmed, I will do my best to provide leadership both inside and outside the IRS.

- b. Looking ahead to the end of your term, what do you want to be your legacy at the IRS?**

Answer

If confirmed, I would like to leave the IRS better than I found it. I would want to have helped improve both taxpayer service and enforcement, and to have moved modernization forward to support both facets of the IRS. I also would like to have recruited, trained, and groomed the next generation of IRS leaders, leaving the agency strong for the decades to come.

On a personal note, I would like to be remembered as a leader who was honest and transparent, led with the courage of his convictions, took on tough problems, and operated in a non-partisan manner.

PRIORITIES**Question 2**

Name your top five priorities for your first year in office. Explain why you selected these five priorities and describe the actions you intend to take to address them.

Answer

If confirmed, I plan to spend time listening to and learning from people inside and outside the IRS. The process will help inform my priorities. However, my initial thoughts regarding first-year priorities would include the following:

1. Focus on the tax gap. Work with the Administration and Congress to implement current plans and think creatively about new ones. Strategically invest in audit, enforcement, and proactive taxpayer services all designed to increase the compliance rate.
2. Develop a multi-faceted plan to prepare the IRS workforce for the challenges of the future. Particularly focus on leadership development, managing an aging workforce, and programs to encourage key personnel nearing retirement age to stay on board.
3. Invest in modernizing IRS technology, focused on ensuring that IRS employees have real-time access to taxpayer information so that assistance is quick and accurate and enforcement resources are properly targeted. Identify any problems quickly for discussion and quick resolution.
4. Focus IRS leadership on staying ahead of the curve on key issues, including financial products, international taxation, tax-exempt organizations, etc. Recruit outside resources as necessary to ensure sufficient levels of expertise in complex and emerging issues.
5. Develop respectful and open relationships with key stakeholders including members of Congress, Administration officials, IRS Oversight Board Members, employees and senior leaders, and the broader tax community.

DIRECT ELECTRONIC FILING FOR FREE**Question 3**

Taxpayers can file a paper tax return directly with the IRS for free. However, they cannot file an electronic return *directly* with the IRS under any circumstances, and most taxpayers who file electronic returns *pay a fee* for the transmission of

their return. I believe taxpayers who want to file directly with the IRS for free should have that option – just one option among many for filing a return.

- a. To what extent do you think the ability to file directly with the IRS for free would help the IRS achieve Congress' goal of 80% electronic filing by 2007 – a goal that has fallen short since about 57% of returns were filed electronically in 2007?

Answer

In my current position, I have had the opportunity to see how the speed of technology change has affected the financial industry. I understand that Congress has set a goal of 80 percent of all returns being filed electronically, but the road map for achieving that goal has not been updated in several years. I understand from my discussions with IRS senior management that the Senate Appropriations Committee has requested an IRS study of options to increase electronic filing. As part of this study, the IRS will review the possibility of creating a way for taxpayers to file directly with the IRS, explore the potential of 2-D bar coding to improve overall tax processing, and consider the effect preparer mandates could have – among other options. I expect that study will become the foundation for a new IRS strategy to increase electronic filing. If confirmed, I intend to review carefully the study and any recommendations it makes.

- b. What actions will you take to increase the rate of electronic filing?

Answer

As I noted above, I understand that the IRS is currently conducting a comprehensive study to examine ways in which the rate of electronic filing can be increased. I have been told that the study will examine a number of options and conduct analysis of the costs and benefits associated with each. If confirmed, I will carefully review this study and the resultant recommendations, and ensure the IRS has a comprehensive strategy to continue to increase electronic filing.

- c. In 2007, less than 4 million individuals out of 90 million used the IRS Free File program.

- i. Why is the rate of usage so low?

- ii. How can the Free File usage rate be increased so more individuals do not have to pay to file their tax returns?

Answer

I understand the Free File program provides the opportunity for many low- and moderate-income Americans to prepare their returns electronically and file them for free. If confirmed, I will need to understand the factors that affect Free File participation

and examine options that the IRS can implement to ensure eligible taxpayers – particularly those who do not already file electronically – take advantage of the program. I understand from my discussions with IRS officials, that the IRS is taking a look at Free File participation. If confirmed, I will review this analysis to determine the steps the IRS could take to ensure eligible taxpayers have the option of filing their returns without cost.

Question 4

TIGTA studies have demonstrated high rates of errors on volunteer prepared returns. The IRS is putting increased reliance on the use of volunteers as the IRS scales back on Taxpayer Assistance Centers. I am concerned that the IRS is shifting the burden to volunteers, but not providing sufficient support to the volunteers to prepare accurate returns.

- a. Describe what you consider to be an appropriate role for volunteer services in tax administration and the IRS's role to support them.**

Answer

In my view, an important responsibility of the Commissioner is assessing how to make the best use of the resources available to serve the needs of taxpayers. In this regard, I believe the IRS volunteer programs fulfill a very important role in tax administration by offering free tax help to low-to-moderate income individuals so they may meet their tax obligations. From my discussions with IRS senior management, I understand that the IRS has partnered with organizations that operate nearly 12,000 sites nationwide in communities where the need exists for volunteer assistance. These volunteers prepare basic tax returns for low-income taxpayers in general, but also those with special needs, including persons with disabilities, non-English speaking persons, and elderly taxpayers. I understand that volunteers are certified to prepare returns at the basic, intermediate, and advanced level, and the IRS prohibits volunteers from preparing returns outside their scope of training.

I have been told by IRS officials that the IRS provides a variety of support to volunteer preparers, ranging from tax law training to tax preparation software to quality review of site operations. While I am not familiar enough with the program to render an opinion about the level of support it needs, if confirmed, I will carefully review this issue.

From my review, these volunteer services are clearly incredibly valuable to the communities that they serve, and I understand that it would be impossible to achieve the same coverage of taxpayers using IRS staff. If confirmed, I will strongly support the use of volunteer services as one part of a multi-pronged strategy for taxpayer service.

- b. How will you ensure that the IRS exercises sufficient oversight of volunteer tax preparation to achieve high rates of accuracy and protections of taxpayer privacy?**

Answer

I believe taxpayers relying on volunteer services should expect high quality, accurate assistance with their tax returns. From my discussions with IRS officials, I understand that the IRS is conducting an analysis of the accuracy of the returns prepared at volunteer sites. If confirmed, I will review this issue thoroughly and adjust the program as needed, based on the results of IRS' analyses.

With respect to privacy, I am aware that all volunteers must sign an agreement that outlines standards of conduct – including protecting taxpayer information. If confirmed, I would look carefully at this aspect of the volunteer program to ensure that appropriate taxpayer protections are in place.

Question 5

Given that the vast majority of our nation's corporate taxpayers are served by the SB/SE Division and are not required to file electronically, what steps would you take to expand e-filing through this taxpayer segment?

Answer

I support efforts to increase e-filing among small and mid-sized businesses and realize it has benefits both to taxpayers and to the IRS. That said, I believe the IRS must carefully consider many factors when trying to increase the rate of business e-filing including the type of business, the capacity of businesses to change their current processes and the resulting costs to the business, and the managerial capacity of the IRS to support business e-file. If confirmed, I will evaluate thoroughly the options for increasing electronic filing in this important taxpayer segment.

Question 6

IRS has made progress in increasing the number of taxpayers who file their tax returns electronically but still receives many returns on paper. In reports on recent filing seasons, GAO has recommended further study of electronic filing mandates or barcoding of computer generated paper returns as options for increasing electronic filing.

- a. To what extent do you agree with GAO's recommendations?
- b. What will you do to implement GAO's recommendations?

Answer

While I am not familiar with all the details of the GAO's study and recommendations, I understand from my discussions with IRS officials that the agency believes that the GAO's recommendations warrant serious consideration. In fact, as noted in my

response to Question 3, I understand the IRS has already begun a study of ways to advance electronic filing that will include direct filing options, mandates, and bar coding of computer generated paper returns. If confirmed, I intend to review the results of that study carefully and consider what additional steps the IRS can take to meet the 80-percent e-filing goal.

Question 7

Currently, in its compliance checking programs (such as computerized matching) IRS limits itself to using a subset of data from all tax returns. For all returns, whether electronically or paper filed, the subset is the selected lines that are transcribed from paper returns.

- a. **To what extent do you believe this practice inhibits the IRS's ability to analyze returns to determine patterns of noncompliance or detect scams and schemes?**
- b. **How much does electronic filing have to increase before it would be worthwhile to transcribe and use all lines off of the remaining paper returns?**

Answer

If confirmed, I will carefully review the types of data the IRS uses to support its compliance programs and evaluate whether there are better ways to capture and employ all the data available to the IRS. My goal will be to ensure that the IRS adopts the most cost-effective and least burdensome methods to obtain and use data contained on tax returns for both compliance and taxpayer-service activities.

As the nominee for IRS Commissioner, I am not currently in a position to tell you how much electronic filing would have to increase before it would be worthwhile to transcribe and use all lines of the paper returns, but if confirmed, I will analyze this issue thoroughly and would be happy to discuss my findings with you.

GLOBALIZATION

Question 8

Multi-national companies and individuals who invest or hide their money offshore place high demands on the IRS to administer the tax laws and identify unreported foreign source income.

- a. **How will you ensure that the IRS isn't outgunned by complex multinational companies and unscrupulous individuals who use offshore accounts to hide their money?**

Answer

From my discussions with IRS officials, I understand that offshore accounts can be among the most complex to investigate and ensure that they are in compliance with the tax laws. As you suggest, some of those taxpayers who use offshore accounts for questionable purposes are quite sophisticated. In order to combat these forces, I would take a multi-pronged approach. First, I would ensure that highly qualified employees are assigned to these cases (with the additional benefit that interesting projects tend to motivate and retain top people). Next, I would engage in dialog with foreign tax administrators, and use existing treaties and information sharing agreements to their fullest extent. Finally, I would use the bully pulpit of the Commissioner's office to make it known that cracking down on misuse of offshore accounts is a priority for the IRS.

- b. 13,000 corporations are headquartered in the infamous Ugland House in the Cayman Islands. What actions will you take to crack down on abusive situations like this so they are not used to avoid US income taxes?**

Answer

I understand from my discussions with IRS officials that there is an on-going GAO study that will make recommendations about these situations. If confirmed, I will study that report carefully and meet with the IRS experts to understand the situation better. With a fuller understanding of this issue and the options available to the IRS, I would be happy to discuss the matter with you further.

- c. What are your views on the merits of a tax system based on worldwide income compared to a territorial tax?**

Answer

I believe that the question of taxation based on worldwide income versus a territorial tax goes to the core of the nation's system of tax administration in a global economy. I understand that the Treasury Department has been examining this issue in some detail. If confirmed, I will review this matter and its implications for tax administration and coordinate with the Treasury Department and Congress on the broader policy issues.

IDENTITY THEFT – PROTECTING TAXPAYERS**Question 9**

Last year, a prisoner told this Committee how easy it was to steal identities and file false tax returns.

- a. What will you do to ensure that taxpayer identities are not misused in the course of tax administration?**

b. How will you assist victims of identity theft so they do not feel like they are being victimized again by the IRS year after year?

Answer

I strongly believe that the American public must know that their data is safe with the IRS. From my review of available materials and discussions with IRS leadership, it is clear that the organization is actively pursuing improved security on numerous fronts, including:

- Implementing secure data transfer procedures;
- Encryption of computers;
- Improved password procedures; and;
- Increased monitoring to enhance the protection of taxpayer information and other sensitive personally identifiable information.

That said, I believe that more work remains to be done. From my personal experience, I know this is a dynamic area in which ever-increasing diligence is needed, penetration attacks and on-line fraud schemes are both growing in number and sophistication.

In my discussions with the IRS officials on this topic, it is also evident to me that it can be very difficult for the IRS to detect a perpetrator who uses a stolen identity in filing a fraudulent income tax return. While I understand that the IRS has a number of tools to detect fraud, it is conceivable that there are no indicators to the IRS that identity theft occurred on a given individual return. I am told that in many instances, the IRS recognizes the fraud only when the legitimate taxpayer files his or her return for that same year. In such instances, I am told that the IRS does notify the taxpayer that their identity information has been compromised.

I also understand that the IRS recently implemented an identity theft victim notification program. In all cases in which the IRS suspects a taxpayer's identity has been comprised, the IRS notifies the taxpayer and offers free credit monitoring services in those cases in which the IRS is at fault. From my experience at FINRA dealing with the broker-dealer industry, I believe this program is in line with what commercial financial sector firms are providing to victims of identity theft.

While positive steps appear to have been taken by the IRS, if confirmed as Commissioner, I would review this program to ensure the IRS is doing all that it should to protect the identities of American taxpayers.

SERVICE**Question 10**

In 2005, I led an effort to prevent the IRS from closing down 70 Taxpayer Assistance Centers. The IRS has been heading in the direction to reduce the opportunities for face to face service and to increase reliance on the web and the telephone for taxpayer assistance.

- a. To what extent do you think taxpayers should have the ability to receive face to face service to get answers to their tax questions? What do you think is the appropriate balance of face-to-face assistance, website assistance, and telephone support?**

Answer

I think taxpayers should have the ability to access the information they need to have their questions answered about the tax laws and what they need to do to meet their tax obligations. Given the advances in technology, I think the way taxpayers want to receive that information is going to vary. And, I think it would be my job as the IRS Commissioner to ensure that the IRS is maximizing the utilization of resources to make sure that taxpayers receive that information in the most efficient means possible.

From my review of the Taxpayer Assistance Blueprint and discussions with IRS senior management, I understand that taxpayer assistance centers (TACs) have historically been an important source of information for many taxpayers. I also understand that despite advances in technology such centers will still be critical to taxpayers in many areas of the country, particularly in rural areas, and to taxpayers who do not have access to computers. If confirmed as Commissioner, I pledge that prior to making any decisions regarding changes to the existing TACs, a thorough analysis will be conducted in accordance with the procedure outlined in the TAB to ensure that taxpayer service is not jeopardized.

- b. Do I have your commitment that you will implement the Taxpayer Assistance Blueprint to provide American taxpayers top notch service?**

Answer

If confirmed as Commissioner, I will not only implement the TAB, but also periodically review it to make sure it remains up to date. I have reviewed the TAB and believe it provides an excellent blueprint on how the IRS should proceed to improve taxpayer assistance.

IRS BUDGET**Question 11**

Mr. Shulman, former Commissioner Everson would never publicly acknowledge that the IRS needed more money than the Administration asked for in its budgets. Yet, the IRS is quick to blame lack of resources when it fails to prosecute identify thieves or to identify non-filers.

- a. How will you work with the Administration to ensure the IRS budget recommendation is adequate?**

Answer

If confirmed, I will be a strong advocate within the Administration for every dollar I think the agency needs to do its job. In reviewing the proposed budget for the IRS for the last three years, I think the Administration has recognized the need for additional IRS resources as it has requested an increase in each of the last three years.

- b. How can I be assured that you will be candid with me and this Committee about the level of resources that are necessary for the IRS to operate efficiently and effectively?**

Answer

I will restate the commitment that I have made to you previously: If confirmed, I will meet with you periodically to discuss candidly IRS, its operations, and the resources needed to do the job.

Question 12

History has shown that the IRS has the expertise to improve taxpayer compliance but lacks the necessary resources. The President's fiscal 2008 budget proposal cites the increased collections of delinquent tax debt from \$34 billion in 2002 to \$49 billion in 2006, an increase of 44 percent. Recently, the IRS confirmed that the agency is continuing to make strides in its collection efforts when it announced enforcement revenue in 2007 surpassed \$59 billion, an increase of more than \$10 billion from 2006. In addition, recent IRS data shows that the Service spent 42 cents to collect each \$100 of tax revenue in fiscal 2006, the third lowest figure in the last 25 years and down from 46 cents in 2005.

Given the ability of IRS employees to efficiently collect outstanding taxes, please discuss whether it makes good business sense to fund the IRS at a level where it can continue to see an increase in revenue?

Answer

Absolutely. From my discussions with IRS senior management, I understand that IRS' return on the dollar for enforcement efforts ranges from 3 to 14 times depending on the program. As I noted in my response to Question 11(a), I am pleased that the Administration has requested increased funding for IRS enforcement in the last three years. I should also note that every organization, including the IRS, has capacity issues. An organization can only withstand so much growth in a given year; it can only hire, train, and put so many people to productive use. I believe that funding should be adequate to help IRS do the job, but not greater than the agency can reasonably handle.

Question 13

As you know, the President will release his budget request for FY 2009 on February 4. As Commissioner, if provided with any additional resources above the president's budget request, where specifically would you use them?

Answer

If confirmed, one of my top priorities will be to review the IRS' current funding and the budget request for FY 2009. Once I have a complete understanding of the inner workings of the IRS, I will be able to offer an opinion on where any additional funding that Congress might provide could be put to optimal use.

MODERNIZATION**Question 14**

Describe how you were able to modernize technology at the NASD and how you can use your experience to modernize the IRS.

Answer

I arrived at NASD (now known as FINRA) soon after it had outsourced nearly all of the technology development and operations and had suffered some visible technology difficulties.

I focused my attention in a few key areas. First, I recruited new leadership to the technology organization with the experience and skills in building and maintaining large-scale technology systems. I also ensured that we had the appropriate level of in-house expertise to oversee contractors effectively, and deal with problems that inevitably come up in large-scale technology development.

Next, I focused on building a shared commitment and clear set of goals and objectives among the business and technology leadership. For high priority projects, we assigned

some of our best business people to work side-by-side with the technologists to ensure that the project remained aligned with the needs of the business. I also made clear to everyone involved that large-scale technology projects are a team effort, and not just the responsibility of the information technology organization. Business executives were given shared accountability for delivery, and held accountable for the success or failure to deliver.

I worked hard with my colleagues to create a culture that encouraged open, honest dialogue, quick escalation of problems, and focus on continuous improvement and problem resolution, rather than a focus on blame.

And finally, I oversaw a multi-year program to enhance the protection of sensitive market and individual data at FINRA. Today, all FINRA laptops are encrypted, and strong policies and procedures are in place to protect information.

Question 15

What criteria will you use to establish priorities for technology project – there is so much to be done and the IRS budget isn't going to support them all. What projects do you consider to be priorities?

Answer

The criteria that I would establish for technology projects must be tied to the overall priorities for the IRS. As I said in my testimony, my experience has been that technology projects go awry when the business and technology priorities are out of sync. Therefore, we must have the discipline to candidly assess the merits of all technology projects in light of the overall priorities, and allocate resources accordingly.

At the NASD and FINRA, some of the key criteria we used to select IT projects included:

- Business priority and value
- Financial return on investment
- Risk of implementation
- Adherence to the Enterprise Architecture
- Development of capabilities that can be leveraged by other projects

Based on my discussions with IRS leadership, I believe the current selection criteria used by the IRS are similar to what I have listed above. If confirmed as Commissioner, I would review these criteria carefully and work with IRS leadership to revise them as appropriate, bringing my previous experience to bear.

Regarding which projects would be priorities, I refer back to my testimony at my confirmation hearing at which I stated that my goal for modernization is to ensure IRS employees have real-time access to current taxpayer data both to serve the taxpayer

better and to support enhanced compliance activities. As such, based on my initial understanding of the IRS' current projects, the Business Systems Modernization (BSM) portfolio appears to remain of utmost priority. I understand that modernized e-File will enable electronic filing of all major IRS form types and provide the data to the IRS in a manner that it can be used more easily than either via paper filing or the legacy e-file system. I also understand that the Customer Account Data Engine (CADE) will replace the antiquated master files and provide taxpayer data that can be accessed and updated on a real-time basis. Finally, I understand that the Accounts Management Services (AMS) project will provide the tools necessary for real-time access and update of taxpayer data. While I will need to conduct my own thorough assessment of these projects, they appear to be the appropriate priorities for the IRS.

Question 16

What will you do to get IRS technology projects like CADE back on track?

Answer

As I more fully address in Question 20 below, there are certain principles to ensure success in delivering large-scale IT projects. First, there must be a well-articulated set of business objectives for the project. All stakeholders, including the users of the system and the IT organization, must agree on those business objectives from the outset. Second, the organization must implement a robust and mature set of project management standards and tools to ensure a highly disciplined and comprehensive approach is used to manage all aspects of the project. For example, a mature requirements management process is essential to ensure that the project develops a complete and detailed set of requirements that will meet those business objectives. Finally, the project must have the proper personnel management and governance to clarify authority and accountability at all levels of the organization. People must understand their role and be held accountable for their performance.

With regard to CADE, it is clear to me that IRS senior management is committed to, and focused on, its delivery in a timely fashion. I have been told that the IRS has taken a number of specific steps to address issues in the CADE project, and while these steps do not guarantee success, I believe they show continuing maturation of the IRS development process. If confirmed, I will support continued improvements to these project management disciplines and work to extend them to all of IRS' IT projects. I also expect to make my own assessment of CADE and work with the senior leadership of IRS to make any changes that are warranted.

Question 17

What are the security risks when data, including taxpayer information, is sent off-site, handed over to a contractor or given to a subcontractor?

Answer

Data security is a rapidly evolving issue, in both the private and public sectors. I believe that contractors and subcontractors must be held to the same data security standards as the IRS itself. I know from first-hand experience that data security risks can come in a variety of forms – external threats to information technology such as hacking, employee misuse of media or paper-based data, data loss through mishandling of media or paper-based data, and other risks. From my review of this subject, I understand that the Office of Management and Budget and Congress have made it clear that there should be no distinction between the amount of data protection in place for government-operated systems and those operated by contractors – a standard I fully support. I also believe contractors and IRS employees must be held to the same high ethical standard regarding disclosure and privacy of data.

Ensuring information technology security and protection of taxpayer information will be a high priority if I am confirmed as Commissioner. Clearly this extends beyond the boundaries of IRS itself, but to the other government agencies and contractors that are entrusted with taxpayer and other sensitive data. If confirmed, I will thoroughly review current security programs and ensure a comprehensive security program encompasses all of the organizations and contractors with which the IRS has a relationship.

Question 18

What is your strategy for strengthening the security over the agency's computer systems?

Answer

As I explained in my response to Question 9 above, computer and information security is of paramount importance to the IRS and the country. Confidence in the tax administration system is critical to the American public, which entrusts the IRS with the safekeeping of their tax information. From my discussions with IRS officials and review of available information, I know this is an area of focus for the IRS. Nevertheless, as threats continue to evolve, there is more work to be done.

As I have learned in my work at FINRA, ensuring security must be top-of-mind for all employees. At the IRS, security must be an essential ingredient in all work processes and systems, not viewed as an afterthought. When new systems are designed and developed, the information security requirements must be identified at the start, and tracked and tested with the same rigor as core business requirements. This is the culture of security that must exist at the IRS, and if confirmed as Commissioner, I will work to ensure such a culture is developed and maintained.

The other key aspect of information system security is constant online monitoring. All IT assets, including both hardware and software, must be constantly monitored for penetration attacks, viruses, and other forms of malware. Maintaining the latest

versions of systems and ensuring security patches are implemented timely is critical. I recognize that the challenge for the IRS' security posture is that it is only as good as its weakest point. A comprehensive monitoring program of all IT assets in the enterprise is essential for success. As Commissioner, I would make it a high priority to ensure that such comprehensive monitoring is in place.

Question 19

The previous commissioner met with the modernization contractor on a monthly basis. Will you continue these regular meetings in order to keep this critical program on track?

Answer

If confirmed, I will meet regularly with senior IRS officials responsible for modernization, as well as contractors.

Question 20

How will you ensure that that modernization needs are adequately identified, that contracts are sufficiently detailed to establish contractor accountability and sufficient IRS oversight is conducted so that modernization projects are completed timely, accurately and reliably?

Answer

Over the past seven years at the NASD and now at FINRA, I have had responsibility for information technology, including the implementation of large-scale information technology projects. During that time, I have seen how difficult it is to deliver large-scale IT projects on time and within budget, and provide the business value initially promised. In my experience, it is easy to underestimate the complexity in providing the new promised functionality, both in terms of the new system itself, and the interfaces with other existing systems in the enterprise. This would be especially true at the IRS, where one must deal with an exceptionally complex tax code and an IT environment consisting of hundreds of legacy systems.

That said, there are certain principals to ensure success in delivering large-scale IT projects. First, there must be a well-articulated set of business objectives for the project. All stakeholders, to include the users of the system and the IT organization, must agree on those business objectives from the outset. Second, the organization must implement a robust and mature set of project management standards and tools to ensure a highly disciplined and comprehensive approach is used to manage all aspects of the project. For example, a mature requirements management process is essential to ensure that the project develops a complete and detailed set of requirements that will meet those business objectives. Finally, the project must have the proper personnel management and governance model to clarify authority and accountability at all levels

of the organization. People must understand their role and be held accountable for their performance.

From my review of available materials and my discussions with IRS leadership, it is clear that the IRS has improved its ability to manage large-scale IT modernization projects. The IRS admits, and I concur, that the agency is still not fully mature in all project management processes, including areas such as contract, performance, and configuration management. If confirmed, I would build on the successes that the IRS has achieved to date, and ensure that the IRS continues to drive improvements in all areas of IT program and project management.

Question 21

With limited technology funding, how will you determine which proposed IRS modernization and updating projects will be funded?

Answer

As I stated in my response to Question 15 above, the criteria used to rank and select technology projects is an integral part of a solid modernization program for any business that is highly reliant on technology. And I know that when it comes to IT, demand always outstrips supply. In my response to Question 15, I set out some of the key criteria we used at the NASD and FINRA, which I understand are similar to those currently in use at the IRS. If confirmed as Commissioner, I would review these criteria carefully and work with the team to revise them as appropriate, bringing my previous experience to bear.

Question 22

What do you believe are the long-term risks to IRS's modernization that you will have to deal with and what are the consequences if they are not successfully managed?

Answer

For the IRS to improve its productivity and overall effectiveness significantly, modernization of its administrative and IT systems is a necessity. Therefore, if confirmed, one of my highest priorities as Commissioner would be to ensure the organization is effectively addressing the key risks that can endanger its modernization efforts. From my discussions with IRS senior management, I understand that the key long-term risks to modernization include:

- Replacement of master file systems that were designed in the 1960s;
- Modernizing very complex and interrelated legacy systems; and
- Managing the loss of the key IT personnel with knowledge of IRS critical legacy systems.

IRS modernization is critical to supporting key IRS business objectives in both enforcement and taxpayer services. Therefore, the consequences of not managing IRS' modernization risks effectively are that IRS may not be able to fully execute its long-term enforcement and taxpayer services plans.

IRS WORKFORCE

Question 23

Last year, Senator Grassley and I went to IRS headquarters and visited with Commissioner Everson and senior IRS leaders. I was disappointed by the lack of enthusiasm and excitement among IRS executives to find ways to improve tax administration. If IRS senior leaders are not excited, I don't see how the 100,000 IRS employees will be excited about serving American taxpayers, either.

- a. How would you instill a sense of enthusiasm into IRS senior leadership? Into employees ranging from New York to California and all points in-between? How do you make them care?**

Answer

Actions, not words, are critical. I believe that employees are enthusiastic when they have a leader who is engaged, willing to set clear priorities, make difficult decisions, and learn from mistakes. If confirmed, I would commit to an open two-way dialog with the employees and do everything in my ability to create an environment where people feel motivated and engaged by their work.

I also believe that the experience that employees have with their direct managers greatly influences their daily outlook about their employer. When employees have excellent managers, they usually enjoy their work and do good work. When employees have ineffective managers, they often feel trapped and become disengaged. If confirmed, I will make it a priority to support the good managers at the IRS and bolster the management ranks of the IRS through a combination of training, professional development, and recruiting of new talent where needed.

Finally, I truly believe that the work of the IRS is immensely important. As I said in my testimony, how the IRS approaches its work, and interacts with taxpayers, greatly affects both the functioning of the federal government, as well as Americans' overall view of their government. The IRS touches every adult, every business, and every non-profit organization in America. For many citizens, it is the only federal agency with which they will have contact in a given year. If confirmed, I will communicate my belief that each employee can make a difference in the lives of the American people, and try to connect employees' daily work with a larger mission.

- b. How will you encourage and reward IRS employees for thinking innovatively and being willing to try new ways to improve tax administration?**

Answer

If confirmed as Commissioner, I will set a clear "tone from the top" that for the IRS to succeed, the workforce needs to be engaged and contributing above and beyond business as usual. I would make direct employee outreach a regular part of my schedule, and I would challenge the IRS' senior executives to ensure that they are capturing the best of their employees' thinking on ways to improve tax administration.

- c. Many IRS employees will be eligible to retire within the next 3 to 5 years. This could create a real "brain-drain" that could have a detrimental effect on tax administration.**
- i. What will you do to encourage IRS staff to stay on the job past their eligibility date?**
 - ii. How will you attract high quality employees to come to work at the IRS to replace those who do retire?**
 - iii. How will you retain new hires so the IRS doesn't spend its resources to become nothing more than a good training ground, only to see new staff leave within a few years?**

Answer

I believe the key to retaining the best people at the IRS is making the IRS a great place to work: a place where people are challenged, supported, respected, held accountable, and given opportunities to grow personally and professionally. Making the IRS one of the best places to work in the government, while developing the next generation of IRS leaders, would be major themes of my tenure if I am confirmed.

I understand that the IRS has a number of programs in place to retain key personnel, and I plan to review those programs. I understand the IRS has developed a recruitment program that provides the IRS with access to a wide range of potential employees, including individuals entering the workforce for the first time, seasoned individuals looking for new challenges, and retirees looking to rejoin the workforce.

Question 24

IRS staffing has fallen from 112,000 in 1995 to just 91,000 in 2006, a decrease of nearly 20%. During this period, revenue officers and revenue agents - two groups critical to reducing the tax gap - have shrunk by 30 and 18 percent respectively. Former IRS Commissioner Rossotti called for a 2% increase in staffing per year

and steady increases in funding for modernization for several years to build the IRS workforce back up and to improve tax administration.

- a. Do you agree with Commissioner Rossotti's proposals for increasing staffing and funding?**

Answer

Until I am confirmed and have an opportunity to look closely at the IRS' staffing needs, I am unable to offer an opinion on what the appropriate or desired level of staffing should be. I assume that technology tools have advanced significantly since 1995, and without knowing more about the nature of the IRS staff, I am hesitant to say that the agency should return to the staffing levels of that or any year. Beyond the issue of knowing the specific staffing level increase, I do think Commissioner Rossotti's recommendations reflect a couple of realities. First, staffing cannot be built overnight. It will take time and is a gradual process. And second, if there is a need to rebuild staffing or any other aspect of the IRS budget, it must be done carefully and within the capacity of the IRS to handle and make productive use of the increase in any given year.

In addition, for the IRS to improve its productivity and overall effectiveness significantly, I believe it is essential that the IRS modernize its administrative and IT systems. Therefore, one of my highest priorities as Commissioner, if confirmed, would be to ensure the organization is effectively addressing the key risks that can endanger its modernization efforts.

- b. What strategies will you pursue to address the gap between IRS's capacities and responsibilities?**

Answer

One of my most important jobs, if confirmed as IRS Commissioner, will be to make an overall assessment of the resource needs of the agency for such things as money, people, and technology. Such an assessment requires a constant reassessment of where the organization stands as opposed to where we want it to be, with necessary adjustments along the way. For example, as certain issues are addressed, other needs will change and must be adjusted accordingly.

I also envision doing a capability assessment for each of my top priorities. Once we have a vision and a goal to achieve, I will work with the IRS senior management to assess what capabilities the IRS has, what capabilities it does not have, and develop a plan to close that gap.

- c. To what extent have these staffing reductions hampered Service efforts to close the tax gap?**

Answer

Without being inside the agency and looking closely at its staffing needs, it is impossible for me to know what areas are deficient and to what extent, if any, this has hampers the IRS' efforts to reduce the tax gap. I understand that In FY 2002 the IRS collected \$34 billion in enforcement revenue, and by FY 2007, that had grown to over \$59 billion. In addition, I am told that the IRS spent 42 cents to collect each \$100 of tax revenue in fiscal 2006, the third lowest figure in the last 25 years and down from 46 cents in 2005. My review of the available information related to the tax gap suggests that the best ways to reduce it is by increased third-party reporting and by improved transparency. That would give the IRS more tools to utilize and leverage the existing employee base.

- d. Describe your long-term and short-term strategies to determine optimal staffing levels for the IRS, and to achieve them.**

Answer

I think the IRS need to continue to expand its enforcement staff at a rate that allows the agency to train new hires adequately to be most effective. I also think the IRS needs to look at enforcement staff within the overall resource allocation of the agency. Additionally, I believe that the IRS needs to have an appropriate return on investment in both services and enforcement, and that should be a factor in determining the appropriate staffing levels. It is my understanding that the IRS has established a high rate of return for enforcement activities. As long as the IRS can maintain such a high rate, it makes sense to continue to hire additional enforcement personnel.

Finally, I think it is important that the IRS' enforcement efforts be carried out in such a way continues to recognize the IRS' dual role of enforcing the tax laws and providing taxpayer service.

- e. During times of budget shortfalls, budgets for planned hiring often are raided to pay for unanticipated or excessive costs. To what extent do you consider this an acceptable trade-off? What are alternative ways to cover costs that will not have such a long-term detrimental effect on the agency?**

Answer

Resource allocation tradeoffs are a reality of tough budget times, and I am under no illusion that IRS will be exempt in any way. From my previous positions, I understand that output will be affected depending on how resources are allocated. I view my job in such a situation to be managing the resources – all the resources not just people – that are available to me in a manner that achieves the most productive result. This may not always result in a reduction in planned hiring, but it might if it is known that there will also be a lack of resources to train the new hires and get them into the field for productive use.

Also, as we have discussed, I believe a key job of a leader is to remain focused on a long-term vision, even when there are short-term imperatives that must be met. A key goal of mine, if confirmed, would be to keep investing in the long term even in tough budget times.

Question 25

According to IRS data, while the number of employees at the IRS has decreased by almost 20,000 since 1995, the number of managers who supervise these employees has increased over this same period. During the period between 2000 and 2005, the number of bargaining unit employees, the frontline employees who do the work, decreased by 4,756, a decrease of 5.1%. During that same time, the number of managers and management officials increased from 12,514 to 12,684, an increase of 170, an increase of 1%.

- a. Why would the IRS need more managers today than it needed six years ago when it now has 4,700 fewer front-line employees?**
- b. Describe any plans you have to study the IRS workforce to determine strengths and weaknesses, as well as optimal staffing levels.**

Answer

As a nominee, I have not had the opportunity to review data regarding the mix of IRS employees and managers, so it would be premature for me to offer an opinion on the concern you raise. I can say that one principle I follow is that resources need to be aligned with priorities, and this includes human resources. If confirmed, one of my jobs will be to assess if resources are distributed properly to meet the mission, and I plan to do so. However, I have found in my experience in the private sector that traditional models of workforce distribution may no longer be effective, and a more agile staffing model is needed that can quickly change to meet new business requirements stemming from advancements in technology or other new developments.

PREPARER OVERSIGHT

Question 26

Approximately 60% of the 135 million individual tax returns are prepared by paid preparers. Volunteers prepare several million more. The Government Accountability Office and the Treasury Inspector General for Tax Administration have reported shortcomings in IRS oversight of tax preparers. Only 25% of Electronic Return Originator applications are subjected to FBI checks that take only a few minutes to complete.

- a. How will you encourage preparers to maintain high standards of accuracy and ethics?
- b. What actions will you take to ensure that the IRS conducts adequate oversight of preparers and provides sufficient support to volunteer preparers?
- c. To what extent do you support legislation that would establish competency and ethics standards for preparers?
- d. Do I have your commitment that you will work with me to develop responsible legislation and that you will make implementation of good government legislation a priority?

Answer

I believe that taxpayers deserve to get knowledgeable, professional, and honest service from preparers. I understand that the IRS already has a variety of tools at its disposal to ensure that these high standards are met, including the bully pulpit, education, dialog, and outreach, and where appropriate fines and disciplinary actions.

I am intimately familiar with registration and regulation of professional service providers in the financial services industry. If confirmed, I would give careful consideration to the issues surrounding the registration and regulation of preparers.

Regulation has clear benefits, but it also comes with costs. Regulation puts an additional burden on preparers, especially those who are already capable and ethical. It also imposes industry-wide costs, which inevitably would be borne by taxpayers. Before mandating regulation, I believe we need to ensure that the benefits in terms of improved compliance outweigh the costs and burdens that such regulations would impose. Finally, regulation of tax preparers would require IRS senior management attention and financial resources that would otherwise be devoted to other aspects of tax administration, namely taxpayer service and enforcement.

If confirmed, I will consider all of these issues with an open mind, and I look forward to the opportunity to study the issue further.

IRS RESTRUCTURING COMMISSION

Question 27

Mr. Shulman, you worked on the IRS Restructuring Commission. You were in a position to study the IRS, identify problems and design solutions.

- a. To what extent did the recommendations of the Restructuring Commission and the legislation that followed improve tax administration?**

Answer

At the time when the Restructuring Commission was doing its work, the IRS was under tremendous criticism for the way it was perceived to treat taxpayers and for its lack of quality service. I believe that both the recommendations of the Commission and the legislation that followed set the stage for a better system of tax administration, one that Americans can believe in and trust. Furthermore, I think the IRS has made tremendous strides over the intervening years in treating taxpayers much more fairly and in providing better service to taxpayers generally. That is not to say that there is not room for more improvement, and if confirmed, I will strive to make sure the IRS stays on the path to improvement in these areas, as well as maintaining a robust enforcement presence.

- b. In retrospect, would you change any of the recommendations? Which ones, any why?**

Answer

I do not know that I would change any recommendations per se, as the Commission did consider many of the issues that are at the forefront today, such as IRS workforce, modernization, electronic filing, taxpayer rights, and financial accountability. However, I continue to believe that the Commission did the right thing by highlighting tax-law simplifications as an essential element of a better tax administration system.

- c. Please comment specifically on the results of dividing the IRS compliance operations into four operating divisions. To what extent is this structure effective? To what extent is it inefficient?**

Answer

I think that creating the four operating divisions made sense because it focused the IRS better to its customer base. For example, concentrating IRS expertise into an organization that deals with complex business issues (LMSB) or tax-exempt organizations (TEGE) just makes good business sense. I am sure there were many startup issues, and there may be room for improvement today regarding how compliance issues are handled among these four organizations. However, this is something I will be able to consider and, perhaps improve if I am confirmed.

- d. Were there any recommendations made that were not adopted that you think are good ideas and should be pursued? What are they?**

Answer

As I noted above, I still believe tax-law simplification would benefit tax administration.

e. What do you consider your major contribution to the Commission?

Answer

I hope, and believe, that I contributed as a valuable staff member. I am certainly proud of the report that the Commission produced and its subsequent impact on IRS restructuring and reform legislation.

f. How will you apply the knowledge you learned about the IRS during your tenure on the Restructuring Commission to the job of IRS Commissioner?

Answer

My work on the Commission staff gave me valuable insight into the IRS, as well as its wide and varied constituents. I certainly learned a great deal about the IRS generally and, though the IRS has changed quite a bit in the last 11 years, this knowledge will help me to get my feet on the ground if I am confirmed.

TAX REFORM

Question 28

Implementing fundamental tax reform would be one of the primary challenges you face as Commissioner. How would you address these challenges, for example ...

a. How would you train IRS staff on a timely basis so they can accurately apply changes to the law?

Answer

Training would be an important theme under my leadership if I am confirmed. While at FINRA, we confronted similar challenges in developing and maintaining a high level of specialized expertise among the workforce as there were rapid changes in the financial-services industry. We established "Examiner University" – a comprehensive training program for new examiners that combines intensive classroom instruction with mentoring and on-the-job training. We also enhanced the level of training available to experienced staff members. I would envision a continued focus and emphasis on training for IRS employees – new recruits and experienced staff alike.

b. How would you motivate IRS employees to embrace fundamental change?

Answer

I believe that people are motivated and engaged in change when they have a clear sense of goals and objectives, and believe that they are contributing to something larger than themselves. If confirmed, I would clearly articulate a vision for the future, and work with IRS executives to connect that vision to the day-to-day realities of the IRS workforce.

c. What measures would you take to ensure that computer systems and IRS processes are updated timely and accurately?

Answer

If there were tax reform, it would be important that the IRS had a seat at the table so that it could anticipate as early as possible what system and process changes would be required. With respect to ensuring that systems are updated timely and accurately, as I stated in my responses to earlier questions, there are certain principles to ensure success in delivering large-scale IT projects. First, there must be a well-articulated set of business objectives for the project. All stakeholders, including the users of the system and the IT organization, must agree on those business objectives from the outset. Second, the organization must implement a robust and mature set of project management standards and tools to ensure a highly disciplined and comprehensive approach is used to manage all aspects of the project. Finally, the project must have the proper personnel management and governance model, to clarify authority and accountability at all levels of the organization. People must understand their role and be held accountable for their performance.

In the case of tax reform, it would be important that the IRS adhered to these disciplines and ensured that its operations met the timelines of reform.

d. What measures would you take to minimize burden on taxpayers?

Answer

If tax reform were to occur, I would take a multi-faceted approach to minimizing the burden on taxpayers. Publishing clear and timely guidance, providing top quality taxpayer service, and continuing to enhance the IRS website are all important parts of the approach. If confirmed, I would also make maximum use of the IRS Office of Taxpayer Burden Reduction as a means of reducing the paperwork burden on individual taxpayers and small businesses. I would also look forward to working with Congress and the Administration as they craft legislative proposals, informing them how they could make it easier for taxpayers to comply. There have been a number of positive

suggestions and programs coming out of the Taxpayer Assistance Blueprint, the IRS/Treasury report on reducing the Tax Gap, and other studies.

- e. How would you prioritize the needs for legal guidance so taxpayers can understand how the IRS is going to administer reforms?**

Answer

Providing clear legal guidance is a critical function of the IRS and the Treasury Department, and I believe there should be an open dialog between them and the Congress, especially where there are difficulties in providing guidance on matters of great importance to taxpayers. Involving tax experts from IRS early and completely in the tax reform legislative process could reduce the amount of time it takes to publish immediate guidance and to implement legislation.

TAX GAP

Question 29

Where would you rank the tax gap among all of the challenges you will face at the IRS?

Answer

The tax gap would be one of my top priorities and challenges if I am confirmed as IRS Commissioner.

Question 30

The annual tax gap is \$345 billion. To what extent do you think that it is acceptable that \$345 billion dollars go unpaid each year?

Answer

I share your view that the tax gap is of great concern and has the potential to undermine the effectiveness of the nation's voluntary tax system.

Question 31

What is your assessment of the accuracy of the IRS estimates of the size of the tax gap and the distribution of the tax gap among non-filers, underreporters and underpayers? Discuss any flaws in methodology or information gathering that may affect accuracy.

Answer

At this point, I am not in a position to assess the accuracy of the estimates of the size or composition of the tax gap.

However, as the IRS study points out, additional research is needed to improve estimates of taxpayer compliance. For example, the report points out that the last time that the IRS conducted an S corporation study was in 1984. I understand that an updated S corporation study is ongoing, and if confirmed, I will ensure that this and other important research studies are completed. I believe that better research will inform and improve IRS efforts to combat non-compliance across the different types of taxes and taxpayers.

Question 32

The IRS estimates the current rate of voluntary compliance is 83.7% - it's been in that ballpark for many years. In 2004, and again in 2007, I set a goal for 90% voluntary compliance.

- a. What are your thoughts on the current rate of voluntary compliance? Do you think 83.7% is an acceptable rate? What should it be?**

Answer

As I stated during my confirmation hearing, I do not believe that I am in a position to know what level of compliance is the right one. The IRS' report on the tax gap notes that compliance levels appear to have hovered around the same rate for decades. For example, based on data from the 1960s through the 1980s, the IRS estimates that the compliance rate has moved within a range of two percentage points and was virtually the same in tax year 2001 as it had been in tax year 1985. I am hesitant to commit to a specific target because I believe it would be premature for me as a nominee to make pronouncements on fixing a decades-old problem without time for in-depth discussion and planning.

- b. Do you think it's fair for those who pay what they owe, on time, to shoulder the tax burden for those who choose not to comply?**

Answer

No.

- c. To what extent do you think 90% is a realistic goal?**

Answer

As I stated above, I am not in a position as a nominee to offer an opinion on a realistic goal.

d. To what extent do you think 90% is achievable?

Answer

I would imagine that such a goal could be achievable, but the IRS alone does not have all of the tools needed to achieve it. I also believe that to achieve such a goal, we would need to understand that it would likely require a significant change to the relationship between taxpayers and the IRS and impose extensive new burdens on both compliant and non-compliant taxpayers.

e. What are the five primary actions you would take to improve the voluntary compliance rate?

Answer

Rather than addressing this separately, I would say that I support the multi-pronged strategy outlined by the IRS and Treasury Department in 2006 to address the tax gap. I believe that a combination of – among other things – legislative changes, enhanced taxpayer service, increased enforcement activities, improvements in IRS technology, and better research are all critical parts of this long-term initiative.

In addition, as I offered in my confirmation hearing, I would bring a fresh set of eyes to the issue if I am confirmed. One area worth significant study and consideration is increasing third-party information reporting, which may be particularly relevant in the area of sole proprietors. The IRS tax gap report identifies sole proprietors as a significant area of underreporting, and the research shows that compliance increases as third-party information reporting increases. With that said, I am aware that there are potential downsides to increased reporting, in that it may increase the burden on compliant taxpayers. This is clearly an area worth exploring, and one that will require continued discussions among the IRS, the Treasury Department, and Congress, given its broad ranging policy implications.

Question 33

Last year, I asked Treasury and the IRS develop a comprehensive and credible plan to reduce the tax gap. The plan was delivered in August of 2007.

a. Have you read the plan? What is your assessment of the plan?

- b. Describe how you will ensure that the plan is fully implemented and that the IRS follows through on the plan. How will you make sure the plan isn't "forgotten" after a year or two?**
- c. How will you measure whether the IRS is making progress on reducing the tax gap?**

Answer

I have studied the plan quite closely, and I think it significantly advances the dialog around the tax gap. There are a number of excellent proposals and initiatives outlined in the report. If confirmed, I would immediately begin a review of the recommendations to understand where the IRS stands with implementation, prioritize key initiatives, and determine what resources would be needed to execute against those initiatives.

If confirmed as Commissioner, this issue will be one of my top priorities. Reducing taxpayer non-compliance should and will infuse everything that the IRS does, and I will hold those responsible for specific initiatives accountable for performance.

In particular, I agree and support the recommendation of the IRS' tax gap report to use research as a foundation for establishing benchmarks of performance. While benchmarks are never perfect, they are incredibly helpful in objectively assessing performance over time.

Question 34

Will you give me your commitment that you will make 90% voluntary compliance a top priority?

Answer

Raising the level of voluntary compliance will absolutely be a top priority for me if I am confirmed. As outlined in the IRS tax gap report, significantly raising the level of compliance will need to be a coordinated effort among the IRS, the Treasury Department, and Congress. You have my commitment that I will be a willing partner in effecting change, and in engaging in honest dialog about how to achieve our shared objectives.

Question 35

Will you commit that implementation of the Tax Gap Plan will be a top priority, and that you will regularly keep me apprised of the IRS's progress to reduce the tax gap and improve compliance?

Answer

Yes.

Question 36

A significant part of the tax gap is due to noncompliant sole proprietors. GAO recently identified [Tax Gap: A Strategy for Reducing the Gap Should Include Options for Addressing Sole Proprietor Noncompliance, GAO-07-1014] options in several categories that could improve sole proprietor compliance. The categories included simplifying record keeping and reducing complexity, enhancing and expanding information reporting of income, and expanding information reporting of expenses. In response to GAO, Treasury said that GAO's options provide valuable insights for the administration's tax gap strategy.

- a. Which options have the most promise?
- b. What will you do to help implement them?

Answer

I am generally familiar with the GAO report and understand that it included an approach to address the tax gap problem with sole proprietors. From my perspective, I think the problem with the high levels of noncompliance by sole proprietors is a function of two factors. First, due to the complexity of our tax laws, sole proprietors may not understand fully their tax obligations. I am aware that IRS has a number of programs in place that are designed to help sole proprietors and other small businesses as well as the tax practitioners that serve them. If confirmed, I will examine these programs more closely to see if they need to be expanded further or redirected. The second problem is the relative lack of transparency and third-party reporting of the transactions conducted by sole proprietors. From my review of the public information related to the tax gap, it is clear that the levels of compliance are higher in instances where there is third-party reporting. I understand that the Administration has made some legislative proposals to increase reporting, and I believe enactment of these proposals would improve the IRS' ability to verify small business transactions. In addition, I believe the IRS, the Treasury Department, and the Congress need to look at other ways to increase third-party reporting with respect to sole proprietors and small businesses.

RESEARCH

Prior to 2006, it had been approximately 18 years (1988) since the IRS measured compliance through its Taxpayer Compliance Measurement Program. In 2000, the IRS established the National Research Program to identify major areas of individual and business non-compliance. The program has completed an initial reporting compliance study of Form 1040 taxpayers and is close to completing a study of Form 1120S filers. One of the findings of the early study was the high

non-compliance of small business owners. However, other important segments, such as large and small corporate taxpayers, have not been updated.

Question 37

What importance will you place on the National Research Program?

Answer

From what I understand from talking with IRS officials, I think the NRP is a critical component to assist IRS in better understanding taxpayer compliance. From reading the IRS' tax gap report, it appears that the NRP was able to develop innovative ways to collect the information needed without the burdensome audits that had previously been conducted under the Taxpayer Compliance Measurement Program. Based on this information, I would place a high importance on the NRP, and if confirmed, I would want to see it continue.

Question 38

Will you make it a funding priority despite the cost?

Answer

If confirmed, I intend to make research a funding priority within the context of the overall IRS budget.

Question 39

Do you think IRS is devoting enough of its resources to compliance research?

Answer

From talking with IRS officials, I understand that the NRP is a critical component of the IRS' understanding of taxpayer compliance. Based on available information and my own inherent belief in the need for quality research to make important decisions, I would consider the NRP to be of critical importance to the IRS, and if confirmed, I would want to see it continue. I can only reiterate my strong support for research especially in the IRS where there is an essential need to understand better the reasons for noncompliance.

Question 40

Do you consider current funding levels sufficient? If not, why not, and what funding levels would you consider sufficient?

Answer

Please see my response to the previous question. Without looking carefully and thoroughly at the IRS budget and specifically at compliance research, I am unable as a nominee to offer an informed opinion on whether the level of resources being devoted is appropriate. However, I recognize a strong need for compliance research within the agency.

Question 41

How many resources would you devote to compliance research activities?

Answer

As noted in my responses to Questions 39 and 40, I cannot offer an informed opinion as a nominee on the level of resources I would devote to compliance research without more in-depth analysis of resource allocation at the IRS and the context of compliance research in that overall allocation. However, I recognize a strong need for compliance research within the agency.

Question 42

What other areas of non-compliance should be priorities for future study?

Answer

As I mentioned in response to Question 37, I understand that the IRS is now undertaking annual compliance studies of individual taxpayers. I am told that the IRS is also nearing completion of a study of Form 1020S filers. With respect to other areas of non-compliance, I think the IRS needs to take an even closer look at sole proprietors given the significant contribution they make to the tax gap. I also think the IRS should have appropriate research on compliance among all taxpayers, and not just filers of Form 1040 or Form 1120S. However, I am not sure, without looking into this deeper and discussing it with the appropriate IRS officials, what the appropriate manner would be to conduct this research (i.e., whether it would fit within the context of an NRP study).

Question 43

How regularly should research studies be conducted to measure noncompliance?

Answer

Compliance research is critical information, and ideally I would want the latest data as soon as possible. Also, I would imagine that information about trends is as important as the raw data itself. I think most people find it hard to believe that the latest data the IRS

has on individual taxpayer compliance is from Tax Year 2001. That is why I salute the IRS' current effort to sample smaller groups of taxpayers over several years to develop a timelier estimate of compliance information. If confirmed as Commissioner, I will look at other ways the IRS can improve the timeliness of the compliance information.

FINANCIAL MANAGEMENT

Question 44

IRS continues to face many challenges in its ongoing efforts to improve the accuracy and reliability of its financial and information management systems and correct internal control weaknesses. For example, despite notable progress and despite having received clean, or unqualified, audit opinions on its financial statements for many years, financial management at IRS has been on GAO's high-risk list since 1995, first as a separate issue and later as a component of the IRS Business Systems Modernization high risk area. Although IRS again received an unqualified audit opinion on its financial statements in 2007, it continues to need to manually analyze and correct data generated by its financial systems. This approach does not produce timely information for managing the agency.

- a. What are your views on the need for IRS to modernize its financial management systems, and do you view this as a high priority for the agency?**

Answer

I am committed to moving forward with the modernization of the IRS financial management systems to address the issues in the GAO reports you referenced. I believe it is a high priority for the IRS to have strong financial management controls to ensure the integrity of its financial statements.

- b. When can we expect to see the kinds of changes implemented that will enable GAO to remove financial management at IRS from its high-risk list?**

Answer

I understand that the IRS has a plan in place to address this issue, and I am committed to moving forward to modernize the IRS financial management systems if confirmed. I also understand that the GAO provides updates on the status of IRS financial management system improvements in its annual audit report.

PERFORMANCE MEASURES**Question 45**

According to past GAO work, IRS needs to ensure that it has comparable performance measures over time and sufficient data to assess performance. IRS needs to routinely evaluate its programs to identify ways to improve their performance.

What is your strategy to help ensure that IRS managers acquire sufficient data to assess performance and routinely evaluate performance to make continuous improvements in programs?

Answer

In my experience as an executive in the private sector, goals and measures are incredibly powerful tools. In order to change behavior and achieve continuous improvement, managers and their employees need to understand clearly how their performance is being judged, and what behaviors are most rewarded.

If confirmed, I plan to conduct a review of measures in place at the IRS today and make sure that they are aligned with the priorities of the IRS as a whole. In so doing, I plan to engage a wide array of employees in this review because above all else, the measures must be clear, and they must engender the desired behavior.

**Senator John F. Kerry
Questions for Douglas Shulman**

Question 1

In 2004, citing a proliferation in the use of electronic filing (e-filing), the IRS announced plans to close five of its ten paper tax return submission processing (SP) centers by 2011. Those plans include the closure of a facility in Andover, Massachusetts with 1,524 workers by September 2009. The scheduled closing of the Andover center will be the fourth under the IRS restructuring plan -- following the closure of paper return facilities in Long Island, NY (2004), Memphis, TN (2005) and Philadelphia, PA (2007). The IRS also plans to close the paper submission facility in Atlanta in 2011. The IRS originally sought the closings of the five SP centers in order to comply with the IRS Restructuring and Reform Act of 1998 which established a goal for the IRS to have 80 percent of Federal tax returns filed electronically by 2007. But the IRS recently reported that, in 2007, just 57 percent of all returns were filed electronically. Furthermore, the agency has previously acknowledged that it is getting harder to convert additional taxpayers to e-filing as those who might convert most readily have already done

so. Given the fact that the number of taxpayers opting to e-file is not increasing as rapidly as the IRS had originally projected, wouldn't it make sense to cancel or delay the scheduled closing of the Andover facility?

Answer

As the nominee to be IRS Commissioner, I have not been briefed on the details of the IRS' restructuring plans. Nevertheless, I believe it is prudent to review these plans periodically to ensure they are still on track with actual experience. If confirmed, I will look into this issue thoroughly.

Question 2

The IRS has stated that it will receive millions of dollars in cost savings as a result of the SP site consolidation. However, an August 2007 report by the Treasury Inspector General for Tax Administration (TIGTA) found that the agency's business decision to consolidate sites did not include a cost-benefit analysis (TIGTA Report Number: 2007-40-165). In addition, the report found that the IRS had not adequately updated or monitored financial information on the personnel costs of consolidations and had included savings not attributable to site consolidation in some of its analyses. What is most disturbing is that while the IRS acknowledged some of the assumptions used to determine the consolidation plan may have changed, they refused to complete a cost-benefit analysis to determine if the existing plan is optimal or if alternatives need to be considered. Given the fact that the IRS consolidation strategy rests on an incomplete business plan, wouldn't it be prudent for the IRS to postpone further site consolidations until a comprehensive cost-benefit analysis can be completed to ensure optimal in cost savings and benefits?

Answer

As noted in the previous question, I have not been briefed on the IRS' consolidation plan. I understand that this plan was developed several years ago, and some assumptions may not be borne out by actual experience. I believe it is important to review these plans periodically to ensure they are still on track. If confirmed, I will look into this issue thoroughly to ensure that decisions about consolidation are based on the best information possible.

Question 3

The TIGTA report also raises questions about the ability of the remaining SP sites to handle the increased workload from previously closed SP centers. For example, the report cited several unanticipated developments at the Fresno, CA, Processing site due to increased return volume -- including delays in processing returns and a possible staffing shortfall. The report further notes that the IRS is having difficulty hiring a sufficient number of qualified workers at the site and

that, according to IRS' own methodology, it will be unable to hire enough staff if it reaches its projected workload in Fresno. Is the agency concerned that further consolidation of SP centers might only serve to exacerbate some of the capacity and staffing issues such as those at the Fresno center? To date, has the agency developed any contingency plan to minimize the negative impact that further consolidation may have on taxpayers?

Answer

If I am confirmed, I will take a fresh look at this issue. I am not well versed in TIGTA's findings and recommendations in the report, but I understand from my discussions with IRS senior management that the IRS has taken great care to make sure that there are sufficient processing sites to deliver successful filing seasons. If confirmed, I will ensure that the IRS is using every means at its disposal to minimize the effect of consolidation on current employees, and hire the most qualified personnel at every site.

Question 4

While moving forward with drastic reductions to staff in submission processing operations, the IRS has, at the same time, cited a lack of manpower as one of the primary justifications for outsourcing tax collection duties to private collection agencies. But given the agency's admission that the return on investment when using IRS employees is roughly three times that of private collectors, wouldn't it make sense for the agency to look at retraining some of these SP employees, such as those at the Andover facility, to perform the debt collection work currently being performed by private collectors?

Answer

I understand your concern about the reduction in numbers of submissions processing employees. However, as a nominee, I am not familiar enough with the work of those employees to offer an opinion as to whether they could do the work currently being performed by private debt collection agencies. As a general matter, I believe that whenever possible attempts should be made to redeploy employees affected by restructurings into other jobs within an organization. If confirmed, I will look into this area thoroughly, and if there is a way that the skills of these employees can be utilized outside of submissions processing, I believe that should be carefully considered.

Question 5

History has shown that the IRS has the expertise to improve taxpayer compliance but lacks the necessary resources. The President's own fiscal 2008 budget proposal trumpets the increased tax collections produced by IRS's own employees and cites the increased collections of delinquent tax debt from \$34 billion in 2002 to \$49 billion in 2006, an increase of 44 percent. Recently, the IRS confirmed that the agency is continuing to make tremendous strides in its

collection efforts when it announced enforcement revenue in 2007 surpassed \$59 billion, an increase of more than \$10 billion from 2006. In addition, IRS data shows that the Service spent just 42 cents to collect each \$100 of tax revenue in fiscal 2006, the third lowest figure in the last 25 years and down from 46 cents in 2005. Given the ability of IRS employees to efficiently collect outstanding taxes, do you agree that it makes good business sense to fund the IRS at a level where it can continue to see an increase in revenue?

Answer

Absolutely. From my discussions with IRS senior management, I understand that IRS' return on the dollar for enforcement efforts ranges from 3 to 14 times depending on the program. I am also pleased that the Administration has requested increased funding for IRS enforcement in the last three years and that Congress has generally been supportive of these funding requests. I should also note that every organization, including the IRS, has capacity issues. An organization can only withstand so much growth in a given year; it can only hire, train, and put so many people to productive use. I believe that funding should be adequate to help IRS do the job, but not greater than the agency can reasonably handle. If confirmed as Commissioner, I pledge to be a strong advocate within the Administration for every dollar I think the agency needs to do its job, and within Congress for every dollar the Administration requests.

Question 6

IRS staffing has fallen from 112,000 in 1995 to just 91,000 in 2006, a decrease of nearly 20%. Even more alarming is that during this period, revenue officers and revenue agents - two groups critical to reducing the tax gap - have diminished by 30 and 18 percent respectively. As Commissioner, would one of your goals be to return staffing levels to 1995 levels - particularly in the area of enforcement - in order to help increase taxpayer compliance and close the tax gap? Do you believe these staffing reductions have hampered Service efforts to close the tax gap?

Answer

Until I am confirmed and have an opportunity to look closely at the IRS' staffing needs, I am unable to offer an opinion on what the appropriate or desired level of staffing should be. I assume that technology tools have advanced significantly since 1995, and without knowing more about the nature of the IRS staff, I am hesitant to say that the agency should return to the staffing levels of that or any year. Also, without a deeper examination, I cannot determine the areas in which the IRS is deficient in staff and to what extent, if any, this has hampered efforts to reduce the tax gap.

However, as you stated in Question 5, the IRS has a strong record of improving taxpayer compliance in recent years. In terms of the tax gap specifically, my review of the publicly available information suggests that the best ways to reduce the tax gap is

by increased third-party reporting and by improved transparency. I believe that would give the IRS more tools to support and leverage its employee base.

Question 7

In September 2006, the IRS began turning over thousands of taxpayer files, which include private and sensitive taxpayer information, to private sector debt collectors. Under the IRS plan, the private collection agencies (PCAs) are allowed to keep up to 24% of what they collect, depending on the size of the case. But in testimony before Congress, IRS officials have repeatedly acknowledged that using private collection companies to collect federal taxes is more expensive than having IRS do the work itself. According to the IRS, the return on investment (ROI) from using IRS employees to collect these taxes is 13 to 1, while the ROI for the PCAs is just 3 to 1. In addition, according to the IRS, after commission payments to the PCAs totaling more than \$5.5 million, the net revenue generated by private collectors in FY '07 was just \$20 million. In fact, to date, after spending \$71 million in start up and ongoing maintenance costs through the end of FY '07, the IRS private tax collection program has lost \$50 million. Given the drastic disparity in the return on investment between private contractors and IRS employees as well as the dismal performance of private collectors, do you believe it makes sense for the IRS to continue to pay private collectors almost 25 cents for every dollar collected on the easiest cases in which IRS employees could collect much more cost-effectively?

Answer

I believe one of the jobs of the Commissioner is to make sure the IRS has the correct allocation of resources – the right people, the right funding levels, and the appropriate use of contractors. If confirmed as Commissioner, I would review the resource allocation across the IRS. I also believe that there are a large number of very talented and able IRS employees who do a lot of this kind of work. As for the private debt collection program in particular, I believe that Congress authorized the IRS to use these contractors with the understanding that the IRS would use them as one tool to collect previously uncollected tax debts, which is one aspect of the tax gap. I understand that this issue has been debated extensively in Congress. As long as it is authorized, I would anticipate this program, like every other program, would be run well. If confirmed, I would apply the same principles of efficiency, proper oversight and safeguards, and respect for taxpayer rights and privacy to this program as I would to any other program administered by the IRS.

Question 8

The legislation authorizing the private tax collection program actually allows the PCAs to retain up to 25% of amounts collected. These commission rates were never put up for competition. The fear that allowing private collectors to collect tax debt on a commission basis would lead to contractor abuse was realized

when the IRS recently confirmed that the agency had received more than five dozen taxpayer complaints against the PCAs, including violations of taxpayer privacy laws. In addition, concerns over taxpayer treatment recently led the IRS to terminate its contract with one of the three PCAs contracted to do collection work and penalties totaling \$10,000 have been imposed by the IRS on the PCAs for taxpayer violations. The problem of excessive commission rates was recently addressed by Congress in legislation overhauling the Department of Education's student loan program, which the IRS has consistently held up as a model for the IRS private collection program. The "Higher Education Access Act of 2007," enacted last year, lowers from 23 percent to 16 percent the amount of recovered money that private guaranty agencies contracted by the government can retain on defaulted loans. Should private collection agencies be allowed to keep 25 percent of what they collect or 9 percent more than student loan collectors?

Answer

As the nominee to be IRS Commissioner, I am not familiar with the specific revenue sharing agreement that the IRS has negotiated with the contractors hired under the private debt collection program. I assure you I will review those agreements thoroughly, if I am confirmed, to ensure they provide the proper incentive for the contractors without providing excessive compensation.

Question 9

Do you believe there are security risks when data, including taxpayer information, is sent off-site, handed over to a contractor or given to a subcontractor? Can you describe some of those risks and the level of risk at which data is most vulnerable when a government agency is dealing with contractors? Do you believe data is more vulnerable to security breaches in an agency that contracts with an industry that has high staff turnover?

Answer

Data security is a rapidly evolving issue, in both the private and public sectors. I believe that contractors and subcontractors must be held to the same data security standards as the IRS itself. I know from first-hand experience that data security risks can come in a variety of forms – external threats to information technology such as hacking, employee misuse of media or paper-based data, data loss through mishandling of media or paper-based data, and other risks. From my review of this subject, I understand that the Office of Management and Budget and Congress have made it clear that there should be no distinction between the amount of data protection in place for government-operated systems and those operated by contractors – a standard I fully support. I also believe contractors and IRS employees must be held to the same high ethical standard regarding disclosure and privacy of data.

Ensuring information technology security and protection of taxpayer information will be a high priority if I am confirmed as Commissioner. Clearly this extends beyond the boundaries of IRS itself, but to the other government agencies and contractors that are entrusted with taxpayer and other sensitive data. If confirmed, I will thoroughly review current security programs and ensure a comprehensive security program encompasses all of organizations and contractors with which the IRS has a relationship.

Question 10

While continuing to cite a lack of resources as the primary rationale for contracting out a number of inherently governmental activities, including the collection of taxes, the IRS has continued with ongoing reductions in force of IRS employees that are capable of being trained to do the work that is being given to private collectors. One possibility might be to look at the thousands of IRS employees that are scheduled to be laid off at a number of paper submission processing sites over the next several years. A number of these sites already have the infrastructure and technological capabilities to work the type of cases being turned over to the private companies. In addition, these employees have already undergone extensive background checks and have been trained on the importance of protecting the privacy of all taxpayers. Retraining these employees would allow the IRS to collect outstanding taxes more efficiently without putting taxpayers' financial privacy at risk. Given the agency's admission that IRS employees are more efficient at collecting taxes than private collectors, wouldn't it make sense for the IRS to look at retraining IRS employees scheduled to be laid off to do the work that is being outsourced to private collection companies?

Answer

There is nothing more important to an organization than to have a strong, competent, motivated, loyal, and committed employee base. This is impossible if the organization itself does not show loyalty and support to employees. An important way to do this is that in times of downsizing or reductions in force attempts are made to redeploy affected employees into other jobs within the organization. This is something I am committed to do whenever possible. As the nominee for IRS Commissioner, I do not have the information necessary to comment on the specific example you cite in your question. Once I have a better appreciation for the skill sets of the affected employees compared with what is needed in other areas or how union contracts might affect the redeployment, I will be able to offer a perspective on this issue. However, you have my commitment to look deeper into this matter if I am confirmed.

Question 11

As you know, the President will release his budget request for FY 2009 on February 4th. As Commissioner, if provided with any additional resources above the president's budget request, where specifically would you use them?

Answer

If confirmed, one of my top priorities will be to review the IRS' current funding and the budget request for FY 2009. Once I have a complete understanding of the inner workings of the IRS, I will be able to offer an opinion on where any additional funding that Congress might provide could be put to optimal use.

Question 12

I assume you are familiar with the cases of thousands of taxpayers around the country who have gotten caught up in the ISO-AMT nightmare – i.e., who have lost homes and life savings trying to pay sometimes gigantic tax bills on stock gains that were never realized and that evaporated in the dotcom bust. I have heard from many Massachusetts constituents whose lives have been upended due to this quirk in the tax code. One constituent reports that he had to pay \$80,000 in ISO AMT tax, despite the fact he never realized any gain from the stock. This employee had been unable to sell the stock before the decline due to insider trading restrictions. To pay the ISO AMT tax on phantom income, he had to take out a second mortgage on his home, and could no longer save for his children's education or his wife's and his retirement due to the increased mortgage payments. Do you think Congress needs to give the IRS clearer or broader authority to deal with problems like ISO AMT, that come up from time to time?

Answer

Your question raises an important issue, which I would defer to the Treasury Department's Office of Tax Policy. If confirmed, I will look into this issue and would be happy to discuss my findings with you at an appropriate time.

Question 13

The IRS already has authority to negotiate offers in compromise with taxpayers, but I understand the IRS decided a few years ago to continue to insist on full payment of the ISO-AMT tax, even in cases where the taxpayer had realized nothing at all from the stock. In other words, we have a case where the tax code imposes a tax that no one in Congress could possibly have intended, but the IRS seems powerless to do anything about it administratively. Do you believe that the IRS regulations implementing the IRS Reform and Restructuring Act of 1998 need to be modified to better effectuate Congress's intent to provide relief, through effective tax administration principles, in situations such as ISO AMT where unusual economic or personal factors cause a tax provision to impact taxpayers with these kinds of severe unintended consequences?

Answer

From my discussions with IRS senior management, I am aware that the offer in compromise program can be a valuable tool in resolving disputes with taxpayers. Although I am very sympathetic to the issues you raise, where the obligation to adhere to the tax code has left families in unfortunate circumstances, I am not currently in a position to know whether it would be appropriate to use in this type of situation. If confirmed, I will look into this issue carefully and determine for myself the proper application of the IRS' offer in compromise program.

**Senator Charles Schumer
Questions for Douglas Shulman**

Question 1

I am worried that tax preparers or payday loan vendors will try to use the RAL model to “advance” Americans the rebate that we are providing, as a way of speeding up the process and getting a smaller rebate check into families’ hands sooner. What rules can the IRS put in place to ensure that unscrupulous lenders or scam artists to not try to take advantage of the rebate process – or does Congress need to include some explicit prohibition in the actual legislative language of the stimulus package? I understand that we have rules with Social Security checks that do not allow them to be “advanced” in this way, and I would like to understand what options we have to prevent American families from being taken advantage of when it comes to the rebate checks.

Answer

Since my confirmation hearing, I have spoken with the IRS' senior management about this issue. I have been told that the IRS is developing plans to administer the rebate checks and will take a number of steps to ensure that rebate checks are sent directly to taxpayers and not through loan providers. I am also aware that the IRS and the Treasury Department recently released proposed rules that are intended to address the problem of refund anticipation loans. If confirmed, I will do what I can to ensure that the IRS continues to address this important issue.

Question 2

The IRS has just released a revised Form 990 and Schedule H for tax exempt hospitals. I appreciate the fact that the IRS will be allowing for a transition period before hospitals need to use the new forms. How will IRS assist hospitals in collecting and accurately reporting the new information?

Answer

With my background in regulating the financial services industry, I understand the critical importance of engaging the affected industries prior to the issuance of new rules or regulations. By doing this, we get a lot of valuable input into the process and hopefully avoid potential problems later. From my discussions with IRS senior management, I understand that one of the IRS' principles in the development of the new form was to engage the affected parties as early and as often as possible in the process. I have been assured that the IRS plans to continue the same high level of engagement as it moves forward with the implementation of the new schedule and the development of related instructions. I support this approach and understand that it will help minimize the transition effects and reporting burden as the hospitals begin using the new schedule. I believe this level of engagement with the non-profit hospital community is very beneficial, and if confirmed, I would work to ensure that the reporting burden on all types of hospitals, whether large or small, or located in inner cities, suburbs, or rural communities, is a key consideration in implementing the new schedule and redesigned Form 990.

**Senator Chuck Grassley
Questions for Douglas Shulman**

Questions A: General Questions**Question 1**

Clarifying the role of the oversight board was an important part of the IRS Restructuring Act. I am worried that the role being exercised currently by the oversight board is not in accordance with the direction provided by the IRS Restructuring Act. Please explain to me your views of the board's role, its responsibilities and its duties. Please provide your commitment to ensure that the board will have an opportunity to approve the performance goals not only when the proposed budget is sent to Treasury, but also when Congress enacts a final appropriation for the IRS and the when the IRS sets those goals in keeping with that appropriation.

Answer

As a staff member of the IRS Restructuring Commission, I was involved in formulating the concept of the Oversight Board. I believe that the Board can play a valuable oversight role in working with the Commissioner and other senior IRS officials to set strategy and direction for the IRS. As I mentioned in my at the hearing before the Finance Committee, I view the Board as an asset to the IRS and would treat it as such. I have already met with the current Chairman of the Oversight Board and have spoken with other members. I believe we will have a very productive working relationship, and

that they will continue to play an important role in strategy formulation at the IRS. Regarding the precise timing of when the Board reviews budgets and performance goals, I am not familiar enough with the process to be able to give you a definitive answer at this point. However, you have my commitment to work with the Board in accordance with the IRS Restructuring Act, and to work in a spirit of partnership and cooperation.

Question 2

The IRS has several advisory boards, including those regarding tax-exempt organizations and electronic tax administration. I am very worried that these boards are increasingly being filled by industry, lobbyists and attorneys with client interests. This trend greatly undermines the credibility these boards have with me. The industry, lobbyists and lawyers have already beaten a path to the IRS and have no trouble making their voices heard. The IRS needs to make certain that it is also hearing from voices that are independent and objective and have in mind the priority of good tax policy – those policies that are good for all taxpayers. I ask for your pledge to take steps to ensure that emphasis is placed on having such independent and objective voices making up the majorities on IRS boards.

Answer

I agree wholeheartedly that the IRS needs to have independent and objective advice from its stakeholders. In my current role, I deal with many advisory boards, and the overriding criteria in the selection of members of those boards is to have the very best qualified people who are willing to put the integrity of the market above their own proprietary interests. I pledge to work within the IRS to make sure the various advisory boards that assist the IRS are comprised of people who put the public good, not their own proprietary interests, first.

Question 3

I recognize that you are not a tax professional and that you are being considered for the position of commissioner based on your management experience. The fact that you do not have tax experience naturally suggests that the role of the chief counsel and the importance of the chief counsel will be significantly elevated. It is my view that this places upon you a heightened obligation to make certain that the chief counsel and the office of the chief counsel, in their actions and work, are conforming to the overall goals and policies of the IRS. Please provide me your views on this matter.

Answer

If confirmed, I will view myself as accountable for the administration of our nation's tax laws. As such, I will need the authority to do that job appropriately and the best advice

possible to carry out that duty. The Chief Counsel will be my primary source for counsel and my chief legal advisor, and I expect to get the best advice he or she can offer. I expect open and honest communication from all the IRS employees, including the Chief Counsel and his or her staff, and I will share the same with them. I will make sure I am deeply involved in all the necessary issues to ensure that actions of all IRS employees are in keeping with the overall goals of the IRS.

Question 4

It has been suggested that the tax withholding crisis in the banking industry is due to the lack of audits on hedge funds to whom the banks sold the withholding products, and that this has caused banks to be overly aggressive. What are your plans in this regard, and what is your general strategy for future industry examinations? Given your background in the financial industry, what do you see as the top priorities of examination in this area? Where do you think the IRS needs to do more auditing and examinations in the financial industry?

Answer

The financial services industry is one with which I have a high degree of familiarity. This is a rapidly evolving industry that is quickly changing the products it is making available to its customer base. If confirmed as Commissioner, I intend to provide my insights on a regular basis to the experts within the IRS who deal with this industry on a regular basis and to learn more about what has been done in the past in terms of industry examinations and the establishment of future priorities. I would need to familiarize myself better with the approach the IRS has taken with respect to financial services in the past before offering concrete opinions about examinations in this area.

Question 5

The GAO has reported that the IRS does not use all the tax return information it receives for its automated compliance checking programs. In essence, IRS policy is to post the same lines from electronic and paper returns to its enforcement databases. This means that IRS employees are dealing with only limited information and many individuals who file electronically are potentially needlessly contacted because of additional information that is available. Please provide me your commitment that within the next few months the IRS will post, and continue to post, all lines from electronic returns to its enforcement databases.

Answer

If confirmed, I will carefully review the types of data the IRS uses to support its compliance programs and evaluate whether there are better ways to capture and employ all the data available to the IRS. My goal will be to ensure the agency adopts

the most effective methods to obtain and use data contained on tax returns for compliance activities.

Question 6

I asked a question about IRS members doing union work at your nomination hearing. Please provide a more complete answer and note that I do not consider your stated lack of familiarity with IRS hiring practices and procedures to be part of a satisfactory response. I have heard continuously from the IRS, the NTEU and some members of Congress that there are not sufficient employees at the IRS to do the job. At the same time, there are thousands of FTE's at the IRS doing union work at taxpayer's expense. This makes no sense to the American people.

Treasury has informed me that the number of union hours at the IRS is greater than the average in the federal government. I want your assurance that Treasury and IRS will only sign a union contract that provides for no more than the average number of union hours in the federal government. In addition, if a new contract is not signed, that you will take action within 60 days to limit union hours to no greater than the average number in the federal government and ensure that no IRS employee will spend less than 10% of their work time directly or indirectly on union activities. Please provide in detail what benefits will be realized by reducing the number of union hours to the federal average – in terms of additional hours for taxpayer service, audits, collections, enforcement and other activities. Please discuss in detail the impact this will have on addressing the tax gap. Please inform me of the number of IRS employees that are currently spending more than 10% of their time directly or indirectly on union activities.

Answer

If confirmed, I intend to be fully briefed on the status on the national agreement between the IRS and the NTEU. As I stated at the hearing before the Senate Finance Committee, I believe the Commissioner must exercise leadership over the entire IRS workforce – managers, rank-and-file, union, and non-union. My goal would be for all IRS employees to be focused on IRS priorities.

From my limited discussions with IRS management on this issue, I understand that currently the number of union hours at the IRS is not in line with the federal government averages, and I have been told that IRS management is working to bring union hours closer to the government-wide averages. Clearly, there is more to be accomplished in this area. If confirmed I will look into this matter closely, work to address any problems, and consult with you on progress made.

Question 7

One of the greatest burdens for middle management at the IRS is having to deal with a union workforce – and specifically the time spent by employees on union

activity and travel for union activity. Please detail for me those concrete steps that you will take to ensure that middle management at the IRS knows that you have their support in dealing with the union workforce.

Answer

While I am generally familiar with the roles and responsibilities of the union workforce within the IRS, if confirmed, I intend to be fully briefed on the current relationship with the union and the important role that I understand the NTEU plays under the labor laws. While I cannot respond to your specific questions at this time, once confirmed, I will give this issue my attention, and I will be happy to offer specific input once I have a better understanding of this matter.

As I stated previously, I believe the key to retaining the best people at the IRS is making the IRS a great place to work: a place where people are challenged, supported, respected, held accountable, and given opportunities to grow personally and professionally. My goal is to make the IRS one of the best places to work in the government, while developing the next generation of IRS leaders. From my initial discussions with IRS senior management, these beliefs appear to be in alignment with the agency's goals of maximizing employee resources to meet business needs, relieving management burden, and ensuring the recruitment of the right people for the right jobs. I believe that middle management is the key to this goal, and if confirmed, I will ensure that they know that I support them.

Question 8

The Taxpayer Advocate has recently suggested that a priority for TE/GE should be to quickly process requests for tax exempt status. My investigations have shown that we have very significant problems in the tax-exempt area and that these problems will be exacerbated by sending a message to TE/GE that in reviewing exempt status – speed is the priority. The priority of TE/GE in reviewing requests for tax-exempt status should be conforming with the intent and spirit of the tax laws; ensuring the credibility and public trust of the tax-exempt sector; and, protecting the public fisc. Tax exemption is a right not a privilege. I want your assurance that you will make certain that TE/GE understands that compliance with the tax laws, maintaining public trust and protecting the public fisc is TE/GE's first priority in reviewing and approving applications for tax exempt status now and in the future.

Answer

I recognize that tax exemption provides a special status to certain organizations, in exchange for which the Congress and the public expect each organization to further public purposes and comply with the requirements for exemption. It is for this reason that most charities and certain other organizations must apply to the IRS for a determination that the organization is exempt rather than taxable. From my discussions

with the IRS on this issue I understand that the primary objective of the application process is to ensure that the organization is properly organized and intends to pursue an appropriate tax-exempt purpose. Yet, the process also provides the IRS an opportunity to educate the organization about the requirements and responsibilities of the special tax-exempt status.

From my perspective, this process seems to require a careful balance. On the one hand, a significantly delay in granting tax exemption may stand in the way of an organization beginning to pursue its mission – for example, providing meaningful social benefits to those in need. On the other, if the IRS is too hasty, an organization could receive tax benefits it does not deserve. While I would work hard to ensure timely processing of applications for tax-exempt status, I am committed to enforcing the tax law, protecting the fisc, and sustaining the public trust in the tax-exempt sector.

Questions B: Virgin Islands

Question 9

In 2004, the Finance Committee became aware of significant tax abuse by U.S. taxpayers of improperly claiming residency status in the Virgin Islands. In cooperation with the Department of Treasury and the IRS, we included legislation in the JOBS Act to shut down this abuse. I wrote on this matter to the IRS on May 24, 2007 and received a reply on November 9, 2007.

Please provide me your views on the legislation proposed in the House that would have modified the anti-abuse language in the JOBS Act and allowed the statute of limitations to run retrospectively based on the filings of a Virgin Islands tax return. Please explain whether you oppose or support the proposal by the House and your views on the impact of such legislation in addressing the tax gap and ensuring taxpayer confidence in the tax system.

Answer

From my initial discussions with IRS senior management, I understand that there are a number of audit-related issues involving the U.S. Virgin Islands. Until I am confirmed, I am unable to be briefed on the details of those issues, which involve confidential taxpayer information. Accordingly, I am not in a position to assess the impact that this legislation might have on the IRS' enforcement responsibilities. If confirmed, I will make it a priority to be fully briefed on this issue, and I would be happy to discuss this with you further once I have a better understanding of this matter.

Question 10

Please provide me your assurance that you will take all steps to fully support the IRS' and Department of Justice's enforcement efforts and actions as it relates to the Virgin Islands. Please provide me your assurance that you will take no steps

that will undermine or otherwise limit IRS and Department of Justice enforcement efforts as it relates to the Virgin Islands.

Answer

If I am confirmed and sworn in as the IRS Commissioner, I will take an oath to uphold the laws of the United States. Accordingly, I will follow the law and support the law-enforcement actions of the IRS and the Department of Justice with regard to the U.S. Virgin Islands.

Question 11

Please provide me your assurance that you will give me a written update on the information requested in my May 24, 2007 letter every six months beginning July 1, 2008.

Answer

If confirmed, I will be happy to update you on the IRS' enforcement efforts with regard to the Virgin Islands within five months of my confirmation and provide appropriate ongoing updates.

Questions C: Compliance and Collection Activities

Question 12

IRS has set a goal of achieving an 85 percent compliance rate by 2009. Others have pressed for a higher goal, such as 90 percent.

Do you think the 85 percent goal is realistic and can be achieved with existing resources? What about a 90 percent goal? Do you believe that a goal of 90 percent can be achieved in ten years? How do you expect to address the compliance rate, the tax gap? How will the Finance Committee measure your success in this area? What do you intend to accomplish in your first year? Please provide your proposals to address the tax gap?

Answer

I share your concerns about the tax gap and believe it is a significant problem that should be actively addressed. The estimates show a large amount of due, but unpaid taxes, which has the potential to undermine the entire system.

As Chairman Baucus mentioned in the hearing, continuity of approach is important for an agency like the IRS. Therefore, as a starting point, I would anticipate continuing to implement the strategy developed by the Treasury Department in September 2006, which offered a seven prong strategy that included: Reducing Opportunities for

Evasion, Making a Multi-Year Commitment to Research, Continuing Improvements in Information Technology, Improving Compliance Activities, Enhancing Taxpayer Service, Reforming and Simplifying the Tax Law, and Coordinating with Partners and Stakeholders. I would also continue work on the proposals set forth in the report submitted by the IRS in August 2007, entitled "Reducing the Federal Tax Gap, A Report on Improving Voluntary Compliance." From my review of the report, I understand that specific initiatives were identified within each of the seven prongs of the tax gap strategy along with corresponding timetables by which action should be completed.

In addition, as I promised in my hearing, I would bring a fresh set of eyes to the issue. One area worth significant study and consideration is increasing the third-party information reporting requirements, which may be particularly relevant in the area of sole proprietors. The report mentioned above identifies sole proprietors as a significant area of underreporting, and the research shows that compliance increases as third-party information reporting increases. With that said, I am aware that there are potential downsides to increased reporting, in that it may increase the burden on compliant taxpayers. This is clearly an area worth exploring, and one that will require continued discussions among the IRS, the Treasury Department, and Congress, given its broad ranging policy implications.

Regarding a specific target, as I stated in my hearing, I do not feel I am in a position to know what compliance level can be achieved. The report notes that compliance rates appear to have hovered around the same level for decades. For example, based on data from the 1960s through the 1980s, the IRS estimates that the compliance rate has moved within a range of two percentage points and was virtually the same in tax year 2001 as it had been in tax year 1985. I am hesitant to commit to a specific target because I believe it would be premature for a nominee to make pronouncements on fixing a decades-old problem without time for in-depth discussion and planning. I am sure we could increase compliance, but care needs to be given to placing additional burdens on compliant taxpayers and to making other policy and operational trade-offs.

If confirmed, I will commit to study this issue closely, become personally involved in the tax gap issue, and discuss with you further my views regarding the potential options available to make a significant dent in the tax gap.

Question 13

In his last report to the IRS Oversight Board, Commissioner Rossotti noted that the growth in the number of taxpayers combined with a decline in enforcement staffing levels meant that IRS was facing a "huge gap" between (1) the numbers of taxpayers who were not filing returns, not reporting properly on filed returns, or not paying the taxes they owe and (2) IRS's capacity to address the compliance problems. He proposed that IRS receive a steady growth in staff levels of about 2 percent per year and steadily increasing funding for modernization for several years. Although IRS has received budget increases since 2002, they have not allowed for such growth in staffing.

Do you agree with his proposals for increasing staffing and funding? What strategies will you pursue to address the gap between IRS's capacities and responsibilities? What areas do you believe the IRS can save funds and be more efficient?

Answer

Without being inside the IRS and looking carefully at the budget and resource allocation within the agency, I cannot comment on what the appropriate, staffing increase, if any, should be per year. If confirmed, I intend to be a strong advocate within the Administration for every dollar I think the agency needs to do its job, and within Congress for every dollar the Administration requests. Beyond the issue of knowing the specific staffing level increase, I do think Commissioner Rossotti's recommendations reflect a couple of realities. First, staffing cannot be built overnight. It will take time and is a gradual process. And second, if there is a need to rebuild staffing or any other aspect of the IRS budget, it must be done carefully and within the capacity of the IRS to handle and make productive use of the increase in any given year.

In addition, for the IRS to improve its productivity and overall effectiveness significantly, I believe it is essential that the IRS modernize its administrative and IT systems. Therefore, one of my highest priorities as Commissioner, if confirmed, would be to ensure the agency is effectively addressing the key risks that can endanger its modernization efforts.

I also envision doing a capability assessment for each of my top priorities. Once we have a vision and a goal to achieve, I will work with the IRS senior management team to assess what capabilities the IRS has, what capabilities it does not have, and develop a plan to close that gap.

Also, as I mentioned at my confirmation hearing, I believe that any organization can always improve. I am sure that there are areas that need more investment at the IRS, and there are areas where I could find cost savings. I am committed to looking for and pursuing areas where there can be cost savings and efficiencies.

Question 14

How will you determine the appropriate staffing levels for IRS's enforcement activities, and what short and long-term strategies will you employ to ensure that IRS's enforcement staffing levels are appropriate?

Answer

I think the IRS needs to continue to expand its enforcement staff at a rate that allows the agency to train new hires adequately to be most effective. I also think the IRS needs to look at enforcement staff within the overall resource allocation of the agency.

Additionally, I believe the IRS needs to have an appropriate rate of return on investment and that should be a factor in determining the appropriate staffing levels. As I understand it, the IRS has established a high rate of return for enforcement activities. As long as the IRS can maintain such a high rate, then it makes sense to continue to hire additional enforcement personnel.

Finally, I think it is important that enforcement efforts be carried out in such a way that continues to recognize IRS' dual role of enforcing the tax laws and providing taxpayer service.

Question 15

A significant part of the tax gap is due to noncompliant sole proprietors. GAO recently identified [Tax Gap: A Strategy for Reducing the Gap Should Include Options for Addressing Sole Proprietor Noncompliance, GAO-07-1014] options in several categories that could improve sole proprietor compliance. The categories included simplifying record keeping and reducing complexity, enhancing and expanding information reporting of income, and expanding information reporting of expenses. In response to GAO, Treasury said that GAO's options provide valuable insights for the administration's tax gap strategy.

Which approaches have the most promise? What will you do to help implement them?

Answer

I am generally familiar with the GAO report and understand that it included an approach to address the tax gap problem with sole proprietors. From my perspective, I think the problem with the high levels of noncompliance by sole proprietors is a function of two factors. First, due to the complexity of our tax laws, sole proprietors may not understand fully their tax obligations. I am aware that IRS has a number of programs in place that are designed to help sole proprietors and other small businesses as well as the tax practitioners that serve them. If confirmed, I will examine these programs more closely to see if they need to be expanded further or redirected. The second problem is the relative lack of transparency and third-party reporting of the transactions conducted by sole proprietors. From my review of the public information related to the tax gap, it is clear that the levels of compliance are higher in instances where there is third-party reporting. I understand that the Administration has made some legislative proposals to increase reporting, and I believe enactment of these proposals would improve the IRS' ability to verify small business transactions. In addition, I believe the IRS, the Treasury Department, and the Congress need to look at other ways to increase third-party reporting with respect to sole proprietors and small businesses.

Question 16

GAO also made recommendations to strengthen the Offer In Compromise program [IRS Offers in Compromise: Performance Has Been Mixed; Better Management Information and Simplification Could Improve the Program. GAO-06-525] by reducing staffing to match workload; better measuring performance; setting timeliness goals for each taxpayer; analyzing trends in repeat offers, timeliness, and access; and eliminating offer types that are not meaningfully distinct. IRS has reduced staffing and is analyzing repeat offers.

When will the analysis of repeat offers be completed and what will you do to ensure implementation of the other recommendations?

Answer

As the nominee for IRS Commissioner, I do not have access to information about the analysis that you mentioned, when it might be completed, or what additional steps may need to be taken relative to the other recommendations. If confirmed, I will certainly look into this matter and will be happy to offer you my specific input once I have a better understanding of this matter. However, though I cannot respond specifically to your question, I can tell you that I see real value in the Offer in Compromise Program within the IRS. Based on my understanding of this program, I believe that it results in the collection of tax revenues that might otherwise not be there. If the IRS is going to be serious about improving compliance, the agency needs to be willing to use all the tools available, and I view the Offer in Compromise Program as being one of those important tools.

Question 17

In addition, GAO recommended that Congress consider requiring basis reporting on the sale of securities [Capital Gains Tax Gap: Requiring Brokers to Report Securities Cost Basis Would Improve Compliance if Related Challenges are Addressed, GAO-06-603]. Congress is currently considering passage.

Based on your experience in the financial services industry, how quickly could such a requirement be implemented?

Answer

During my tenure at FINRA, I worked extensively with the financial services industry to implement regulatory changes. From the transformation of U.S. equities trading in the United States, to the introduction of transparency to the corporate debt market, to reforms in the mutual fund industry, I have experience with a number of different approaches to introducing large changes to this dynamic industry.

For cost-basis reporting, I believe that an incremental approach may be warranted. Many firms currently track cost basis as a service to their clients, but it is not required. And, while many firms have the capability to track cost basis for securities purchased at that firm, there are no consistent procedures in place for determining cost basis for securities purchased at other firms and subsequently transferred.

In addition, certain types of securities introduce particular issues that must be considered. In order to speed implementation, it might be advisable to focus initially on the types of securities most commonly owned by individual taxpayers. Other financial products, particularly complex hybrid securities, may present more challenging considerations that could delay implementation.

I believe that for securities purchases in the current year, implementation could be on a shorter timeframe, recognizing that securities firms, especially those that do not currently track basis for their clients, will need a reasonable amount of time to adapt. For securities purchases in previous years, an incremental approach would make sense. For securities that were transferred from another brokerage account, the timeframe would likely be longer. And, there will be cases of incomplete or non-existent records, in which case, I would recommend working with the financial services industry to create a long-term solution to this problem.

Question 18

I am frustrated that the IRS continues to improperly allocate resources on audits that result in “no-change.” This means that IRS is not effectively picking cases for audit and wasting limited resources. It also means that innocent taxpayers are subject, unnecessarily, to examination.

How do you intend to improve audit selection for individual taxpayers and small businesses? What goals and milestones can we hold you accountable for in this area for next year?

Answer

I stated during my confirmation hearing that, if confirmed, I will work to ensure that IRS actions are seen as fair and impartial. I also indicated that I will evaluate how resources are currently being used to ensure that they are allocated in the most effective manner. Although this is an issue that I want to understand in more detail, let me give you my general perspective.

I believe it is important that the IRS not create additional burden for compliant taxpayers and that enforcement resources be focused on those taxpayers who are the least compliant. As such, the optimal compliance-case selection needs to result in as low a no-change rate as possible. However, from my initial discussions with IRS management, I understand there are other reasons that cases are selected for examination. For example, for research, audits need to be selected randomly in order

for the research to be valid. In those cases, the no-change rate will understandably be higher. Similarly, I understand that the IRS tries to maintain a certain level of coverage across all income levels, so audits selected to maintain that kind of coverage may also have a higher no-change rate than when non-compliance is specifically targeted.

This is obviously a very important issue for both the IRS and taxpayers, and I commit to discussing this with you further once I have a better understanding of this issue.

Question 19

The other concern I am hearing that is just as troubling as the IRS not doing a good job of finding the right targets for audit is that IRS agents are sometimes not properly trained or educated in the relevant tax law. In addition, IRS employees face pressure from senior management to be current in audit. The bottom line: individual taxpayers and small businesses too often face an IRS employee who is not sufficiently knowledgeable in the law and is under pressure to make a determination quickly regardless of the law and facts. This leaves the individual or small business owner holding the bag and having to engage in a costly and time intensive fight through the IRS bureaucracy, appeals and the courts to get at the right answer. That is not how it should be.

Please provide me your views on this in general. Please inform me how you are going to ensure that IRS examination gets it right the first time – that agents are properly trained and have sufficient education and support to come to the correct answer. Please provide a detailed answer of how you intend to hold individual examination employees and their managers personally accountable for the quality of their work. Please provide me a written update on these efforts every six months beginning July 1, 2008.

Answer

Based on my prior experience, I recognize that a well-trained workforce is essential to the success of any organization. If confirmed as Commissioner, one of my priorities will be to ensure that the IRS provides the appropriate and necessary training for its workforce and, in particular, make sure that employees are trained to stay current with the tax law. I will also work to ensure that IRS employees are equipped with the right tools to carry out their appointed duties.

While I have not yet had the opportunity to review the full complement of IRS training programs, I understand the challenges associated with training new recruits, as well as keeping the technical workforce prepared to face new tax law issues. While at FINRA, we confronted similar challenges in developing and maintaining a high level of specialized expertise among the workforce. We established "Examiner University" – a comprehensive training program for new examiners that combines intensive classroom instruction with mentoring and on-the-job training. We also enhanced the level of training available to experienced staff members. If confirmed, I would envision bringing

similar creative solutions to the training and development of IRS employees – new recruits and experienced staff alike. Providing employees with proper training and professional development opportunities would be an important theme under my leadership.

Electronic Filing

Question 20

While progress has been made in increasing the number of taxpayers who file their tax returns electronically, IRS still receives many returns on paper. In reports on recent filing seasons, GAO has recommended further study of electronic filing mandates or bar coding of computer generated paper returns as options for increasing electronic filing.

What will you do to implement GAO's recommendations?

Answer

I have reviewed a number of GAO's recommendations, and I believe they warrant serious consideration. From my initial discussions with IRS senior management, I understand the IRS has already begun a study of ways to advance electronic filing that will include a look at mandates and bar coding of computer generated paper returns. If confirmed, I intend to review the results of the study carefully and consider additional steps the IRS can take to meet the 80-percent e-filing goal set by Congress.

Question 21

Please provide me your stated goals for electronic filing and how you will achieve them, and please provide the year-by-year measurements for which Congress should hold you accountable.

Answer

I understand that Congress has set a goal for electronic filing of 80 percent. As noted above, if confirmed, I intend to carefully review the IRS study on advancing electronic filing that is currently under way. My objective would be to develop a strategy that will enable the IRS to achieve and eventually exceed the 80-percent goal. However, I would need to examine the details of this strategy before I could offer appropriate measurement criteria.

Customer Service**Question 22**

A majority of taxpayers use tax professionals to get tax law assistance and prepare their tax returns. These preparers provide a critical checkpoint in the tax system but, as GAO found [Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors, GAO-06-563T], they often make serious errors. GAO also recommended that IRS determine the extent to which paid preparers live up to their responsibility to file accurate and complete tax returns. IRS agreed with GAO's message and has begun some research into the performance of paid preparers.

What are your views on whether tax return preparers should be registered and regulated by the federal government?

Answer

I believe that taxpayers deserve to get knowledgeable, professional, and honest service from preparers. I believe that the IRS already has a variety of tools at its disposal to ensure that these high standards are met, including the bully pulpit, education, dialog, and outreach, and where appropriate fines and disciplinary actions.

I am intimately familiar with registration and regulation of professional service providers in the financial services industry. If confirmed, I would give careful consideration to the issues surrounding the registration and regulation of preparers.

Regulation has clear benefits, but it also comes with costs. Regulation puts an additional burden on preparers, especially those who are already capable and ethical. It also imposes industry-wide costs, which inevitably would be borne by taxpayers. Before mandating regulation, I believe we need to ensure that the benefits in terms of improved compliance outweigh the costs that such regulations would impose. Finally, regulation of tax preparers would require IRS senior management attention and financial resources that would otherwise be devoted to other aspects of tax administration, namely taxpayer service and enforcement.

If confirmed, I would look all of these issues with an open mind, and I look forward to the opportunity to study the issue further.

Question 23

What will you do to ensure that GAO's recommendation to get better information on paid preparer performance is implemented fully?

Answer

As previously stated, I need to become more familiar with the IRS' current relationship with preparers. Getting better information on paid-preparer performance would be an essential part of the process. Understanding return preparer behavior, needs, and preferences is critical to providing targeted service and focused enforcement activity. I understand IRS has initiated various research projects in support of the Tax Gap Strategy and the Taxpayer Assistance Blueprint (TAB), which will provide critical data and information to base decisions regarding service, enforcement, and technology generally, and with respect to return preparers, in particular.

Compliance Research**Question 24**

Measures of voluntary compliance are important for determining compliance levels, allocating resources, and identifying specific compliance issues that could be addressed through changes in tax forms and instructions or the tax laws. IRS currently has a National Research Program (NRP) that has measured the level of voluntary compliance among individual taxpayers and is examining S corporations. In addition, the Taxpayer Assistance Blueprint calls for more research on the effect of service on compliance.

**Do you think IRS is devoting enough of its resources to compliance research?
How many resources would you devote to compliance research activities?**

Answer

I understand that the National Research Program is critical to the IRS' efforts to understand taxpayer compliance better. From reading the 2007 Tax Gap Report, I understand that the National Research Program was able to develop innovative ways to collect the information needed without the burdensome audits that had previously been conducted under the Taxpayer Compliance Measurement Program. Based on this information and my own inherent belief in the need for quality research to make important decisions, I believe the NRP is critically important to the IRS, and if confirmed, I would want to see it continue. However, without looking carefully and thoroughly at the IRS budget and this specific program, I cannot comment on whether the level of resources devoted to compliance research is appropriate. I can only reiterate my strong support for research especially given the IRS' need to understand better the reasons for noncompliance.

Human Capital Management**Question 25**

IRS has taken a number of steps to improve its human capital management practices but, like other federal agencies, faces challenges attracting and retaining key personnel. IRS is likely to lose many experienced personnel to retirement in the next few years.

What strategy will you pursue to minimize the loss of key personnel and to ensure that IRS is able to hire adequate numbers of appropriately skilled staff?

Answer

I believe the key to retaining the best people at the IRS is making the agency a great place to work: a place where people are challenged, supported, respected, held accountable, and given opportunities to grow personally and professionally. Making the IRS one of the best places to work in the government, and developing the next generation of IRS leaders, would be major themes of my tenure, if I am confirmed.

I understand that the IRS has a number of programs in place to retain key personnel, and I plan to review those programs. I understand the IRS has developed a recruitment program that provides the IRS with access to a wide range of potential employees, including individuals entering the workforce for the first time, seasoned individuals looking for new challenges; and retirees looking to rejoin the workforce.

Veterans**Question 26**

The nation is seeing a significant number of veterans, many of whom are disabled, returning from Iraq and Afghanistan. These are extraordinary young men and women, and our country is honored by their service. There is no question that these men and women are extremely capable. I think it is important for the federal government to do all that it can to hire these returning veterans, and it is clear that the IRS offers many opportunities for these servicemen and women, particularly the disabled. These veterans will bring to the IRS a good deal of much-needed youth, a fresh outlook and experience and, most importantly, a "can do" attitude that is much needed. The IRS will greatly benefit from these veterans joining its ranks.

I raised this issue during your nomination hearing and would like you to answer in greater detail. I want your commitment to set a goal of hiring one thousand Iraq and Afghanistan veterans this fiscal year, with a particular emphasis on those who are disabled. Please provide me a discussion of how you will seek to implement this goal, including outreach, job classifications and reclassifications,

notification, working with veterans' organizations, and working with the Department of Veterans Affairs and the Department of Defense. In addition, if there are any legislative changes that will aid or assist this effort, please identify them. However, I am confident that the IRS has significant authority at hand to accomplish this goal.

Answer

I assure you that I share your goal and the sentiment of doing all we can to help our returning service men and service women. While not completely familiar with IRS hiring process and rules, I commit to you to work with the Administration and affected agencies toward this objective.

Managing and Modernizing IRS

Question 27

IRS has experienced delays in delivering new versions of CADE, the centerpiece of its ongoing systems modernization effort, on time.

What is your strategy for ensuring that the systems modernization program at IRS delivers systems with promised benefits, within budget, and on schedule?

Answer

As I stated in my testimony, IRS employees must have timely access to taxpayer data so assistance is quick and accurate. This will require focusing on and investing in IRS tax administration processes, as well as IRS' information technology systems. If confirmed as Commissioner, I would make this one of my top priorities.

Over the past seven years at the NASD and now at FINRA, I have had responsibility for information technology, including the implementation of large-scale information technology projects. During that time, I have seen how difficult it is to deliver large-scale IT projects on time and within budget, and provide the business value initially promised. In my experience, it is easy to underestimate the complexity in providing the new promised functionality, both in terms of the new system itself, and the interfaces with other existing systems in the enterprise. This would be especially true at the IRS, where one must deal with an exceptionally complex tax code and an IT environment consisting of hundreds of legacy systems.

That said, there are certain principles to ensure success in delivering large-scale IT projects. First, there must be a well-articulated set of business objectives for the project. All stakeholders, including the users of the system and the IT organization, must agree on those business objectives from the outset. Second, the organization must implement a robust and mature set of project management standards and tools to ensure a highly disciplined and comprehensive approach is used to manage all aspects

of the project. For example, a mature requirements management process is essential to ensure that the project develops a complete and detailed set of requirements that will meet those business objectives. Finally, the project must have the proper personnel management and governance model, to clarify authority and accountability at all levels of the organization. People must understand their role and be held accountable for their performance.

From my review of available information and my discussions with IRS leadership, it is clear that the IRS has improved its ability to manage large-scale IT modernization projects. The IRS admits, and I concur, that the agency is still not fully mature in all project management processes, including areas such as contract, performance, and configuration management. If confirmed, I would build on the successes that the IRS has achieved to date, and ensure that the agency continues to pursue improvements in all areas of IT program and project management.

Question 28

What do you believe are the long-term risks to IRS's modernization that you will have to deal with, and what are the consequences if they are not successfully managed? What benchmarks should we use to monitor and measure your performance in this area?

Answer

For the IRS to improve its productivity and overall effectiveness significantly, modernization of its administrative and IT systems is a necessity. Therefore, if confirmed, one of my highest priorities as Commissioner would be to ensure the organization is effectively addressing the key risks that can endanger its modernization efforts. From my discussions with IRS senior management, I understand that the key long-term risks to modernization include:

- Replacement of master file systems that were designed in the 1960s;
- Modernizing very complex and interrelated legacy systems; and
- Managing the loss of the key IT personnel with knowledge of IRS critical legacy systems.

With respect to measuring success, I believe it should be determined by the IRS' ability to meet the business objectives promised by modernization. If confirmed as Commissioner, I will work to ensure that timelines for the major modernization projects are in place and that there are clear business objectives for each of the modernization projects.

Question 29

In the past, GAO identified significant and material weaknesses related to the security and control of the agency's computer systems and networks.

What is your strategy for strengthening the security over the agency's computer systems?**Answer**

Clearly computer and information security is of paramount importance to the IRS and the country. Confidence in the tax administration system is critical to the American public, which entrusts the IRS with the safekeeping of their tax information. From my review of available materials and discussions with IRS leadership, it is clear that the organization is actively pursuing improved security on numerous fronts, including:

- Implementing secure data transfer procedures;
- Encryption of laptop computers;
- Improved password procedures; and;
- Increased monitoring to enhance the protection of taxpayer information and other sensitive personally identifiable information.

That said, I believe that more work remains to be done. From personal experience, I know this is a dynamic area in which ever-increasing diligence is needed; penetration attacks and on-line fraud schemes are increasing, and the IRS must respond to thwart such attacks. As I have learned in my work at FINRA, security must be top-of-mind for all employees. At the IRS, security must be an essential ingredient in all work processes and systems, not viewed as an afterthought. When new IT systems are designed and developed, the information security requirements must be identified at the start, and tracked and tested with the same rigor as core business requirements. This is the culture of security that must exist at the IRS, and if confirmed as Commissioner, I will work to ensure such a culture is developed and maintained.

The other key aspect of information system security is online monitoring. All IT assets, to include both hardware and software, must be constantly monitored for penetration attacks, viruses, and other forms of malware. Maintaining the latest versions of systems and ensuring security patches are implemented timely is critical. I recognize that the challenge for the IRS' security posture is that it is only as good as its weakest point. A comprehensive monitoring program of all IT assets in the enterprise is essential for success. As Commissioner, I would make it a high priority to ensure that such comprehensive monitoring is in place.

Financial Management**Question 30**

IRS continues to face many challenges in its ongoing efforts to improve the accuracy and reliability of its financial and information management systems and to correct internal control weaknesses. For example, despite notable progress and despite having received clean, or unqualified, audit opinions on its financial

statements for many years, financial management at IRS has been on GAO's high-risk list since 1995, first as a separate issue and later as a component of the IRS Business Systems Modernization high risk area. Although IRS again received an unqualified audit opinion on its financial statements in 2007, it continues to need to manually analyze and correct data generated by its financial systems. This approach does not produce timely information for managing the agency.

What are your views on the need for IRS to modernize its financial management systems, and do you view this as a high priority for the agency? What benchmarks should we use to monitor and measure your performance in this area?

Answer

I am committed to moving forward with the modernization of the IRS financial management systems to address the issues in the GAO reports you referenced. I believe it is a high priority for the IRS to have strong financial management controls to ensure the integrity of its financial statements.

I understand from my discussions with IRS officials that the IRS is modernizing the revenue accounting systems to address the GAO issues, has benchmarks in place to monitor its progress, and reports its progress on a quarterly basis to the Treasury Department and the Office of Management and Budget.

Question 31

When can we expect to see the kinds of changes implemented that will enable GAO to remove financial management at IRS from its high-risk list? Please provide specifics that we can use to monitor and measure your performance in this area.

Answer

As noted in Question 30, I understand that the IRS has a comprehensive plan in place to address this issue, and I am committed to moving forward to modernize the IRS financial management systems if confirmed. I also understand that the GAO provides updates on the status of IRS financial management system improvements in its annual audit report.

Performance Measures

Question 32

According to past GAO work, IRS needs to ensure that it has comparable performance measures over time and sufficient data to assess performance. IRS

needs to routinely evaluate its programs to identify ways to improve their performance.

What is your strategy to help ensure that IRS managers acquire sufficient data to assess and routinely evaluate performance to make continuous improvements in its programs?

Answer

In my experience as an executive in the private sector, goals and measures are incredibly powerful tools. In order to change behavior and achieve continuous improvement, managers and their employees need to clearly understand how their performance is being judged, and what behaviors are most rewarded.

If confirmed, I plan to conduct a review of measures in place at the IRS today and make sure that they are aligned with the priorities of the IRS as a whole. In so doing, I plan to engage a wide array of employees in this review because above all else, the measures must be clear, and they must engender the desired behavior.

Questions D: Nonprofit/Tax-exempt Questions, Part I

Question 33

The IRS has consistently stated that Supporting Organizations are one of the most abusive areas in the field of exempt organizations. Congress passed legislation to address this matter in the Pension Protection Act and the Treasury/IRS issued regulations in this area last year. A key component of these regulations is a requirement of a 5% payout for nonfunctionally integrated supporting organizations. However, in breaking with normal practice, the regulations provided no effective date – they were issued as Advanced Notice of Proposed Rulemaking. This is unacceptable. I ask that you or Treasury/IRS provide me assurance that Treasury/IRS will implement the guidance promptly and make the 5% payout effective within 30 days of your receipt of this question. I will have additional views and concerns regarding this proposed rule, separate from the 5% requirement, that I will address in a separate question.

It is important to immediately designate an effective date for the 5% payout, and there should be no transition relief. There is no reason that the payout rules cannot take place immediately. These supporting organizations have been on notice for a significant period of time that there were going to be changes in current operations. Charities have waited too long to finally get the funds that were donated to these supporting organizations. In addition, I ask that you provide me a written update every 6 months, beginning July 1, 2008, of the efforts IRS and Treasury are undertaking to address other identified abusive problems in supporting organizations and donor advised funds. Finally, I ask for your written

response to the additional views I have regarding these regulations that I will send separately.

Answer

The charitable sector makes important contributions to our society, and I recognize the important work that you and the Committee have done in this area. I am aware of the Advance Notice of Proposed Rulemaking you referenced and that the IRS FY 2008-2009 guidance plan includes projects addressing these provisions and donor advised funds. While I am familiar with a number of issues in these areas, I am not yet in a position to offer an opinion about an effective date for the supporting organization guidance being developed by the IRS and the Treasury Department. However, from my experience as a regulator in the securities industry, I recognize the importance of expeditiously issuing administrative rules after the passage of legislation. I can assure you that if confirmed, I will work with the Chief Counsel and the Treasury Department to implement this guidance project on a priority basis, and to establish an effective date that is based upon a careful and deliberate consideration of all relevant factors.

Regarding the other concerns you raise, if I am confirmed, I will update you within the first five months of my tenure.

Question 34

The IRS is to be commended for its efforts in revising the Form 990 for tax-exempt organizations. This is a vital document that provides transparency and openness to the public, the press and the Congress.

- a. There cannot be a delay in making this form and its schedules effective. I want your assurance that there will be no changes in the effective dates for the Form 990 and, particularly, for the Schedule H for hospitals.**

Answer

I am very much aware of the important work you have done to promote transparency with respect to the tax-exempt sector, as well as your suggestions for, and support of, the redesign of the IRS Form 990. I agree with the views that you and many others have expressed that the new form, including the new Schedule H for hospitals, will improve transparency and will do a much better job of providing the IRS the information it needs to assess compliance. If confirmed, I would support the Form 990 redesign and, I would expect to implement the entire form, including the Schedule H, in accordance with the timelines announced by the IRS last December.

- b. One of the most important tables on Schedule H is Part III dealing with community benefit. The IRS made the right decision in Part III by not describing bad debt and Medicare shortfalls as elements of "community**

benefit.” Bad debt and medicare shortfalls are inappropriate on several policy grounds, and including them allows nonprofit hospitals to provide a misleading picture of their work to policymakers, the public and the press. I want your commitment that there will be no changes to that table.

Answer

From my discussions with IRS officials, I understand that the new Schedule H, including the treatment of bad debt expense and Medicare shortfalls incurred by non-profit hospitals, was arrived at after extensive discussions with the non-profit hospital sector and significant public comment. While I am not an expert in this area, I believe the manner in which bad debt and Medicare shortfalls are to be reported on the new Schedule H reflects a reasonable view. If confirmed, I would support the new Schedule H, and I am committed to seeing that it is implemented in accordance with the timelines announced by the IRS last December.

- c. Regarding the Form 990, Senator Baucus and I raised the idea, in writing, to the IRS that there should be a separate schedule for nonprofit hospitals and also one for colleges and universities. I am pleased that the IRS has created a separate schedule for nonprofit hospitals, but I am disappointed that there was not one created for colleges and universities. The recent public debate about colleges and universities and their tuition, endowments and president’s salaries have all highlighted that there is much need for additional information in this area. I would ask that you contact the Department of Education, the members of the Spellings Commission, and other interested parties representing parents and students to review the benefits of having a separate schedule and what information should be included on a separate schedule. In addition, I believe that such a schedule should provide significantly more information about endowments – including details of how the funds are being used, investment advisory fees and other relevant information. The recent letter sent by the Finance Committee to colleges and universities on January 24, 2008, may be useful to review in this light. I ask for your commitment to undertake such a review now, and I ask you to provide a detailed written response by September 8, 2008.**

Answer

As in most parts of the tax-exempt sector, I agree that there is a need for transparency with respect to the nation’s tax-exempt colleges and universities. From my review of the revised Form 990, I believe it will go a long way toward getting that information in areas such as compensation, governance, and endowments. Whether ultimately that is sufficient for colleges and universities is a fair question. I understand that the IRS is undertaking a review of this important part of the tax-exempt sector. If confirmed, I

commit to reviewing this issue thoroughly, and I will gladly discuss my findings with you in the fall.

- d. The House Oversight Committee has recently held hearings on charities that are ostensibly created to benefit veterans. Unfortunately, too often, the real beneficiaries are the managers of the charities and their contractors. Chairman Waxman and Congressman Davis should be commended for holding these hearings. One statement from a witness who manages a veterans charity that was a subject of the hearing is of particular interest: "If we disclose, which I'm more than happy to do, we'd all be out of business. Nobody would donate. It would dry up." This statement, reported in the *Washington Post*, was in response to a question from Congressman Shays asking what would happen if his charities told donors how their donations were spent.

This witness's statement highlights why I am very frustrated that one of the few poor decisions the IRS made in regards to the new Form 990 was eliminating from the summary page the percentage of raised funds used for the charitable purpose. I recognize that a few charities complained, but the IRS should be putting the taxpayer first and, most importantly, the intended beneficiaries of the charity. This information is of great interest to the donating public. To say that the information is buried elsewhere in the Form 990 and schedules isn't satisfactory. I want your commitment now that the IRS will make as a top priority ensuring that on the summary page there will be easy-to-understand information about the percentage of dollars raised (not including transfers from other charities) that go to the actual charity purpose (with a tight common sense definition of what counts as charity purpose). I ask for an update on this matter every six months starting July 1, 2008. In addition, I ask that you provide by July 1, 2008, a complete written review of the issues raised by the hearings in the House on veterans charities including detailed discussion of all efforts you have taken within the authority of the Treasury and IRS to address these abuses through guidance, regulations, notices, enforcement and other actions. In addition, I ask that you also provide at that time any legislative reforms that you believe Congress should enact in response to these abuses. This review should consider not only veterans charities, but also "badge charities"—those involving fire and police officers – which have been the subjects of continual reports of abuse.

The House Oversight Committee's hearings on veterans' organizations, many of which are classified as tax-exempt organizations described in section 501(c)(19) of the Code, revealed instances of exorbitant compensation received by managers of these organizations. Currently, the excess benefits provision of section 4958 could not be imposed on these managers since section 4958 deals only with organizations

described in sections 501(c)(3) and (4). What are your views on making provisions of section 4958 applicable to organizations described in other subparagraphs of section 501(c)? How else do you propose to deal with exorbitant compensation involving 501(c)(19)s?

Answer

I find very troubling the prospect that managers of veterans' organizations, or any other tax-exempt entity, are receiving exorbitant compensation. People should not be taking advantage of tax-exempt status for improper purposes, and the IRS should be concerned when any tax-exempt organization appears to be spending funds for the wrong purpose.

On the issues of fundraising and efficiency, philosophically I agree that the IRS should facilitate the disclosure of how much of every donor's dollar is actually used for charity. As you note in the question, this was a controversial issue in the Form 990 redesign process. I have not had an opportunity to assess the sector's criticisms of the IRS attempt to use the form to enhance transparency in these areas, and I need to understand those concerns better before offering a perspective on it. However, I believe that the IRS should continue to explore ways to improve transparency, and if confirmed, I would maintain as a priority, improvements to accurate and complete reporting on the Form 990, including helping readers understand how and to what extent donations are used for proper purposes.

As to the issue of what tools the IRS has to address excessive compensation with respect to veterans' organizations, if confirmed, I will look at excessive compensation in this area and in other areas, and will work with you regarding ways to improve compliance in the non-profit sector.

Question 35

The Pension Protection Act required a report from Treasury/IRS regarding donor advised funds and supporting organizations. As discussed above, Congress took some steps to deal with the abuses that were highlighted by the IRS in the Pension Protection Act, but I am concerned that there is still much to be done. This report is months late. Please have the Treasury/IRS provide a copy of the report. This report will be incomplete if it does not include detailed findings, observations and conclusions along with recommendations for regulatory and guidance changes and any need for legislation. I have long been concerned that Treasury/IRS believes the report meets Congressional intent if it provides a summary of statements from interested parties – nothing could be further from the truth. I expect hard analysis and review of these areas that the IRS has consistently held up as long-time sources of abuse. We need to come to real solutions.

Answer

I understand your concern with this issue, and if confirmed, I will certainly look into this matter thoroughly.

Question 36

In the letter to the IRS regarding Form 990, Chairman Baucus and I also raised the issue of charities acting in a manner commensurate with their resources – the “commensurate test.” I would ask for your views on the commensurate test and what steps you will take to ensure that charities are acting in a manner that effectively benefits the public sector. What steps will you have the IRS take to ensure that charities are delivering public benefits commensurate to their resources? I am especially interested in your views regarding nonprofit hospitals, colleges and universities. I ask for your response to these questions now and written updates every six months on your actions in this area beginning July 1, 2008.

Answer

I do not yet have enough knowledge to offer an opinion about the test itself, although I believe this is an important area that warrants a closer look. I do know from my discussions with IRS officials that the IRS has a significant role to play in ensuring that charities act in a manner that effectively benefits the public. This may include, among other things, an assessment of whether an organization is providing public benefit that corresponds with its financial resources. I believe the new Form 990 made great strides in this regard.

I also believe your work, and the work of the Committee has been helpful in highlighting concerns in this area. If confirmed, and as I learn more, I will explore additional ways to assess whether an organization is providing public benefit consistent with its tax exemption, and to improve transparency regarding an organization's delivery of benefits to the public.

Question 37

Your predecessor, Mark Everson, showed tremendous leadership in the area of tax-exempt organizations. I want assurance that under your leadership, there will be no slippage in the priority and focus IRS gives to tax-exempt organizations. I want your commitment to make every effort to guarantee there is no aggregate reduction of support for the functions of examination, outreach and determination. In addition, I believe it is important in this area that we have someone in top management who has a good technical understanding of the relevant tax laws and the sector from day one. I ask for your assurance that when it comes time to replace the head of exempt organizations, the candidate will meet that criteria. I also ask for your assurance that there will be a significant

effort to recruit and hire individuals with experience in examination of tax-exempt organizations at the state level. There are a few states that do exceptional work and have shown real results in addressing abuses. The IRS would benefit from such individuals being part of its workforce.

Answer

You have my assurance if I am confirmed, that under my leadership there will be no slippage in the priority and focus the IRS gives to tax-exempt organizations. The charitable sector remains a vibrant and valued part of America and the world. Tax exemption does come with responsibilities, however. The IRS must ensure that this sector has what it needs to understand and meet the rules. I believe the IRS needs to do this with a balanced approach that includes both education and a healthy enforcement presence.

I intend to see that the IRS' Tax Exempt and Government Entities division is well supported and appropriately funded within the context of the overall IRS budget.

On the other matters you raise, certainly knowledge of the sector, technical understanding of the tax law, as well as executive, managerial, and leadership skills are desirable qualities for top management in the Tax Exempt and Government Entities functions, and I would continue to look for these qualities in my leadership team.

As to your question on hiring state investigators, my understanding is that the IRS has strong partnerships with the states' charity officials. In terms of hiring state charity investigators, I concur that individuals with excellent experience and demonstrated results in examining or investigating tax-exempt organizations at the state level would be valuable additions to the IRS workforce. If confirmed, I will explore what can be done to encourage such individuals to seek careers with the IRS, and to improve even further the strong partnership between the IRS and the states.

Question 38

The study on nonprofit hospitals is expected to be completed by September 2008. I want your assurance that you will make a priority of having this report completed by that time period. I also want your assurance that the report will include an assessment of the community benefit standard and recommendations (and timetable for implementation) for Treasury and IRS to implement all necessary guidance and regulations to ensure that nonprofit hospitals are providing real and valued benefits to those in need in their community. The interim report showed many problems with nonprofit hospitals and showed that there was significant variation in reporting of community benefits – with some reporting no community benefits. This demonstrates the need for clear rules and guidance in this area. In general, please provide me your views of whether the current situation regarding nonprofit hospitals – in which hospitals receive significant tax breaks and are not required by Treasury/IRS to provide any charity

care or real measurable community benefit – is acceptable. Please explain your views on whether you believe it is appropriate, and in keeping with a nonprofit hospital's charitable status, that a nonprofit hospital would charge an uninsured, low-income individual a rate three or four times (and often much greater) higher than an insured individual would be charged for the same service. Please provide any additional comments or observations that you have regarding this issue.

The fundamental change in the treatment of nonprofit hospitals, including the end of requirements for charity care, came with Rev. Rul. 69-545 (there was no change in statute). It has been said that the community benefit provisions of Rev. Rul. 69-545 were developed from a vast study of hospitals' tax exemptions. The study, authored by Robert S. Bromberg and published on December 20, 1968, is titled TS 65-30, "A Treatise on the Voluntary Hospital as a Charitable Institution," and it is my understanding that TS 65-30 contains no taxpayer information. Please submit a copy of TS 65-30 as well as the file on Rev. Rul. 69-545.

Answer

From my discussions with IRS officials, I understand that the IRS is working toward completion of the hospital study report by September 2008 and is on schedule to do so. If confirmed, I will drive hard to meet that schedule. I have been told that the project was designed to aid the IRS in gathering objective information on the extent of tax-exempt hospitals' community benefit activities. I also understand that the interim report included several recommendations regarding community benefit reporting and was instrumental in the IRS' development and release of the new Schedule H included in the redesigned Form 990. As I have suggested elsewhere in my responses, I believe the new Schedule H will enable the IRS to get a clearer picture of the tax-exempt hospital sector's activities, and more reliable data set with respect to the entire nonprofit hospital sector.

If I am confirmed, I will work to assure that the final report includes information that advances the understanding and debate on the community-benefit standards. At this point, I do not have enough background to tell you what the right answers are to the issues you raise on the standard itself or the charging practices of certain hospitals. I am hopeful that the IRS will gain sufficient information from its remaining work on the hospital study, from Schedule H filings, and from other work to provide a basis for assessing the continued relevance of the current standards.

As to the technical study and background file you requested, I must refer that request to the IRS and the Treasury Department since I do not have that information.

Question 39

As discussed above, the interim report by the IRS on nonprofit hospitals found that there were several hospitals that provided little to no community benefit.

Thus, I am stunned to find that hospitals are not included in the current audit plan for exempt organizations. I want your assurance (or the assurance of Treasury/IRS) that within thirty days of receipt of this question, there will be an inclusion of an audit plan for hospitals with a particular emphasis on those hospitals that have already admitted to providing little to no community benefit. I ask that you provide a written update on these examination efforts, findings and resolutions every six months beginning July 1, 2008.

Answer

As the nominee for IRS Commissioner, I have not been briefed on any IRS audit plans for tax-exempt hospitals or other taxpayers. If confirmed, I will make it a priority to look into this issue thoroughly and consult with you on these issues.

Question 40

The IRS issued a report on executive compensation that identified several instances of excessive compensation in private foundations and public charities. Please provide (or have the IRS provide) an update for each of these cases, including the status and a description of the general facts in each case. Additionally, please provide a written update of all audits involving excessive compensation every six months beginning July 1, 2008.

In public statements, IRS officials have stated that there were instances in which they found executive compensation that they believed would be viewed as excessive by the public (or even themselves), but was still reasonable under Treasury/IRS regulations and guidance. Please provide all examples of these findings that were identified by the IRS in relation to this report. Please detail how the IRS decided what was reasonable and what was not. Newspapers have been filled with accounts of salaries that have sparked public outrage, yet the IRS stated it didn't find widespread abuse. Why is this? Was the IRS looking at the right organizations, or does the IRS/Treasury have an inappropriate standard? Are IRS employees not using common sense, or does the statute need to be modified?

Answer

As I said in my response to Question 26 regarding veterans' organizations, I find the prospect that managers of tax-exempt organizations are receiving exorbitant compensation to be very troubling. I strongly believe that people should not be taking advantage of tax-exempt status for improper purposes, and the IRS should always be concerned when any tax-exempt organization appears to be spending funds for the wrong purposes. Because public trust is so important in the tax-exempt area, it is essential that the public have confidence that non-profit executive compensation is within acceptable bounds.

I recognize this as an important issue, and if confirmed, I will work to ensure that the IRS has an active presence in the area.

Question 41

I understand that the IRS has a work plan to examine colleges and universities. Given that colleges and universities are very much in the public eye, I ask for your assurance that this review will be made a top priority. I ask that the questions to colleges and universities be sent within three months and a final report within 18 months. Also, it is my understanding that the work plan will include an examination of endowments, UBIT, executive compensation and relationships with affiliates. These are important issues that need to be in the final report, and I ask for your assurance that they will be included. I expect this report to provide strong analysis as well as proposals for reform.

Answer

I recognize that colleges and universities constitute a significant part of the tax-exempt sector, and that some of the important issues raised by non-profit hospitals exist in this area as well. As you have noted, these include executive compensation and the level of revenues and savings used to deliver public benefit. I have been told by IRS officials that this is a top priority in the tax-exempt area in the coming year, and I agree that it should be. The specific areas you raise are extremely important. Although I do not have sufficient information to speak to the timelines you suggest in your question, I can say I am personally committed to the IRS' continued review and focus on college and university compliance in a timely manner.

Question 42

I wrote to the Secretary of Treasury last year regarding problems of abuse in land conservation easement donation and asked for proposals to address the continuing problems in this area. This has been a matter of extensive oversight by the Finance Committee. The answer I received from an assistant to the Secretary on October 25, 2007, was not responsive to my questions. I now ask that the IRS provide me a detailed, full and complete response to the questions I asked regarding the problems that are being seen in this area and solutions that the IRS and Treasury are proposing through guidance, regulations and any statutory changes that may be necessary. In addition, I ask for your personal assurance that there will be no reduction in the enforcement presence and activity of the IRS in the area of donation of easements for conservation and other purposes. I request an update on this matter by July 1, 2008.

Answer

I believe that conservation and preservation of land, natural resources, and architecture is important to our nation. I am aware that the IRS has focused on conservation

easements over the past few years and has observed problems in the areas of both land and building façade easements. I understand that many of these problems involve the proper valuation of the donated easement.

From my discussions with IRS officials, I understand that the IRS has dedicated significant resources to this compliance effort, and is attempting to resolve these issues and cases in a manner that respects the rights of the taxpayers and is consistent with the law and the particular facts and circumstances of each case. I have also been told that the IRS has worked with many constituents in the conservation and preservation sectors to attempt to identify areas in which further guidance is required so that the substantial charitable giving incentives made available by Congress to promote such giving are not thwarted by IRS enforcement efforts or unclear rules. It has been my personal experience that working with a regulated community can be extremely beneficial for the regulators and the community, and if confirmed, I would continue to support such outreach efforts.

I understand that proper valuation is a difficult issue here, as it is with many other non-cash contributions. Once again, I believe an appropriate balance of guidance and enforcement presence is needed in order to assure fair and equitable treatment of the donors and donees of these easements as well as proper administration of these tax incentives, which were designed to promote conservation giving. If confirmed, I will review the IRS' current efforts to ensure that the agency has an appropriate mix of resources dedicated to this area.

Question 43

One of the difficulties in addressing the tax gap is valuation of charitable donations. Congress has taken steps to address this in several areas in recent years, including car donations and clothing donations. However, it is too often the case that Congress gives the IRS the tools to do the job and the IRS doesn't use them.

I am troubled by the July 26, 2007, TIGTA report entitled "Improved Procedures Are Needed to Identify Noncompliance with the Reporting Requirements for Contribution of Motor Vehicles," which highlighted that the IRS was essentially not taking any action when taxpayers did not file a Form 8283. TIGTA estimated 104,846 taxpayers claimed unsubstantiated motor vehicle donations totaling approximately \$209 million for the tax year ending December 31, 2005. The JOBS Act (section 170(f)(11)) provided that no deduction is allowed if taxpayers fail to provide required documentation for property contributions if a deduction of more than \$500 is claimed. As a matter of standard practice, and as a matter of law, the IRS should deny a taxpayer a deduction for a car donation or other property with a claimed value above \$500 if they do not provide the proper documentation and forms. In addition, the IRS must have in place a system that allows for quick identification of taxpayers who have failed to file a Form 8283. Please provide your pledge that you will take these steps to ensure that these provisions in the

JOBS Act are properly and effectively enforced. I request a written update by July 1, 2008.

In the Pension Protection Act, Congress included language that addressed clothing donations – a billion dollar issue in the tax gap. Congress gave the Treasury/IRS broad authority to define and value clothing donations. This will aid the vast majority of honest taxpayers who want to do the right thing. As with car donations, Treasury/IRS has done little to nothing to take advantage of this authority and publish guidance. I request assurance that you will prioritize the publishing of detailed guidance for taxpayers that will provide certainty on valuations of clothing donations. Please provide a written update by July 1, 2008.

Answer

I believe strongly that people should be encouraged to give and that charities provide important services to our society. However, it is important that donors, as well as the charities themselves, comply with the law. I have been told that the IRS has taken numerous steps to ensure taxpayers and practitioners are aware of the new reporting requirements for the charitable donations of cars, clothes, and other items you referenced. I am aware that numerous publications, forms, notices, and instructions have been developed or revised to address the legislative changes that you also cited. If confirmed, I will review this issue and the plan for further guidance, and I will update you within five months of confirmation.

Private Debt Collection

Question 44

The Private Debt Collection Program was passed by Congress in response to a request from the administration. This program is designed to allow the IRS to collect revenues that would otherwise not be subject to collection action and also to allow the IRS to better allocate its own collection resources. Reports have shown that the private debt collectors have done an outstanding job in all respects and especially in regards to taxpayer rights – an area in which they have outscored IRS employees.

As mentioned earlier, one of the IRS findings has been that private debt collectors have done a better job at times than IRS employees in terms of taxpayer rights. In addition, the private debt collectors are vigorous in disciplining and firing employees who act in an inappropriate manner to taxpayers. Congress enacted section 1203 in the IRS Restructuring Act to ensure that IRS employees who acted improperly would be subject to discipline. The IRS Commissioner has authority to modify the sanctions imposed. I have reviewed the Commissioner's Semi-Annual Report on Disciplinary Actions for 7/01/2006 - 12/31/2006, and I am troubled to find many instances of IRS employees who would be subject to the full sanctions of 1203 or other statutes or regulations

being let off with a slap on the wrist. I am troubled that it appears the private sector is at times treating employees who act improperly towards a taxpayer with greater discipline than the IRS is treating its employees. Please inform me of your personal views on how you will use your authority to mitigate disciplinary penalties under section 1203 and elsewhere. I ask that you pledge to use such authority rarely. In addition, I am frustrated that the Commissioner's report often lists no mitigating factor, which raises questions of the extent to which Congressional intent is being followed. I ask for your pledge to ensure that this report is complete. Please provide my office an electronic copy of the most recent copy of the Commissioner's Semi-Annual Report on Disciplinary Actions.

Answer

This is an important issue and based upon my work with the IRS Restructuring and Reform Act of 1998, I can assure you that, if confirmed, I will review the report and fulfill both the spirit and the intent of the Commissioner's responsibilities on section 1203 violations.

With respect to the electronic copy of the most recent Semi-Annual Report, I must refer your request to the IRS since I do not have that information.

Whistleblower Program

Question 45

Due to my leadership, Congress changed the law in 2004 regarding rewards to whistleblowers who provide information leading to the recovery of significant amounts of taxes from corporations and wealthy individuals. These rewards are vital to encourage people to come forward, given that these individuals are often risking jobs and careers. The reforms to the Whistleblower Rewards Program were inspired by the great success of the False Claims Act, which has helped the federal government recover billions of dollars over the years. The Whistleblower Office has been created, and there is wide agreement that it has tremendous potential and possibilities. I also wish to commend to you the work of Mr. Stephen Whitlock and his colleagues at the Whistleblower Office in establishing this new program. However, I am concerned that Mr. Whitlock needs strong support from the Commissioner's office if this program is going to perform up to its great potential.

What is your opinion of the IRS Whistleblower Rewards Program?

Answer

At my confirmation hearing, I stated that the IRS must continue its rigorous enforcement programs. The agency must deter those who may be inclined to evade their legal tax obligations and pursue those who engage in tax evasion. I believe that the

Whistleblower Rewards Program plays an important role in helping to achieve those goals.

Question 46

Will you vigorously enforce the Whistleblower Rewards Program?

Answer

If confirmed, I will vigorously support the Whistleblower Rewards Program.

Question 47

Please provide me a discussion of how you will personally ensure broad public awareness and publicity about the Whistleblower Rewards Program to encourage participants, particularly those with knowledge of corporate tax fraud. Please provide me a written update every six months, beginning July 1, 2008, of your efforts to promote, publicize and otherwise support the Whistleblower Rewards Program.

Answer

From my discussions with IRS senior management, I am aware that the IRS has taken some steps already to publicize the Whistleblower Rewards Program. Whether this is sufficient or not, I cannot judge until I have had the opportunity to work directly with Mr. Whitlock. If confirmed, I will be pleased to discuss with you within five months of confirmation, and periodically thereafter, my efforts to promote, publicize, and otherwise support the program.

Question 48

Will you oppose efforts by industry groups, attorneys or others to weaken the Whistleblower Rewards Program?

Answer

You have my commitment that, if confirmed, I will work to ensure that the Whistleblower Rewards Program is not weakened and that it remains an important and effective tool for the IRS in targeting non-compliance by corporations and wealthy individuals.

Question 49

I am very concerned that the Whistleblower Office is being overwhelmed by its own success – that there is not adequate staff and resources to deal with all the

good cases coming in. Will you pledge to ensure that the Whistleblower Office has sufficient funding to vigorously pursue whistleblower claims?

Answer

As I mentioned in my answer to Question 47, if confirmed, I plan to meet with Mr. Whitlock to learn more about the program, its staffing, and its resource needs. It is certainly my intention that the Whistleblower Office be provided with sufficient funding to accomplish its purpose.

Question 50

Will you ensure that the budget of the Whistleblower Office is not reduced in a manner limiting the pursuit of whistleblower claims?

Answer

As I noted in the answer to Question 49, above, if confirmed, it is my intention to see that the Whistleblower Office is provided with sufficient funding.

Question 51

A significant concern with the whistleblower program has been the issue of providing whistleblowers sufficient information to assure them that the IRS is seriously considering the information provided, while also taking into account taxpayer privacy concerns. As these cases may often take years to come to fruition, the whistleblower often feels that the information provided to the IRS has been dropped into a black hole. The IRS does have authority to make disclosures to whistleblowers under its tax administration contract authority. My staff was promised over a year ago that guidance on what information can be disclosed to whistleblowers, and under what circumstances, would be forthcoming. Will you commit to having guidance issued by July 1, 2008 on this very important issue?

Answer

I appreciate the significance of providing interim status reports to participants in the whistleblower program in order for the program to be successful. From my discussions with IRS senior management, I understand that the IRS and the Treasury Department are drafting regulations that will address the disclosure of return information to whistleblowers and their legal representatives pursuant to written tax administration contracts, and that these regulations are expected to be released before the date you specify. If confirmed, I will make every effort to see that these regulations are released as soon as possible.

Question 52

Please assure me that you personally will make efforts to recognize whistleblowers whose work has benefited the IRS and also those IRS employees who have incorporated the work of a whistleblower to help them succeed at their jobs.

Answer

If confirmed, I will make efforts to recognize whistleblowers whose work benefits the IRS, as well as those employees who have used the work of whistleblowers in their enforcement efforts.

Question 53

One of the benefits of whistleblowers assisting the IRS is the ongoing dialogue and give-and-take between the whistleblower and the IRS. I am very worried that the IRS may be chilling those discussions by imposing on whistleblowers a "one-shot" rule – i.e., that there can be only one meeting with the whistleblower and the IRS, particularly when the whistleblower is a present employee. As I understand it, the concern is that if there are meetings after the initial meeting the whistleblower could be viewed as an agent of the IRS. This is an issue that the Department of Justice, in administering the False Claims Act, has successfully navigated. I ask for your pledge to consult with the Department of Justice as well as the qui tam bar regarding this matter, and to issue guidance by July 1, 2008, that will give common sense clarity to this issue and provide direction as to when multiple meetings between a whistleblower and the IRS can take place.

Answer

I understand that the benefits of the whistleblower program can be significant and the ability to engage in discussions with a whistleblower has the potential to enhance those benefits. From my discussions with IRS officials, I understand that the IRS is aware of this issue and is in the process of clarifying the rules for interactions with whistleblowers, including when it may be appropriate to have multiple meetings between the whistleblower and the IRS. If confirmed, I will make every effort to ensure that the IRS consults with the Justice Department and other stakeholders, and will make every effort to see that guidance on clarifying this important topic is provided within five months of my confirmation.

Question 54

I frequently hear from whistleblowers expressing concern that their submissions are not being sent to the field to be worked in a timely manner. I believe this could very well be a resource problem at the Whistleblower Office, but given the statute of limitations, it is important that this is corrected quickly. Speed in

providing information to the field will also, of course, assist the examiners in their important work. Please give me your pledge that you will review this matter and report to me on progress by July 1, 2008.

Answer

If confirmed, I will review this matter thoroughly and would be happy to discuss my findings with you within 5 months of confirmation.

Question 55

I am worried that in regards to 10% discretionary rewards, the guidance suggests that if a broad tax issue is identified on a company Audit Plan the whistleblower would not have an opportunity for a reward. This raises very real concerns for me that overly broad audit plans will be used as a justification to foreclose a reward. There is no doubt that a whistleblower can come forward with critical, valuable information (regarding information within an audit plan) that sheds detailed light on a taxpayer's actions and saves the IRS significant time and resources. I think there is a strong argument that such a whistleblower should be entitled to at least the 10% reward. I ask that you pledge now to review this matter closely and ensure that whistleblowers who provide important information will still be provided a reward. Also, I request a full, written response describing the actions you have taken in this regard by July 1, 2008.

Answer

If confirmed, I will review this matter thoroughly and would be happy to discuss my findings with you within five months of confirmation.

Question 56

I am concerned that whistleblowers may not be receiving their rewards in a timely manner. I am worried that whistleblower rewards are being delayed because the IRS may be taking the view that it must receive payment from all taxpayers prior to paying any share to the whistleblower. There seems to be no justification for this action. I request your commitment now to review this matter and any other issues that are delaying reward payments to whistleblowers. In addition, please provide a full, written response describing the actions you have taken in this regard by July 1, 2008.

Answer

If confirmed, I will review this matter thoroughly and would be happy to discuss my findings with you within five months of confirmation.

**Senator Olympia Snowe
Questions for Douglas Shulman**

Question 1

This question is asked on behalf of the Credit Unions in Maine. There are over 70-affiliated Credit Unions in Maine that provide great service to their 600,000 members, with low cost loans, checking and savings accounts. Maine's credit unions want to make sure that they are treated fairly and have equal access to the IRS Commissioner. In the past, one of your predecessors met with banking industry on different business tax issues but did not have similar meetings with the credit unions. If you are confirmed, will you strive to meet all types of interested parties and trade associations, and provide an open-door policy to receive and consider all viewpoints and perspectives on critical policy issues?

Answer

Yes. I believe that it is important for the IRS to stay in touch with a broad range of stakeholders.

Question 2

The nation's over 4,000 state credit unions, which are subject to unrelated business income taxation, have been concerned about the manner in which the IRS has attempted to impose an unrelated business income tax (UBIT) on fees from the sale of certain insurance products that appear to be fully consistent with credit union activities. Some credit unions felt that the IRS was imposing UBIT in an arbitrary way. They filed a suit earlier this year to stop the IRS from imposing UBIT. In your tenure, will you take steps to ensure that IRS policy decisions are not implemented in an arbitrary manner, and that all institutions that provide banking and credit services are treated fairly?

Answer

Yes.

**Senator Gordon Smith
Questions for Douglas Shulman**

Question 1

We have handled 58 IRS cases since January 2007. For comparison during that same time, we had 255 VA cases and 753 INS/State Department cases. If you use the number of cases to judge problems with federal agencies, you could fairly say that the IRS does a pretty good job.

That being said, within the IRS cases, there are two themes that appear:

- **Delays in processing non-profit (501(c)(3)) applications and**
- **Levies against Social Security benefits for IRS liabilities.**

Can you comment on these two issues?

Answer

I understand that there has been some frustration with the time it takes the IRS to act on applications for tax exemption. However, I also understand that there are some cases that are complex and may take more time to resolve. From my discussions with IRS officials, I believe that while the IRS must move expeditiously to give taxpayers certainty, it must not sacrifice the quality of the review. If confirmed, I will certainly look into this issue thoroughly, and I would be happy to discuss my findings with you.

As to levies against Social Security benefits, I understand that this is part of the federal debt collection law. If confirmed, I will review this matter carefully to determine whether there are issues with the way the law is being administered.

Question 2

I wanted to touch base with you on an issue of concern. As you know, in the last 20 years, many large companies have converted their traditional pension plans to cash balance plans. And this has caused a lot of concern because traditional plans are generally more favorable for older, longer service employees. Companies have tried hard to be sensitive to these concerns, and have put in various arrangements to try to take care of their older, longer service employees. The most favorable arrangement is one where the company promises to give their employees the better of the benefit under the old traditional plan or under the new cash balance plan. This automatically ensures that employees can't be hurt by the change.

IRS officials are now saying that these arrangements are illegal. There have been letters to the Treasury Secretary from both sides of the aisle asking that the IRS position be reversed, including a letter from the Chairmen and Ranking

Members of the Finance Committee and the HELP Committee. Could you please look into this issue personally and let me know where things stand?

Answer

I understand that the IRS released guidance in early February that is expected to help resolve this issue. If confirmed, I will look into this issue and would be happy to discuss my findings with you.

Question 3

There is one rather unique IRS program that I wanted to highlight. The Free File Alliance program is a public-private partnership between software providers and the IRS where the software companies provide free Federal and State tax preparation and e-filing to 70 percent of all taxpayers – all those with adjusted gross income below \$54,000.

The program is housed within the IRS website, with the link to Free File displayed prominently on the front page of the IRS website. Many states also utilize this same partnership program – my state of Oregon being one of them. In the free-file states, the same software companies provide free State return preparation and e-filing. It has proven to be a win-win for the taxpayers in my state – and for Oregon’s Department of Revenue.

I think it is very important to preserve and strengthen Free File. Since its inception, the program has donated over 23 million Federal returns and saved the federal government over \$37 million dollars. Reforms over the past several years have made it a consumer safety zone where taxpayers can get on the site, have their taxes prepared and e-filed for free – and then get off the site without any cross marketing or offering of refund anticipation loans. The program also provides bilingual tax preparation in English and Spanish.

In addition to the millions who now use Free File, there are thousands, if not millions of additional taxpayers across Oregon and the country that would benefit from this service – we need to make sure they know about it.

I know the Administration supports the Free File program; I want to know that I have your commitment to work with me and others to continue to expand usage, and improve and strengthen this program?

Answer

While I am not familiar with all the details of the Free File program, I am aware that it provides a valuable option for many low- and moderate-income taxpayers to meet their tax filing obligations, while also providing a significant benefit to the IRS by increasing

the number of returns that are filed electronically. You have my commitment that, if confirmed, I will work with you on this important program.

Question 4

We're about to experience an aging tsunami. The aging of our population will have a significant impact on many aspects of our society, including potential labor shortages and a potential brain drain. The effects of these trends can be mitigated if older workers decide to stay in the workforce longer.

In 2005, Senator Kohl and I asked the Labor Department to convene an inter-agency task force to develop legislative and regulatory proposals addressing the issues raised by the aging of our workforce. We asked that the task force be comprised of all of the federal agencies that deal with issues facing older workers, including the IRS. The Labor Department is expected to issue their first report any time now.

- **The IRS has participated in this initiative. As IRS Commissioner, will you direct the IRS to continue to participate in this older workers task force?**

Answer

Yes.

- **What are your thoughts on the aging of our workforce?**

Answer

I am aware that many knowledgeable and experience IRS employees will be approaching retirement eligibility in the coming years. Thus, it will be crucial to recruit, train, and groom the next generation of IRS leaders. At the same time, if confirmed, I would want to explore ways to keep valuable, older workers on the job.

- **Is the IRS seeing an aging of its workforce? If so, do you have any suggestions on addressing the issue?**

Answer

The aging of the IRS workforce will require a multi-pronged response. One aspect, as you suggest, will be to explore opportunities to have older workers stay on the job longer. This will require new thinking on what it takes to make the workplace attractive to those who could otherwise retire at any time.

This trend will also spotlight the IRS' ability to develop the next generation of subject matter experts and leaders. I am a strong advocate for proactive leadership

development and succession planning. I believe the IRS will need to identify future leaders early in their careers, and expose them to as many different experiences as possible.

**Senator Jim Bunning
Questions for Douglas Shulman**

Question 1

How does the IRS intend to deter fraudulent efforts to obtain economic stimulus rebate checks via the Internet or other means?

Answer

As a nominee, I have not had discussions with IRS officials about the administrative details surrounding the recent stimulus legislation. I am confident that it will be IRS' priority to get rebate checks to the appropriate parties as soon as possible. I have been told that the IRS has fraud detection systems in place for its programs, and if confirmed, I will look into what systems it has in place to prevent fraudulent claims for rebate checks.

Question 2

Are IRS audits as effective today as they were in the past in discovering and deterring non-compliance?

Answer

I do not have sufficient information to offer an opinion on the effectiveness of IRS audits today versus in the past. However, from my discussions with IRS officials, I understand that today the audits the IRS conducts are effective. The IRS has been able to utilize technology to reach more people from a compliance perspective than ever before. I also understand that one of the results of this has been the steady increase in enforcement revenue climbing from \$34 billion in FY 2002 to over \$59 billion in FY 2007.

Question 3

Should the audit rate be the primary measure of IRS performance in enforcing tax laws? What other objective, historically comparable measures, other than the IRS budget and number of employees, should Congress and the public use to measure IRS performance?

Answer

This is an interesting question and one I deal with in my current job. It is very difficult to assess the overall effectiveness of an organization like the IRS, but easy to measure outputs like the number of audits, enforcement revenue, number of employees, etc. Other outcomes are much more difficult to measure, and it is even more difficult to determine how they can be used to determine the overall effectiveness of the organization. I am unable at this time to identify any single objective standard that should be used to evaluate IRS performance. If I am confirmed, and once I have an opportunity to work within the IRS, I should be able to respond to this question.

Question 4

Approximately how many individuals who are required to file, fail to file a federal income tax return every year (i.e. the number of non-filers)?

Answer

I understand the IRS estimates that for Tax Year 2001, about 13.5 million filing units (or around 11 percent) required to file an individual income tax return did not meet their filing obligation. Historically, I am told this percentage has fluctuated in a relatively narrow range around 10 percent.

Question 5

How do you intend to promote electronic filing? What is your opinion of the proposal to extend the filing deadline 15 days for taxpayers who file and pay electronically?

Answer

From my discussions with IRS officials, I am aware that the IRS is already taking steps to promote electronic filing. In addition, I understand the IRS has already begun a study of ways to advance electronic filing that will include direct filing options, mandates, and bar coding of computer generated paper returns. If confirmed, I intend to review the results of the study carefully and consider what additional steps the IRS can take to meet the 80-percent e-filing goal set by Congress. With respect to your specific question, I need to study the proposal to extend the filing deadline for electronic filers before offering an opinion. It is an interesting idea that could have a significant effect on e-filing, and if confirmed, I will certainly give it serious consideration.

Question 6

How do you intend to improve the IRS's training of revenue agents and officers? How important is training?

Answer

Based on my prior experience, I recognize that a well-trained workforce is essential to the success of any organization. If confirmed as Commissioner, I will make it one of my priorities to ensure that the IRS has the appropriate and necessary training for its workforce and, in particular, make sure that employees are trained to stay current with the tax law. I will ensure IRS employees are equipped with the right tools to carry out their appointed duties.

While I have not yet had the opportunity to review the full complement of IRS training programs, I understand the challenges associated with training new recruits, as well as keeping the technical workforce prepared to face new tax law issues. While at FINRA, we confronted similar challenges in developing and maintaining a high level of specialized expertise among the workforce. We established "Examiner University" – a comprehensive training program for new examiners that combines intensive classroom instruction with mentoring and on-the-job training. We also enhanced the level of training available to experienced staff members. If confirmed, I would envision bringing similar creative solutions to the training and development of IRS employees – new recruits and experienced staff alike. Providing employees with proper training and professional development opportunities would be an important theme under my leadership.

Question 7

To what extent should the Internal Revenue Manual be binding on IRS employees?

Answer

My understanding is that IRS employees look to the Internal Revenue Manual for direction and guidance and are expected to follow its relevant provisions. I have been told, however, that the Internal Revenue Manual is not intended to be legal guidance for taxpayers.

Question 8

What is your opinion of proposals to require paid income tax preparers to register with the IRS and meet educational requirements?

Answer

I believe that taxpayers deserve to get knowledgeable, professional, and honest service from preparers. I believe that the IRS already has a variety of tools at its disposal to ensure that these high standards are met, including the bully pulpit, education, dialog, and outreach, and where appropriate fines and disciplinary actions.

I am intimately familiar with registration and regulation of professional service providers in the financial services industry. If confirmed, I would give careful consideration to the issues surrounding the registration and regulation of preparers.

Regulation has clear benefits, but it also comes with costs. Regulation puts an additional burden on preparers, especially those who are already capable and ethical. It also imposes industry-wide costs, which inevitably would be borne by taxpayers. Before mandating regulation, I believe we need to ensure that the benefits in terms of improved compliance outweigh the costs and burdens that such regulations would impose. Finally, regulation of tax preparers would require IRS senior management attention and financial resources that would otherwise be devoted to other aspects of tax administration, namely taxpayer service and enforcement.

If confirmed, I would look all of these issues with an open mind, and I look forward to the opportunity to study the issue further.

Question 9

Would registering preparers be less burdensome if the IRS certified training programs provided by third parties instead of directly administering a test, similar to the program run by the State of California?

Answer

I would have to become more familiar with the program you mention in California, as well as what would be involved for such an operation within the IRS, before I could offer an opinion on that approach. If confirmed as Commissioner, I would review that proposal carefully.

Question 10

Does the IRS have plans to design and implement customer relationship management (CRM) software that will allow IRS agents to interact with taxpayers over the telephone with concurrent access to relevant taxpayer information?

Answer

I have been told that the IRS is currently implementing a project called Accounts Management Services (AMS) that addresses your question. As I understand it, AMS is part of the IRS Business Systems Modernization (BSM) program, and is being developed in conjunction with the Customer Account Data Engine (CADE), which is the project to replace the IRS antiquated master files. The vision, which I support, is to enable IRS employees to have real-time access to taxpayer data for customer service and enforcement needs.

Question 11

As you know, taxpayers sometimes face a difficult task to understand how court precedents apply to them. Would you propose streamline the jurisdiction of federal courts and the U.S. Tax Court to hear tax claims, and, if so how?

Answer

I understand that tax litigation can create complexity and inconsistency. However, I am not in a position to have an opinion on the jurisdictional issues you raise. If confirmed, I would be happy to discuss with the Treasury Department and Congress any changes that would streamline jurisdiction in a way that would enhance tax administration and preserve taxpayer rights.

Question 12

Are changes needed to the Internal Revenue Code to enhance the IRS and Justice Department's ability to defend civil tax claims against the United States or prosecute tax crimes? What changes would you recommend?

Answer

I am told that the IRS and the Tax Division of the Justice Department have an excellent working relationship, and if confirmed, I would expect that to continue. As a nominee, I do not have sufficient information to offer recommendations for changes that could enhance the government's ability to litigate civil tax claims or prosecute tax crimes. If confirmed, I would look into this matter and coordinate closely with tax policymakers to resolve any issues inhibiting the IRS' ability to enforce the tax laws.

Question 13

What is the proper role of the IRS in the tax legislative process?

Answer

The IRS Restructuring and Reform Act provided some guidance on this issue by providing for a "tax complexity analysis" and a sense of the Congress that the IRS Commissioner should have a "seat at the table" during consideration of tax legislation. This indicates that Congress has an interest in hearing from the IRS about the tax administration implications of proposed tax legislation.

I believe that the proper role of the IRS is to provide the Congress with an understanding of how proposed tax legislation could affect taxpayers and what it would take for the IRS to implement particular tax legislation.

Question 14

Should there be an exemption from federal fuel tax for fuel used by power take off equipment on commercial vehicles? How should the exemption be measured?

Answer

I am not familiar with this issue, and as a nominee, I do not have sufficient information to offer an opinion. Thank you for bringing it to my attention, and I will be happy to look into it more closely if I am confirmed.

Question 15

What role should tax practitioners play in tax administration? And, how do you intend to promote a constructive relationship with practitioners?

Answer

As I noted during my confirmation hearing, I believe it is essential that the IRS work closely with the practitioner community, including lawyers, accountants, and tax preparers. If confirmed, I will make sure that the IRS uses all the tools at its disposal – dialogue, education, service, and enforcement – to ensure that these important members of the tax community are partners in the IRS' efforts to see that all individuals and institutions meet their tax obligations.

Question 16

What is your opinion of the Joint Review process created by the IRS Restructuring and Reform Act of 1998, now that it has expired?

Answer

I think the notion of bringing all the Committees with jurisdiction over the IRS together once a year to examine the programs and operations of the IRS was a good idea.

Question 17

Are you in favor of publishing more guidance for taxpayers or resolving more disputes on an *ad hoc* basis, through the audit process?

Answer

I believe that taxpayers are most compliant when they are provided with clear, consistent, and prompt guidance. Thus, I see guidance as an integral tool in tax administration. However, I also believe that having a strong audit and enforcement presence is necessary to deter those who may be inclined to try to evade their tax

obligations and to pursue those who engage in tax evasion. I will, if confirmed, review the level of published guidance produced by the IRS and ensure that appropriate resources are provided for both published guidance and audit activities.

Question 18

How would you maintain the independence of IRS Appeals?

Answer

I agree with Congress in the IRS Restructuring and Reform Act that a healthy tax administration system requires an independent forum in which taxpayers can seek to resolve their tax disputes with the government without having to resort to litigation. From my discussions with IRS officials, I understand that the IRS Appeals office resolves over 80,000 cases every year, and I believe that for it to continue to be an effective dispute resolution function, it is essential that the Appeals office maintain public confidence that its work and determinations are fair and impartial to both the government and the taxpayers. If confirmed, I would work with the leadership of the Appeals office, as well as with external stakeholders, to listen to and discuss any areas for improvement. I would also strongly support the integrity and independence of this critical function of tax administration.

Question 19

Would it help the IRS to do its job if the agency invested in knowledge management software, such as the software used by major accounting firms?

Answer

In discussing this question with IRS senior management, I learned that the IRS has no current initiative underway to implement such knowledge management software on an enterprise basis. While implementation of a comprehensive knowledge management program can be beneficial to any large and complex organization, it has been my experience that it is a highly labor intensive and high-risk process. If I am confirmed, I would assess the viability of implementing such an enterprise program in the face of other critical priorities and by also assessing the effectiveness of the IRS current approach to knowledge management.

Question 20

Does the IRS plan to develop return filing software that would compete with third-party commercial software that is currently available?

Answer

I do not believe the IRS has plans to develop return filing software. As I noted earlier, I understand the IRS is studying ways to advance electronic filing that will include direct filing options, mandates, and bar coding of computer generated paper returns. If confirmed, I intend to review the results of the study carefully and consider additional steps the IRS can take to meet the 80-percent e-filing goal set by Congress.

Question 21

What challenges does the rise of internet commerce create for federal tax administration?

Answer

I believe that the internet offers both opportunities and challenges to tax administration. It can fundamentally change the way taxpayers interact with the IRS and enable the agency to meet the needs of taxpayers, the tax professional community, and the American public in new and exciting ways. At the same time, the rise of identity theft and other cybercrimes, means the IRS will have to devote time, energy, and resources to thwart attacks and efforts to undermine the integrity of the tax system. If confirmed, I look forward to leading the IRS in this important work.

Question 22

What administrative changes should the IRS make to assist the IRS in deterring improper offshore tax avoidance and evasion? Should the IRS place at least one agent in the U.S. embassy of every major trading partner?

Answer

From my discussions with IRS officials, I understand that offshore accounts can be among the most complex to investigate and ensure that they are in compliance with the tax laws. As you suggest, some of those taxpayers who use offshore accounts for questionable purposes are quite sophisticated. In order to combat these forces, I would take a multi-pronged approach. First, I would ensure that highly qualified employees are assigned to these cases (with the additional benefit that interesting projects tend to motivate and retain top people). Next, I would engage in dialog with foreign tax administrators, and use existing treaties and information sharing agreements to their fullest extent. Finally, I would use the bully pulpit of the Commissioner's office to make it known that cracking down on misuse of offshore accounts is a priority for the IRS. If confirmed, the allocation, placement and utilization of IRS resources to support international tax compliance will be an area that I will need to explore in greater detail.

Question 23

How do you intend to address the tax administration challenge caused by the declining percentage of taxpayers who pay their federal tax liabilities through pay check withholding?

Answer

Everything that I have read about reducing the tax gap points to two important factors. First, there is a need for greater transparency. The greater the transparency, the higher the level of voluntary compliance. The second factor is third-party reporting. Like transparency, compliance is greater when the taxpayer is aware that there is third-party reporting. Therefore, if confirmed, I will work closely with the Administration and Congress to examine ways to provide greater transparency and proposals for third-party reporting.

Question 24

Do you foresee making changes to the offer in compromise process? What changes are needed?

Answer

At this time, I am not sure what, if any, changes need to be made to the Offer in Compromise Program. From my discussions with IRS officials, however, I see real value in this program. Based on my understanding of it, I believe the program results in the collection of tax revenues that might otherwise not be collected. If the IRS is going to be serious about improving compliance, the agency needs to be willing to use all the tools available, and I view the Offer in Compromise Program as being one of those important tools. If confirmed, I will take a close look at how this program functions, and I would be happy to discuss any recommendations you may have to improve it.

**Senator John Ensign
Questions for Douglas H. Shulman**

Question 1

Mr. Shulman, as you may know, the Finance Committee has debated several proposals that would have the Internal Revenue Service (IRS) provide tax preparation for all taxpayers. It has been called "return-free" or a "web portal" or "direct filing" in its various incarnations. All of these terms are code words for the government preparing the tax returns of the taxpayer. Testimony and studies have indicated that such systems could cost over \$500 million to build and over \$100 million per year to maintain and update for each new tax season. In total

such a proposal would cost a billion dollars over 5 years. Many of us on this committee, including myself, are strongly opposed to this idea. It is an inherent conflict of interest for the tax collector (IRS) to also be the tax preparer. Having the government prepare the tax returns of its taxpayers would not benefit the taxpayers.

With that as background, do you intend to maintain the current policy stated publicly before this committee in testimony by Secretaries Snow and Paulson, and from IRS Commissioner Everson, that the IRS will not pursue nor does it want to pursue being involved in tax preparation except through the VITA or the Free File Alliance programs?

Answer

Although I am not completely familiar with this issue, if confirmed, I would not intend for the IRS to be in the business of preparing tax returns. I believe that tax software providers play a vital role in our tax system, and I understand that they work closely with the IRS to ensure technology is available to meet taxpayer needs and the IRS' processing requirements. From my discussions with IRS officials, I also understand the IRS is currently conducting a study, requested by Congress, on the subject of how to increase the number of returns filed electronically. I am told that study will look at a number of options including creating a direct filing option and e-filing mandates. If confirmed, I will review very carefully the results of that study and consider any recommendations it makes.

Question 2

Mr. Shulman, if the IRS is forced by legislation or acts on its own to provide tax preparation through a web portal or return free system it would immediately terminate the successful Free File Alliance program, which already provides free Federal and State tax preparation and e-filing to 70% of all taxpayers. This action would also create an unfunded mandate on 21 states and force them to build their own tax preparation systems because these states currently utilize the Free File Alliance program to have their state returns prepared and e-filed.

Do you think it is wise during difficult budgetary and economic times to put such an unfunded mandate on the states and force them to divert several hundred million dollars from other important priorities to build a system when today they already get the service for free?

Answer

While I am not familiar with all the details of the Free File program, I am aware that it provides a valuable option for many low- and moderate-income taxpayers to meet their tax filing obligations, while also providing a significant benefit to the IRS by increasing the number of returns that are filed electronically. I believe any policy change in this

area will require careful study and evaluation, especially with respect to potential affects on the IRS' relationship with state and local governments. If confirmed, I will take the time to get to know more about this important program.

Question 3

Will you pledge to support the Free File Alliance program and work with me to continue its improvement during your term as IRS Commissioner?

Answer

As noted above, I do not have a great deal of familiarity with the Free File program, but I recognize that it provides a valuable service to millions of low- and moderate-income taxpayers. If confirmed, I pledge to get to know more about this important program and would be happy to discuss my findings with you.



COMMISSIONER

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

FEB 21 2008

The Honorable Charles E. Grassley
Ranking Member
Committee on Finance
United States Senate
Washington, DC 20510

Dear Senator Grassley:

Following the Finance Committee's confirmation hearing for Doug Shulman on January 29, 2008, you asked that the Internal Revenue Service provide agency-level responses to a number of the questions for the record that you posed. Attached, please find the responses to those specific questions along with a study requested by one of the questions.

If you have any questions, please contact me or Floyd Williams, Director, Legislative Affairs, at (202) 622-4725.

Sincerely,

A handwritten signature in cursive script that reads "Linda E. Stoff".

Acting Commissioner

Attachments

**Response to Questions Presented by
Senator Grassley**

General Questions

Question 4

It has been suggested that the tax withholding crisis in the banking industry is due to the lack of audits on hedge funds to whom the banks sold the withholding products, and that this has caused banks to be overly aggressive. What are your plans in this regard, and what is your general strategy for future industry examinations? Given your background in the financial industry, what do you see as the top priorities of examination in this area? Where do you think the IRS needs to do more auditing and examinations in the financial industry?

Answer

The IRS continues to develop tax-withholding issues through compliance efforts, including examinations of hedge funds. To date, we have found that various transactions, although aggressive, are not necessarily abusive in light of current withholding tax rules. Accordingly, in addition to undertaking compliance initiatives, we are working to identify changes to current income tax regulations that would address more appropriately the treatment of these emerging products and transactions. For example, improved disclosure and transparency by promoters and investors is one possible solution to identify these and other aggressive tax planning transactions better.

Question 5

The GAO has reported that the IRS does not use all the tax return information it receives for its automated compliance checking programs. In essence, IRS policy is to post the same lines from electronic and paper returns to its enforcement databases. This means that IRS employees are dealing with only limited information and many individuals who file electronically are potentially needlessly contacted because of additional information that is available. Please provide me your commitment that within the next few months the IRS will post, and continue to post, all lines from electronic returns to its enforcement databases.

Answer

One of the tenets under which the IRS has operated since adopting e-filing has been that all taxpayers will be treated in an equitable manner, irrespective of how a taxpayer files a return. This policy has allowed the IRS to market e-file successfully and has contributed to the steady growth of the program. For Form

1040 filing, the rate of e-filed returns has gone from slightly over 30 percent in 2001 to more than 57 percent last year. The answer to the question you raise seems to lie in how to obtain more data from paper-filed returns without transcribing additional lines from the paper returns, which is very expensive.

The IRS recently began a study to produce a comprehensive overview of current taxpayer characteristics, identify potential ways to increase electronic filing, and make recommendations, as appropriate, for legislative actions that could enable the IRS to reach the 80-percent e-file rate goal Congress has set for the agency. As part of this study, we plan to further address your question, with particular emphasis on the use of 2-D bar coding to enable the IRS to obtain information more easily from paper returns, along with continued evaluation of various paper transcription approaches as more taxpayers e-file and overall paper-based return volume is reduced.

We would be happy to meet with you or your staff to discuss your concerns regarding this issue and any other options you might recommend.

Question 6

I asked a question about IRS members doing union work at your nomination hearing. Please provide a more complete answer and note that I do not consider your stated lack of familiarity with IRS hiring practices and procedures to be part of a satisfactory response. I have heard continuously from the IRS, the NTEU and some members of Congress that there are not sufficient employees at the IRS to do the job. At the same time, there are thousands of FTE's at the IRS doing union work at taxpayer's expense. This makes no sense to the American people.

Treasury has informed me that the number of union hours at the IRS is greater than the average in the federal government. I want your assurance that Treasury and IRS will only sign a union contract that provides for no more than the average number of union hours in the federal government. In addition, if a new contract is not signed, that you will take action within 60 days to limit union hours to no greater than the average number in the federal government and ensure that no IRS employee will spend less than 10% of their work time directly or indirectly on union activities. Please provide in detail what benefits will be realized by reducing the number of union hours to the federal average – in terms of additional hours for taxpayer service, audits, collections, enforcement and other activities. Please discuss in detail the impact this will have on addressing the tax gap. Please inform me of the number of IRS employees that are currently spending more than 10% of their time directly or indirectly on union activities.

Answer

During Fiscal Year 2006, the IRS average use of official time by union representatives was 7.5 hours per bargaining unit employee. This compares to the Office of Personnel Management's stated government-wide average for use of official time by union representatives of 2.57 hours per bargaining unit employee. During that year, the IRS spent 416,630 hours in excess of the average rate, or 200 staff years above the government-wide average. The latest figures show that 569 IRS stewards spend more than 10 percent of their official time on union activities.

One of the ongoing priorities in the IRS' labor relations strategy is to bring official time usage in line with government-wide averages. The IRS 2002 National Agreement with the National Treasury Employees Union (NTEU) established controls to monitor and reduce the use of official time. The agreement requires Local Official Time Utilization Plans (LOTUP) for each NTEU chapter. These plans are reviewed annually, and chapter presidents must justify union full time stewards. The 2006 re-opener for the National Agreement further strengthened controls to reduce the use of official time by requiring that all local chapters operate within an established LOTUP. These steps helped the IRS realize a reduction of 97,725 official time hours over the past three years. The IRS will pursue further controls to reduce official time during bargaining for a new IRS/NTEU National Agreement.

Compliance and Collection Activities**Question 16**

GAO also made recommendations to strengthen the Offer In Compromise program [IRS Offers in Compromise: Performance Has Been Mixed; Better Management Information and Simplification Could Improve the Program. GAO-06-525] by reducing staffing to match workload; better measuring performance; setting timeliness goals for each taxpayer; analyzing trends in repeat offers, timeliness, and access; and eliminating offer types that are not meaningfully distinct. IRS has reduced staffing and is analyzing repeat offers.

When will the analysis of repeat offers be completed and what will you do to ensure implementation of the other recommendations?

Consistent with GAO's recommendations, the IRS is continuing to strengthen the Offer in Compromise (OIC) program. The GAO report made several recommendations that the IRS is implementing to strengthen the program. We recognize that the OIC program is important and can benefit both taxpayers and the IRS.

The IRS adopted the GAO recommendation to study repeat offers from the same taxpayer. Preliminary data shows that changes made to the program to reduce the number of offers returned for procedural errors have had the intended effect of reducing repeat offers. We expect to complete the repeat-offer study within the next 90 days and will analyze the results to see if other changes in procedures are warranted.

The GAO also recommended that we adopt timeliness goals based on taxpayer needs, and we have instituted several customer satisfaction surveys to assist in that effort. These surveys also focused on what can be done to make the program more accessible. Also consistent with the GAO's recommendations, we have reduced staffing in the program to match current workload. Staffing is monitored and controlled at the headquarters level to ensure it is appropriate for anticipated workload. Finally, we have clarified the differences between various types of offers through more detailed guidance on our website and in the OIC application package.

Veterans

Question 26

The nation is seeing a significant number of veterans, many of whom are disabled, returning from Iraq and Afghanistan. These are extraordinary young men and women, and our country is honored by their service. There is no question that these men and women are extremely capable. I think it is important for the federal government to do all that it can to hire these returning veterans, and it is clear that the IRS offers many opportunities for these servicemen and women, particularly the disabled. These veterans will bring to the IRS a good deal of much-needed youth, a fresh outlook and experience and, most importantly, a "can do" attitude that is much needed. The IRS will greatly benefit from these veterans joining its ranks.

I raised this issue during your nomination hearing and would like you to answer in greater detail. I want your commitment to set a goal of hiring one thousand Iraq and Afghanistan veterans this fiscal year, with a particular emphasis on those who are disabled. Please provide me a discussion of how you will seek to implement this goal, including outreach, job classifications and reclassifications, notification, working with veterans' organizations, and working with the Department of Veterans Affairs and the Department of Defense. In addition, if there are any legislative changes that will aid or assist this effort, please identify them. However, I am confident that the IRS has significant authority at hand to accomplish this goal.

Answer

The IRS has a strong commitment to hiring veterans. We have made the recruitment of returning veterans a priority. Working with "Operation War Fighter" and the Department of Veterans Affairs (VA) "Coming Home to Work" initiative, the IRS is building the relationships and the tactical agility to take advantage of a very valuable pool of potential employees to fill available openings at the IRS. The IRS is dedicating staff and resources to reach out to veterans and military professionals, both within the military and through the nation's veterans' organizations and advocacy groups. A new recruitment program has been designed that focuses on outreach efforts to assist our military veterans in identifying opportunities to transition into the federal civilian workforce. For example, the IRS attends at least 20 military career fairs per year. The IRS has also met with officials of the VA to explore opportunities to provide IRS technical training to our armed service men and women. While this is not an employment program, this training would provide skills that will make these veterans more competitive when applying for IRS positions. In order to facilitate implementation of this program, IRS will provide instructors and training material to assist in the development of these veterans. The IRS' goal is to assist our nation's heroes in finding the best match between their own education, experience, and competencies and the rich and varied occupations at the IRS..

While the IRS is dedicated to hiring veterans, it should be noted that hiring authorities exist to hire all veterans, but these authorities are not exclusive to veterans of the Iraq and Afghanistan campaigns. OPM regulations governing the competitive hiring process, under which Executive Branch agencies must operate, require equal preference be given to veterans regardless of the reason for which preference is conferred.

Financial Management**Question 30**

IRS continues to face many challenges in its ongoing efforts to improve the accuracy and reliability of its financial and information management systems and to correct internal control weaknesses. For example, despite notable progress and despite having received clean, or unqualified, audit opinions on its financial statements for many years, financial management at IRS has been on GAO's high-risk list since 1995, first as a separate issue and later as a component of the IRS Business Systems Modernization high risk area. Although IRS again received an unqualified audit opinion on its financial statements in 2007, it continues to need to manually analyze and correct data generated by its financial systems. This approach does not produce timely information for managing the agency.

What are your views on the need for IRS to modernize its financial management systems, and do you view this as a high priority for the agency? What benchmarks should we use to monitor and measure your performance in this area?

Answer

In its *IRS' Fiscal Years 2007 and 2006 Financial Statements* report, the GAO states:

In fiscal year 2007, for the eighth consecutive year, IRS was able to produce financial statements covering its tax administration and nontax administrative activities that are fairly stated in all material respects. However, until IRS resolves the issues affecting the automated systems it relies on to process the administration of tax-related transactions, it will continue to be challenged to sustain the level of effort needed to produce reliable financial statements in a timely manner.

As a result of these issues, the GAO included the need to improve custodial financial management systems in its Business Systems Modernization high-risk report. The IRS is addressing these issues through the implementation of the Custodial Detail Data Base (CDDB) and the redesign of the Interim Revenue Accounting System (IRACS).

CDDB is an enhancement to the Financial Management Information System (FMIS) and will serve as the sub-ledger for unpaid assessments, revenue, and refunds to IRACS. The sub-ledgers will provide transaction-level traceability to support and prepare the custodial financial statements. CDDB is being implemented through four releases over three years. The IRS implemented Release 1 of CDDB for unpaid assessments in 2006. The IRS implemented Release 2 for revenue and refunds in October 2007 and is expanding the use of CDDB for the FY 2008 audit to include available revenue and refund data that should accelerate the FY 2008 audit cycle by two weeks. Release 3 will be implemented in FY 2008, and Release 4 is scheduled to be implemented in FY 2009.

Each release of CDDB further addresses the material weaknesses in financial reporting that the GAO identified, and the increased degree of IRS compliance with federal accounting standards is measured and validated each year by the GAO in the financial statement audit. With full implementation of CDDB in FY 2009, the IRS expects to be compliant with the Federal Financial Management Improvement Act (FFMIA) of 1996.

IRACS Redesign is a FY 2009 Modernization, Vision, and Strategy (MVS) initiative that will add the United States standard general ledger to the IRACS

database, implement enhanced interfaces with future releases of CADE (the modernized master file) and CDDDB to support the summary general ledger totals with detailed data, and automate complex manual processes that the GAO believes have put the audit process at risk.

The IRS already has benchmarks to monitor its progress. The IRS reports its progress on tax revenue financial management system improvements on a quarterly basis to the Department of Treasury and the Office of Management and Budget (OMB) as updates are available to the remediation plan developed to correct the revenue financial reporting material weakness identified by the GAO. The IRS also reports its progress to the Financial Management initiative that is part of the President's Management Agenda (PMA). Updated plans include milestone dates to bring the revenue financial management systems into FFMIA compliance. In addition, GAO provides updates on the status of IRS revenue financial management system improvements in its annual financial statement audit report.

Question 31

When can we expect to see the kinds of changes implemented that will enable GAO to remove financial management at IRS from its high-risk list? Please provide specifics that we can use to monitor and measure your performance in this area.

With full implementation of CDDDB in FY 2009, the IRS expects to be compliant with FFMIA, and at the conclusion of the FY 2009 audit, the IRS expects the GAO to reduce the material weakness on custodial reporting. The implementation of the redesigned IRACS in January 2010 should substantially resolve the GAO's issues with the custodial accounting system and result in the removal of financial management from its high-risk list.

As stated in the response to Question 30, the IRS reports its progress on financial system improvements on a quarterly basis to the Department of Treasury under the PMA Improved Financial Management initiative and in the remediation plan. Updated plans include milestone dates that ultimately will bring the IRS custodial financial management systems into compliance with FFMIA. In addition, the GAO provides updates on the status of IRS financial management system improvements in its annual audit report.

Nonprofit/Tax-exempt Questions

Question 33

The IRS has consistently stated that Supporting Organizations are one of the most abusive areas in the field of exempt organizations. Congress

passed legislation to address this matter in the Pension Protection Act and the Treasury/IRS issued regulations in this area last year. A key component of these regulations is a requirement of a 5% payout for nonfunctionally integrated supporting organizations. However, in breaking with normal practice, the regulations provided no effective date – they were issued as Advanced Notice of Proposed Rulemaking. This is unacceptable. I ask that you or Treasury/IRS provide me assurance that Treasury/IRS will implement the guidance promptly and make the 5% payout effective within 30 days of your receipt of this question. I will have additional views and concerns regarding this proposed rule, separate from the 5% requirement, that I will address in a separate question.

It is important to immediately designate an effective date for the 5% payout, and there should be no transition relief. There is no reason that the payout rules cannot take place immediately. These supporting organizations have been on notice for a significant period of time that there were going to be changes in current operations. Charities have waited too long to finally get the funds that were donated to these supporting organizations. In addition, I ask that you provide me a written update every 6 months, beginning July 1, 2008, of the efforts IRS and Treasury are undertaking to address other identified abusive problems in supporting organizations and donor advised funds. Finally, I ask for your written response to the additional views I have regarding these regulations that I will send separately.

Answer

The Pension Protection Act (PPA) made significant changes to the statutory provisions addressing supporting organizations, particularly those designated as so-called Type III organizations. The PPA directed the IRS and Treasury Department to establish a new payout requirement for certain of these organizations, and a new definition of a “functionally integrated” Type III supporting organization to be used to determine which organizations would be subject to the new payout requirement.

Because of the significant effect of the statutory change in this area, the IRS and Treasury Department determined it was important to provide the sector ample notice and the opportunity to comment on this new requirement. Therefore, an advance notice of proposed rulemaking, or ANPRM, was issued on August 2, 2007. As a result of the issuance of the ANPRM, the IRS has received valuable comments regarding the guidance. These comments are currently being reviewed as part of the development of proposed regulations on this issue.

Issuance of proposed regulations in this area is on the IRS's 2007-2008 guidance plan, and the IRS and Treasury Department have been working to complete proposed regulations regarding the issues addressed by the ANPRM. We expect to release this guidance before the summer. The effective date of the

guidance will be based upon a careful and deliberate consideration of many factors, including perceived abuse, fairness to the affected sector and organizations, timely implementation of the new provisions enacted by Congress, and our understanding of Congressional intent.

We are committed to addressing problems in the donor advised fund and supporting organization areas.

Question 34

The IRS is to be commended for its efforts in revising the Form 990 for tax-exempt organizations. This is a vital document that provides transparency and openness to the public, the press and the Congress.

- a. There cannot be a delay in making this form and its schedules effective. I want your assurance that there will be no changes in the effective dates for the Form 990 and, particularly, for the Schedule H for hospitals.**
- b. One of the most important tables on Schedule H is Part III dealing with community benefit. The IRS made the right decision in Part III by not describing bad debt and Medicare shortfalls as elements of "community benefit." Bad debt and Medicare shortfalls are inappropriate on several policy grounds, and including them allows nonprofit hospitals to provide a misleading picture of their work to policymakers, the public and the press. I want your commitment that there will be no changes to that table.**
- c. Regarding the Form 990, Senator Baucus and I raised the idea, in writing, to the IRS that there should be a separate schedule for nonprofit hospitals and also one for colleges and universities. I am pleased that the IRS has created a separate schedule for nonprofit hospitals, but I am disappointed that there was not one created for colleges and universities. The recent public debate about colleges and universities and their tuition, endowments and president's salaries have all highlighted that there is much need for additional information in this area. I would ask that you contact the Department of Education, the members of the Spellings Commission, and other interested parties representing parents and students to review the benefits of having a separate schedule and what information should be included on a separate schedule. In addition, I believe that such a schedule should provide significantly more information about endowments – including details of how the funds are being used, investment advisory fees and other relevant information. The recent letter sent by the Finance Committee to colleges and universities on**

January 24, 2008, may be useful to review in this light. I ask for your commitment to undertake such a review now, and I ask you to provide a detailed written response by September 8, 2008.

- d. The House Oversight Committee has recently held hearings on charities that are ostensibly created to benefit veterans. Unfortunately, too often, the real beneficiaries are the managers of the charities and their contractors. Chairman Waxman and Congressman Davis should be commended for holding these hearings. One statement from a witness who manages a veterans charity that was a subject of the hearing is of particular interest: "If we disclose, which I'm more than happy to do, we'd all be out of business. Nobody would donate. It would dry up." This statement, reported in the *Washington Post*, was in response to a question from Congressman Shays asking what would happen if his charities told donors how their donations were spent.

This witness's statement highlights why I am very frustrated that one of the few poor decisions the IRS made in regards to the new Form 990 was eliminating from the summary page the percentage of raised funds used for the charitable purpose. I recognize that a few charities complained, but the IRS should be putting the taxpayer first and, most importantly, the intended beneficiaries of the charity. This information is of great interest to the donating public. To say that the information is buried elsewhere in the Form 990 and schedules isn't satisfactory. I want your commitment now that the IRS will make as a top priority ensuring that on the summary page there will be easy-to-understand information about the percentage of dollars raised (not including transfers from other charities) that go to the actual charity purpose (with a tight common sense definition of what counts as charity purpose). I ask for an update on this matter every six months starting July 1, 2008. In addition, I ask that you provide by July 1, 2008, a complete written review of the issues raised by the hearings in the House on veterans charities including detailed discussion of all efforts you have taken within the authority of the Treasury and IRS to address these abuses through guidance, regulations, notices, enforcement and other actions. In addition, I ask that you also provide at that time any legislative reforms that you believe Congress should enact in response to these abuses. This review should consider not only veterans charities, but also "badge charities"—those involving fire and police officers – which have been the subjects of continual reports of abuse.

The House Oversight Committee's hearings on veterans' organizations, many of which are classified as tax-exempt

organizations described in section 501(c)(19) of the Code, revealed instances of exorbitant compensation received by managers of these organizations. Currently, the excess benefits provision of section 4958 could not be imposed on these managers since section 4958 deals only with organizations described in sections 501(c)(3) and (4). What are your views on making provisions of section 4958 applicable to organizations described in other subparagraphs of section 501(c)? How else do you propose to deal with exorbitant compensation involving 501(c)(19)s?

Answer

The 2008 Form 990 will enhance transparency in the tax-exempt sector and will provide the IRS with additional and improved compliance information. We are committed to the implementation dates announced last December with respect to the entire Form, including the Schedule H. As to the particular information requested on the Schedule H, we believe the required reporting of bad debt and Medicare shortfalls appropriately addresses the extensive comments we received.

On your inquiry regarding colleges and universities, we note that a separate schedule was considered as part of the 2008 Form 990. It was not included because we determined that a decision should wait until we are further along in our colleges and universities project. This will enable us to gain a better understanding of these complex systems. We will have an improved understanding of this area by the fall and will assess the need for a separate schedule at that time.

During the IRS Form 990 redesign process the IRS explored how to facilitate the disclosure of how much of every donor's dollar is actually used for charity. This included reporting some fundraising measures on the form's summary page, such as the percentage of funds raised that was retained by the charity and the percentage that was paid to the fundraiser. This attempt was universally criticized, even by watchdog organizations, as placing undue importance on the proposed measures, and impeding transparency because the proposed measures did not provide meaningful and complete information regarding the use of raised funds. As a result of these comments, we eliminated these summary measures from the redesigned Form 990 summary page. Nonetheless, we will continue to explore whether meaningful reporting can be achieved in this area, and maintain as a priority improvements to accurate and complete reporting on the Form 990, including ways to improve transparency regarding the use of charitable donations for charitable purposes.

On veterans' organizations, the IRS is always concerned where any tax-exempt organization appears to be spending funds for the wrong purposes, including the

payment of unreasonable salaries. As to what tools we have in the area of excessive compensation with respect to veterans' organizations, while they are subject to a prohibition against private inurement, it is true that section 4958 (the intermediate sanction on excess compensation) does not apply. This is also true in some other areas in which the possibility of excessive compensation may occur. Whether the scope of section 4958 should be expanded to some or all of these areas is a matter of tax policy and one that is ultimately for Congress to decide. From the perspective of tax administration, the IRS is prepared to work with the Treasury Department and the Committee staff as any proposals are formulated.

Question 35

The Pension Protection Act required a report from Treasury/IRS regarding donor advised funds and supporting organizations. As discussed above, Congress took some steps to deal with the abuses that were highlighted by the IRS in the Pension Protection Act, but I am concerned that there is still much to be done. This report is months late. Please have the Treasury/IRS provide a copy of the report. This report will be incomplete if it does not include detailed findings, observations and conclusions along with recommendations for regulatory and guidance changes and any need for legislation. I have long been concerned that Treasury/IRS believes the report meets Congressional intent if it provides a summary of statements from interested parties – nothing could be further from the truth. I expect hard analysis and review of these areas that the IRS has consistently held up as long-time sources of abuse. We need to come to real solutions.

Answer

Section 1226 of the Pension Protection Act (PPA) directed that the Treasury Department and IRS undertake a study on the organization and operation of donor advised funds and supporting organizations. The study will consider a number of issues, including whether deductions of charitable contributions to sponsoring organizations are appropriate, whether donor advised funds should have a required pay-out, whether retention by donors of rights or privileges is consistent with treatment of their donations as completed gifts, and whether the foregoing issues may be relevant to other forms of charities. Last year, the Treasury Department and IRS issued Internal Revenue Bulletin Notice 2007-21, which solicited public comment on the issues identified for consideration in the study. Numerous comments have been received in response to the notice, and the Treasury Department and IRS are working to complete drafting of the study, taking those comments into account. Our current goal is to have the study published by this summer.

In addition to the study, the IRS is taking other steps to gather more information about donor advised funds and supporting organizations pursuant to the PPA.

Prior to the PPA, the law provided for very limited data collection by the IRS regarding donor advised funds and supporting organizations. The PPA made significant changes to the statutory provisions governing donor advised funds and supporting organizations, including codifying a definition of donor advised fund and providing exceptions to that definition. After the enactment of the PPA, it became necessary to insert new line items on Form 990 (Return of Organization Exempt from Income Tax) to capture data regarding particular aspects of donor advised funds and supporting organizations. Consequently, these data now will be collected by the IRS and will be helpful in determining what additional steps, if any, should be taken in this area.

Question 38

The study on nonprofit hospitals is expected to be completed by September 2008. I want your assurance that you will make a priority of having this report completed by that time period. I also want your assurance that the report will include an assessment of the community benefit standard and recommendations (and timetable for implementation) for Treasury and IRS to implement all necessary guidance and regulations to ensure that nonprofit hospitals are providing real and valued benefits to those in need in their community. The interim report showed many problems with nonprofit hospitals and showed that there was significant variation in reporting of community benefits – with some reporting no community benefits. This demonstrates the need for clear rules and guidance in this area. In general, please provide me your views of whether the current situation regarding nonprofit hospitals – in which hospitals receive significant tax breaks and are not required by Treasury/IRS to provide any charity care or real measurable community benefit – is acceptable. Please explain your views on whether you believe it is appropriate, and in keeping with a nonprofit hospital's charitable status, that a nonprofit hospital would charge an uninsured, low-income individual a rate three or four times (and often much greater) higher than an insured individual would be charged for the same service. Please provide any additional comments or observations that you have regarding this issue.

The fundamental change in the treatment of nonprofit hospitals, including the end of requirements for charity care, came with Rev. Rul. 69-545 (there was no change in statute). It has been said that the community benefit provisions of Rev. Rul. 69-545 were developed from a vast study of hospitals' tax exemptions. The study, authored by Robert S. Bromberg and published on December 20, 1968, is titled TS 65-30, "A Treatise on the Voluntary Hospital as a Charitable Institution," and it is my understanding that TS 65-30 contains no taxpayer information. Please submit a copy of TS 65-30 as well as the file on Rev. Rul. 69-545.

Answer

The IRS is working toward completion of the hospital report by September 2008 and is on schedule to do so. This project was designed to aid the IRS in gathering objective information on the extent of tax-exempt hospitals' community benefit activities. The interim report included several recommendations with respect to community benefit reporting and was instrumental in development of the new Schedule H as part of the redesigned Form 990 package released in December 2007. The new Schedule H will enable the IRS to have a better picture of the tax-exempt hospital sector's activities, and a more comparable and reliable data set with respect to the entire non-profit hospital sector.

The final report will include information intended to advance our understanding and the debate on application of community benefit standards to hospitals. As stated in the interim report, we will address community benefit practices across various demographics of our surveyed population. We expect to gain sufficient information from the final report and Schedule H filings to provide the basis for assessing the continued relevance of the current standards. The information in the final report and Schedule H filings should shed light on a number of issues, including non-profit hospital charges for individuals in various categories.

Prior to 1969, the IRS took the position that a hospital qualified as a charitable organization if the hospital accepted patients without regard for their ability to pay, to the extent of the hospital's financial ability. Rev. Rul. 56-185, 1956-1 C.B. 202. This "financial ability" standard was criticized in 1969 at Congressional hearings for its imprecise standards concerning the extent to which a tax-exempt hospital must accept patients who are unable to pay. See House Rep. No. 91-413, 91st Cong., 1st Sess. Pt. 1 (1969), at 43. Congressional consideration of the issue led to inclusion in H.R. 13270, 91st Cong., 1st Sess. (1969), of a provision amending section 501(c)(3) to clarify the tax-exempt status of hospitals. Specifically, the bill passed by the House of Representatives in August 1969 treated as charities those organizations that were organized and operated exclusively "for the providing of hospital care." This provision was not enacted into law. According to a later Senate Report, the provision was dropped after the IRS issued Rev. Rul. 69-545, 1969-2 C.B. 117, in October 1969, which included the "community benefit" test. See S. Rep. 91-552, 91st Cong., 1st Sess. (1969) at 61.

Since publication of Rev. Rul. 69-545, the IRS has applied the community benefit test, considering a number of factors to determine whether a hospital operates for the benefit of the community. Over the past few decades, the courts have recognized Rev. Rul. 69-545 as such. See, e.g., *IHC Health Plans, Inc. v. Commissioner*, 325 F.3d 1188 (10th Cir. 2003). As the 1969 revenue ruling was being developed, an internal IRS technical study was written that broadly considered issues relating to the tax-exempt status of hospitals. A copy of the technical study will be provided as requested in connection with this response.

The study has been redacted to eliminate references to return information protected from disclosure under section 6103. An unredacted version can be provided if authorized in accordance with section 6103(f). After conducting an extensive search of Treasury Department, IRS, and National Archives records, in December 2006, documents responsive to your prior request for files relating to Rev. Rul. 69-545 were provided to your office. Aside from the technical study discussed above, no other documents relating to Rev. Rul. 69-545 have been located.

Question 39

As discussed above, the interim report by the IRS on nonprofit hospitals found that there were several hospitals that provided little to no community benefit. Thus, I am stunned to find that hospitals are not included in the current audit plan for exempt organizations. I want your assurance (or the assurance of Treasury/IRS) that within thirty days of receipt of this question, there will be an inclusion of an audit plan for hospitals with a particular emphasis on those hospitals that have already admitted to providing little to no community benefit. I ask that you provide a written update on these examination efforts, findings and resolutions every six months beginning July 1, 2008.

Answer

Hospitals are a key part of the IRS' overall audit plan. As part of its work on the non-profit hospital study, the IRS reviewed the narrative responses of hospitals in the project that reported no dollar amounts in fields related to community benefit expenditures. In those cases, either the hospital was referred for examination or it was discovered that there were reasonable explanations for not including amounts on the questionnaire. In the latter cases, most of the organizations had either just begun operation, ceased doing business, or had merged into a larger entity and thus were no longer reported expenditures individually.

In addition to this continued examination activity, the IRS has other work in the non-profit hospital area. Twenty hospitals in the study were selected for examination of their compensation practices. That work continues. As appropriate, we will open other non-profit hospital cases raising compliance concerns. We will be happy to provide an update in July and periodically thereafter as you requested.

Question 40

The IRS issued a report on executive compensation that identified several instances of excessive compensation in private foundations and public charities. Please provide (or have the IRS provide) an update for each of these cases, including the status and a description of the general facts in

each case. Additionally, please provide a written update of all audits involving excessive compensation every six months beginning July 1, 2008.

In public statements, IRS officials have stated that there were instances in which they found executive compensation that they believed would be viewed as excessive by the public (or even themselves), but was still reasonable under Treasury/IRS regulations and guidance. Please provide all examples of these findings that were identified by the IRS in relation to this report. Please detail how the IRS decided what was reasonable and what was not. Newspapers have been filled with accounts of salaries that have sparked public outrage, yet the IRS stated it didn't find widespread abuse. Why is this? Was the IRS looking at the right organizations, or does the IRS/Treasury have an inappropriate standard? Are IRS employees not using common sense, or does the statute need to be modified?

Answer

As noted in the non-profit executive compensation report, the IRS proposed Chapter 42 excise tax assessments of over \$21 million against 40 disqualified persons. Absent a request under section 6103(f)(1), section 6103 precludes a discussion of the individual cases in this area. We are available to meet with you or your staff to discuss the report in more detail, if desired.

With regard to the cases involved in the executive compensation initiative, when an examiner looked at the compensation in a particular case, the examiner looked at the bottom line figure along with the process that was used in developing it, and reached a conclusion. Valuation engineers were made available to our agents if the compensation appeared questionable. Of the cases included in the initiative, it did not appear, on the whole, that the organizations paid unreasonable compensation. Moreover, as we described in the initiative report, although the executive compensation study touched a large number of taxpayers, it was not a statistical sample representative of the entire population. The fact that we did not find widespread abuse cannot by itself be said to be indicative of the whole sector, and we committed to working compensation components into our future projects in order to test compliance levels further. We are doing this as part of our hospital and college and university projects.

Your question highlights an important issue under current law. The legal standard does not necessarily comport with the public's perception of what is reasonable. While the public may find a given salary excessive or even shocking, the legal standard is quite clear: Is the compensation reasonable when compared to compensation paid to other similarly situated individuals for similar services? This may permit compensation in the sector that is higher than the public's expectation.

Question 42

I wrote to the Secretary of Treasury last year regarding problems of abuse in land conservation easement donation and asked for proposals to address the continuing problems in this area. This has been a matter of extensive oversight by the Finance Committee. The answer I received from an assistant to the Secretary on October 25, 2007, was not responsive to my questions. I now ask that the IRS provide me a detailed, full and complete response to the questions I asked regarding the problems that are being seen in this area and solutions that the IRS and Treasury are proposing through guidance, regulations and any statutory changes that may be necessary. In addition, I ask for your personal assurance that there will be no reduction in the enforcement presence and activity of the IRS in the area of donation of easements for conservation and other purposes. I request an update on this matter by July 1, 2008.

Answer

There has been significant growth in the number of donations of conservation easements in recent years, in substantial part because of incentives offered by federal, state, and local governments to promote land conservation and historic preservation through tax deductions and credits. The IRS has had a robust examination program in place for the past few years in this area, and continues to observe problems with charitable deductions relating to land and façade easements. Most of these issues involve valuation discrepancies, including, for example, the improper use of the subdivision analysis method of valuation in certain cases.

Other issues exist as well. These include questionable donative intent, conservation purpose, and the inappropriate retention of development rights by donors in some instances.

These donor cases are fact intensive and require considerable resources and time, both for the IRS and the taxpayer, whether the cases involve abuse or simply are the result of genuine difficulties in determining the value of these property interests. We continue to develop these cases and litigate those involving substantial questions of valuation or other requirements such as conservation purpose.

To improve our ability to regulate the area, the 2008 Form 990, Schedule D includes expanded reporting by donee organizations receiving easements. The IRS also has examinations underway involving the inability of certain recipient organizations to monitor and enforce the restrictions of the donated easements. In this regard, we are currently designing a project to evaluate a cross section of conservation easement organizations.

You have asked about legislation and guidance. Recent legislative changes imposing appraiser penalties, including the technical corrections clarifying that these penalties apply to estate and gift tax charitable deductions, should be helpful and address overvaluation of contributed easements by certain appraisers. In addition, we believe that the recent legislative changes in the façade easement area resulting from the Committee's work will address some of the problems in that area.

In terms of guidance, we continue to work on implementing recent legislation. We also will continue to work with land trusts and historic preservation organizations to determine whether the IRS and the Treasury Department can provide additional guidance. We are available to meet with you or your staff to discuss any other concerns in this area.

Question 44

The Private Debt Collection Program was passed by Congress in response to a request from the administration. This program is designed to allow the IRS to collect revenues that would otherwise not be subject to collection action and also to allow the IRS to better allocate its own collection resources. Reports have shown that the private debt collectors have done an outstanding job in all respects and especially in regards to taxpayer rights – an area in which they have outscored IRS employees.

As mentioned earlier, one of the IRS findings has been that private debt collectors have done a better job at times than IRS employees in terms of taxpayer rights. In addition, the private debt collectors are vigorous in disciplining and firing employees who act in an inappropriate manner to taxpayers. Congress enacted section 1203 in the IRS Restructuring Act to ensure that IRS employees who acted improperly would be subject to discipline. The IRS Commissioner has authority to modify the sanctions imposed. I have reviewed the Commissioner's Semi-Annual Report on Disciplinary Actions for 7/01/2006 - 12/31/2006, and I am troubled to find many instances of IRS employees who would be subject to the full sanctions of 1203 or other statutes or regulations being let off with a slap on the wrist. I am troubled that it appears the private sector is at times treating employees who act improperly towards a taxpayer with greater discipline than the IRS is treating its employees. Please inform me of your personal views on how you will use your authority to mitigate disciplinary penalties under section 1203 and elsewhere. I ask that you pledge to use such authority rarely. In addition, I am frustrated that the Commissioner's report often lists no mitigating factor, which raises questions of the extent to which Congressional intent is being followed. I ask for your pledge to ensure that this report is complete. Please provide my office an electronic copy of the most recent copy of the Commissioner's Semi-Annual Report on Disciplinary Actions.

Answer

Electronic versions of the Commissioner's Semi-Annual Report on Disciplinary Actions for the periods January 1, 2007 to June 30, 2007 and for the period July 1, 2007 to December 31, 2007 are being transmitted to your office.

Question 53

One of the benefits of whistleblowers assisting the IRS is the ongoing dialogue and give-and-take between the whistleblower and the IRS. I am very worried that the IRS may be chilling those discussions by imposing on whistleblowers a "one-shot" rule – i.e., that there can be only one meeting with the whistleblower and the IRS, particularly when the whistleblower is a present employee. As I understand it, the concern is that if there are meetings after the initial meeting the whistleblower could be viewed as an agent of the IRS. This is an issue that the Department of Justice, in administering the False Claims Act, has successfully navigated. I ask for your pledge to consult with the Department of Justice as well as the qui tam bar regarding this matter, and to issue guidance by July 1, 2008, that will give common sense clarity to this issue and provide direction as to when multiple meetings between a whistleblower and the IRS can take place.

Answer

The Whistleblower Office, working with the Operating Divisions, Criminal Investigations and Chief Counsel, has established a process to review submissions to address the "whistleblower as agent" concern noted in your question. The IRS has also informally discussed the topic with the Department of Justice. The "whistleblower as agent" case-building process will be included in new, comprehensive Whistleblower Office guidance for IRS personnel.

Question 54

I frequently hear from whistleblowers expressing concern that their submissions are not being sent to the field to be worked in a timely manner. I believe this could very well be a resource problem at the Whistleblower Office, but given the statute of limitations, it is important that this is corrected quickly. Speed in providing information to the field will also, of course, assist the examiners in their important work. Please give me your pledge that you will review this matter and report to me on progress by July 1, 2008.

Answer

The IRS recognizes the need to get all potentially useful information into the hands of the appropriate IRS personnel at the earliest opportunity. There are, however, instances in which the Whistleblower Office first must review the cases to resolve potential legal issues, such as privilege issues, that could affect the ability of the IRS to use the information submitted. Premature release of the cases to the Operating Divisions could compromise the integrity of ongoing examinations. The Whistleblower Office has sufficient resources to process the limited number of cases that require additional review, and we have established procedures to ensure expeditious review by the Operating Divisions, Criminal Investigations, and the Office of Chief Counsel.

Question 55

I am worried that in regards to 10% discretionary rewards, the guidance suggests that if a broad tax issue is identified on a company Audit Plan the whistleblower would not have an opportunity for a reward. This raises very real concerns for me that overly broad audit plans will be used as a justification to foreclose a reward. There is no doubt that a whistleblower can come forward with critical, valuable information (regarding information within an audit plan) that sheds detailed light on a taxpayer's actions and saves the IRS significant time and resources. I think there is a strong argument that such a whistleblower should be entitled to at least the 10% reward. I ask that you pledge now to review this matter closely and ensure that whistleblowers who provide important information will still be provided a reward. Also, I request a full, written response describing the actions you have taken in this regard by July 1, 2008.

Answer

The IRS recently issued Notice 2008-4, which describes factors the IRS will consider in determining whether a whistleblower may be eligible for an award. Each case will be examined based on the facts presented, to ensure that each reward decision complies with the guidance in the notice.

Question 56

I am concerned that whistleblowers may not be receiving their rewards in a timely manner. I am worried that whistleblower rewards are being delayed because the IRS may be taking the view that it must receive payment from all taxpayers prior to paying any share to the whistleblower. There seems to be no justification for this action. I request your commitment now to review this matter and any other issues that are delaying reward payments to whistleblowers. In addition, please provide a full, written response describing the actions you have taken in this regard by July 1, 2008.

Answer

The law requires that award payments be made from collected proceeds, and not from appropriated funds. The IRS pays rewards to whistleblowers as soon as proceeds are collected. If there are multiple taxpayers involved, the IRS does not withhold payment pending collection from all the taxpayers.

Commissioner's Semi-Annual Disciplinary Actions Report
January 1 to June 30, 2007

Why is this report being issued?

This disciplinary action report was prepared to fulfill the promise former Commissioner Rossotti made in August 1999, to provide IRS employees with summaries of employee disciplinary actions; and to further the IRS's policy of open communication on matters of interest to IRS employees and the public. We have taken appropriate precautions to protect employees' privacy when preparing these reports.

What is actually in this report?

The report is presented in chart form, with one row for each completed disciplinary action closed in the Automated Labor and Employee Relations Tracking System (ALERTS), for the period January 1, 2007 through June 30, 2007.

Although most of these disciplinary actions occurred between January 1, 2007 and June 30, 2007, some actually occurred outside of that time period. These cases are included here because they were closed in ALERTS during this time period and were not captured in previous reports.

Where five or fewer employees held the same series, grade and job title at the same location, information was modified to avoid identifying the employee involved.

The description of the offense is taken from the IRS Guide for Penalty determinations ("Penalty Guide"), unless more specific information from the discipline document could be provided without identifying the employee.

This report addresses disciplinary actions entered into the ALERTS system during the 1st half of calendar year 2007, and may include misconduct that occurred in a prior year. A column headed "temporal range of misconduct" identifies when the misconduct occurred within a four year range. Thus, misconduct that occurred in 1999 is reported as "1997 to 2000." Use of a range, rather than citing the specific year, is one of the steps taken to help avoid identification of the employee involved and to preserve confidentiality of tax return information when discipline was based on a tax compliance problem.

Other columns describe any mitigating factors and any prior discipline cited in the discipline document. For the most serious disciplinary actions, the personnel process requires a proposed action and an opportunity to reply before the discipline decision is made. When those procedures were applied, both the proposed and actual disciplinary action are included in the report.

What actions were taken most often?

The report summarizes formal disciplinary actions involving IRS employees, including counseling confirmed in writing ("written counseling"), reprimand, suspension, removal and involuntary change to lower grade ("downgrade"). Informal actions, such as oral counseling, are not included. Actions involving employees from Chief Counsel are reported separately.

This report summarizes 2,366 disciplinary actions. Table 1 below shows the number of actions taken for all types of offenses, as well as the actions taken based on the Employee Tax Compliance Program (see Table 1, footnote 1).

Figure A: Table 1 is a three column table. Column 1 lists the various disciplinary actions taken. Column 2 lists the number of all offenses that occurred between January 2007 and June 2007. Column 3 lists only those offenses involving Employee Tax Compliance.

Written Counseling	505 offenses	201 Employee Tax Compliance
Admonishment	681 offenses	384 Employee Tax Compliance
Reprimand	541 offenses	156 Employee Tax Compliance
Reduction in Grade	2 offenses	0 Employee Tax Compliance
Suspension	444 offenses	89 Employee Tax Compliance
Removal	193 offenses	23 Employee Tax Compliance
TOTAL	2,366 offenses	853 Employee Tax Compliance

Table 1, Footnote 1: The Employee Tax Compliance (E T C) Program identifies employees who may have failed to meet their obligations as taxpayers. E T C Program staff first attempt to resolve issues through direct correspondence with employees. Unresolved issues are referred to management to determine whether disciplinary action may be warranted.

Table 1, Footnote 2: IRS automated records on disciplinary actions include "issue codes" to identify the nature of the misconduct. In many cases, disciplinary actions cite more than one "issue code" because the disciplinary action may be based on more than one offense. The numbers reflected on this table are the numbers of times each "issue code" was cited. These numbers do not correspond to the number of disciplinary actions taken.

What were the most frequent offenses resulting in discipline?

Tax compliance issues factored into more cases, by far, than any other. Table 2 represents the ten issues appearing most frequently in this report.

Figure B: Table 2 is a two column table. Column 1 lists 10 issue descriptions. Column 2 lists the number of offenses related to each issue description.

Tax Delinquency, Not §1203 (see Table 2, Footnote 1)	651 offenses
Absence and Leave	332 offenses
Government Travel Card Delinquency	311 offenses
Taxes: Under Reporter- Not §1203 (see Table 2, Footnote 2)	207 offenses
Failure to Follow Instructions	122 offenses
Unauthorized Access-Return or Return Information	112 offenses
Attempted Unauthorized Access	108 offenses
Unprofessional Conduct	100 offenses
Taxes-Not paid or Late pay	75 offenses
Barred Statutes	67 offenses

Table 2, Footnote 1: Employee identified, usually through the E T C Program, that had not filed, timely filed, or timely paid his or her personal income taxes, and the circumstances *do not* meet the definition of a §1203 offense.

Table 2, Footnote 2: Employee identified, usually through the E T C Program, who have not reported all income on his or her personal tax return for a particular year, and the circumstances do not meet the definition of a §1203 offense.

What offenses resulted in removals?

Some of the removals were based on more than one offense. Attendance related offenses, such as absence without leave, accounted for 66 of the removals. Tax compliance issues were a factor in 32 removals; and unauthorized access (UNAX), or attempted unauthorized access to taxpayer records was a factor in 61 removals.

What was the distribution of disciplinary actions by grade?

Table 3 lists the number of disciplinary actions taken against employees at each grade level. The number of employees at each grade level reflects full-time, part time and seasonal employees on the IRS payroll as of June 30, 2007.

Figure C: Table 3 is a three column table. Column 1 lists each grade level. Column 2 lists the number of employees occupying each grade level. Column 3 lists the number of disciplinary actions taken against employees occupying each grade level.

GS 1	138 employees	0 actions
GS 2	1,521 employees	2 actions
GS 3	3,351 employees	80 actions
GS 4	7,991 employees	296 actions
GS 5	8,607 employees	273 actions
GS 6	5,013 employees	142 actions
GS 7	12,174 employees	369 actions
GS 8	9,697 employees	401 actions
GS 9	7,322 employees	177 actions
GS 10	119 employees	2 actions
GS 11	7,006 employees	146 actions
GS 12	8,222 employees	118 actions
GS 13	13,388 employees	171 actions
GS and GM 14	4,817 employees	40 actions
GS and GM 15	1,077 employees	2 actions
IR Pay Band	8,579 employees	147 actions
TOTAL	99,022 employees	2,366 actions

Table 3 Note: Total number of IRS employees = count of records in a Treasury Integrated Management Information System file where Current Employment Status = 0 (active) and Separation accession Type = 0 (Not Separated). Pay-banded employees (pay plan IR) have all been counted as IR.

To view the entire report, go to <http://finance.senate.gov/press/Gpress/2008/prg041508e.pdf>.

**Commissioner's Semi-Annual Disciplinary Actions Report
July 1 - December 31, 2007**

Why is this report being issued?

This disciplinary action report was prepared to fulfill the promise former Commissioner Rossotti made in August 1999, to provide IRS employees with summaries of employee disciplinary actions; and to further the IRS's policy of open communication on matters of interest to IRS employees and the public. We have taken appropriate precautions to protect employees' privacy when preparing these reports.

What is actually in this report?

The report is presented in chart form, with one row for each completed disciplinary action closed in the Automated Labor and Employee Relations System (ALERTS), for the period July 1, 2007 through December 31, 2007.

Although most of these disciplinary actions occurred between July 1, 2007, and December 31, 2007, some actually occurred outside of that time period. These cases are included here because they were closed in ALERTS during this time period and were not captured in previous reports.

Where five or fewer employees held the same series, grade and job title at the same location, information was modified to avoid identifying the employee involved.

The description of the offense is taken from the IRS Guide for Penalty determinations ("Penalty Guide"), unless more specific information from the discipline document could be provided without identifying the employee. This report addresses disciplinary actions entered into the ALERTS system during the 2nd half of calendar year 2007, and may include misconduct that occurred in a prior year. A column headed "temporal range of misconduct" identifies when the misconduct occurred within a four year range. Thus, misconduct that occurred in 1999 is reported as "1997-2000." Use of a range, rather than citing the specific year, is one of the steps taken to help avoid identification of the employee involved and to preserve confidentiality of tax return information when discipline was based on a tax compliance problem. Other columns describe any mitigating factors and any prior discipline cited in the discipline document. For the most serious disciplinary actions, the personnel process requires a proposed action and an opportunity to reply before the discipline decision is made. When those procedures applied, both the proposed and actual discipline were reported.

What actions were taken most often?

The report summarizes formal disciplinary actions involving IRS employees, including counseling confirmed in writing ("written counseling"), reprimand, suspension, removal and involuntary change to lower grade ("downgrade"). Informal actions, such as oral counseling, are not included. Actions involving employees from Chief Counsel are reported separately.

This report summarizes 2,185 disciplinary actions. Table 1 below shows the number of actions taken for all types of offenses, as well as the actions taken based on the Employee Tax Compliance Program¹.

Table 1

	All Offenses	Employee Tax Compliance
Written Counseling	464	220
Admonishment	615	319
Reprimand	456	134
Reduction in Grade	4	0
Suspension	488	96
Removal	158	10
TOTAL	2,185	779

[1] The Employee Tax Compliance (ETC) Program identifies employees who may have failed to meet their obligations as taxpayers. ETC Program staff first attempt to resolve issues through direct correspondence with employees. Unresolved issues are referred to management to determine whether disciplinary action may be warranted.

[2] IRS automated records on disciplinary actions include "issue codes" to identify the nature of the misconduct. In many cases, disciplinary actions cite more than one "issue code" because the disciplinary action may be based on more than one offense. The numbers reflected on this table are the numbers of times each "issue code" was cited. These numbers do not correspond to the number of disciplinary actions.

What were the most frequent offenses resulting in discipline?

Tax compliance issues factored into more cases, by far, than any other. Table II lists the ten issues appearing most frequently in this report.

Table II

Tax Delinquency, Not §1203 ¹	493
Absence and Leave	372
Taxes Not paid or Late pay	220
Government Travel Card Delinquency	209
Taxes: Under Reporter- Not §1203 ²	156
Failure to Follow Instructions	138
Unauthorized Access-Return or Return Information	115
Unprofessional Conduct	102
Attempted Unauthorized Access	83
Falsification Other than Official Documents	53

¹ Employee identified, usually through the ETC Program, that had not filed, timely filed, or timely paid his/her personal income taxes, and the circumstances *do not* meet the definition of a §1203 offense.

² Employee identified, usually through the ETC Program, that has not reported all income on his/her personal tax return for a particular year, and circumstances do not meet the definition of a §1203 offense.

What offenses resulted in removals?

Some of the removals were based on more than one offense. Attendance related offenses, such as absence without leave, accounted for 76 of the removals. Tax compliance issues were a factor in 17 removals; and unauthorized access (UNAX), or attempted unauthorized access to taxpayer records was a factor in 45 removals.

What was the distribution of disciplinary actions by grade?

Table III lists the number of disciplinary actions taken against employees at each grade level. The number of employees at each grade level reflects full-time, part time and seasonal employees on the IRS payroll as of December 31, 2007.

Table III

Grade	Number of Employees	Disciplinary actions
1	89	0
2	1,045	2
3	2,154	80
4	6,212	296
5	8,291	273
6	5,267	142
7	11,883	369
8	9,418	401
9	7,477	177
10	111	2
11	6,869	146
12	8,096	118
13	13,287	171
14	4,967	40
15	1,128	2
IR	8,402	147
TOTAL	94,696	2,185

**Note: Total number of IRS employees= count of TIMIS file where Current employment status = 0 (active) and Separation accession Type = 0 (Not Separation)
Paybanded employees (payplan IR) have all been counted as IR.**

To view the entire report, go to <http://finance.senate.gov/press/Gpress/2008/prg041508g.pdf>.

