

**INTERNAL REVENUE SERVICE OPERATIONS  
AND THE PRESIDENT'S BUDGET  
FOR FISCAL YEAR 2016**

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**HEARING**

BEFORE THE

**COMMITTEE ON FINANCE  
UNITED STATES SENATE**

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

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FEBRUARY 3, 2015

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**INTERNAL REVENUE SERVICE OPERATIONS  
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FOR FISCAL YEAR 2016**

TUESDAY, FEBRUARY 3, 2015

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

The hearing was convened, pursuant to notice, at 10:33 a.m., in room SD-215, Dirksen Senate Office Building, Hon. Orrin G. Hatch (chairman of the committee) presiding.

Present: Senators Grassley, Crapo, Roberts, Cornyn, Thune, Burr, Portman, Coats, Heller, Scott, Wyden, Stabenow, Nelson, Menendez, Carper, Cardin, Brown, Bennet, and Casey.

Also present: Republican Staff: Chris Armstrong, Deputy Chief Oversight Counsel; Kimberly Brandt, Chief Healthcare Investigative Counsel; Chris Campbell, Staff Director; Jim Lyons, Tax Counsel; and Harrison Moore, Professional Staff Member. Democratic Staff: David Berick, Chief Investigator; Adam Carasso, Senior Tax and Economic Advisor; Michael Evans, General Counsel; Christopher Law, Investigator; Todd Metcalf, Chief Tax Counsel; Joshua Sheinkman, Staff Director; and Tiffany Smith, Senior Tax Counsel.

**OPENING STATEMENT OF HON. ORRIN G. HATCH, A U.S.  
SENATOR FROM UTAH, CHAIRMAN, COMMITTEE ON FINANCE**

The CHAIRMAN. The committee will come to order.

The committee welcomes Internal Revenue Service Commissioner John Koskinen, who comes before us today to discuss his agency's budget and operations. We also will be discussing President Obama's fiscal year 2016 budget proposal.

Commissioner Koskinen, this morning's hearing continues a long tradition of the close relationship between the Senate Finance Committee and your agency. More than 152 years ago, the Finance Committee received a letter from George Boutwell, whom President Lincoln had appointed as the first Commissioner of Internal Revenue. The letter came in response to an inquiry from the committee seeking information about the Commissioner's organization, his budget, and the activities of his office.

Does that sound familiar?

In his letter dated January 21, 1863, Commissioner Boutwell tried to answer the committee's questions, but started by first asking Congress for more money. Specifically, he wrote, "Before proceeding to estimate the expenses of assessing and collecting the

revenue, I desire to express the opinion that an increase in the pay of assessors is very important, if not absolutely necessary.”

Now, that part does sound familiar to me. As you and I continue this historic and important relationship, I hope we can begin the 114th Congress on a new footing.

The issues before us are too great for that relationship to be anything but open, honest, and productive. We will certainly disagree a lot on your agency’s implementation of Obamacare, on the application of premium tax credits to Federal exchanges, and on IRS spending, just to name a few issues.

Sometimes a relationship will be contentious. Sometimes it will be congenial. Hopefully, more the latter than the former, but that will depend a lot on you and maybe a little bit on us too.

When we look at the IRS’s operations, there are a handful of basic principles the agency must follow in order to maintain its good working relationship with this committee. Today I am going to talk about three of those principles.

First, the IRS must spend taxpayer dollars wisely. As the agency that collects taxes from American workers and businesses, your agency will continue to be under especially tough scrutiny when it comes to how it spends the money Congress appropriates, and, unfortunately, the IRS’s operations do not appear to be able to withstand such scrutiny at this time.

When you reverse the positions of your predecessors and award bonuses to employees who have not paid their taxes, when your agency throws lavish conferences, and when you spend tens of millions of dollars on public sector union activity, the public loses faith in your ability to spend more money wisely. Now, some of that was not your fault.

When your agency pays tens of billions of dollars in improper payments every year, when the IRS mails thousands of fraudulent refund checks to a single home address, and when a quarter of all Earned Income Tax Credit payments are improper, the public loses faith in the IRS’s ability to protect tax dollars carefully.

Secondly, the IRS must treat taxpayers fairly and respect their rights. Recent scandals have given Americans reason to doubt that the IRS will treat them fairly. While the targeting of applicants for tax-exempt status may have happened before your tenure, taxpayers must have confidence that those days are over.

Now just before, Mr. Koskinen, you became Commissioner, the IRS and the Treasury Department released a proposed regulation that would limit the ability of social welfare organizations to engage in speech about matters of public importance. After an outcry from all sides of the political spectrum, the proposed regulation was withdrawn. But now I hear you have a plan to reissue it. I think this would be a mistake, and I hope you do not go down that path of trying to limit political speech. That would only further entangle your agency in needless political debate and controversy.

Third and finally, the IRS must be open and honest with this committee. We must have a mutual trust between us. I believe you to be an honest man, and, when you tell me something, I take you at your word. But it is because of this trust that I am concerned about a recent development in the committee’s investigation of political targeting at the IRS.

Last July, your agency told the committee that it had completed its production of documents regarding Lois Lerner, the central figure in the investigation. Then late last month, as the committee worked to finalize its investigative report, your agency delivered 86,000 pages of new documents, including 30,000 pages of new Lois Lerner documents, including new e-mails—30,000 pages of new documents, e-mails that fill 8 boxes, and I have here about a tenth of those just in this pile that I cannot even lift. I might be able to if I stand up. But I have about a tenth of those.

These documents are central and relevant to the committee's investigation. They were given to us without notice or explanation roughly 20 months after we made our initial document request and really after Senator Wyden and I and other members of this committee thought we were going to be able to have a final report on this matter.

Now, this is not the way to build trust with this committee. This prolongs the committee's investigation and raises more questions than it answers. We will be following up on this matter more after today's hearing.

Now, Commissioner Koskinen, we are here today to discuss your agency's operations and the President's budget proposal. There is much to discuss on these two topics, and I look forward to hearing your testimony and answers.

In your opening remarks, I would appreciate it if you took the time to address three specific concerns that I have. First, I would like to hear what the IRS plans to do to address the consistently high levels of fraud and overpayments for the Earned Income Tax Credit.

Second, I would like to hear what specific changes you plan to make in the agency's spending habits to deal with the budgetary shortfalls you have publicly decried.

Third, I would like to hear about any contingency plans you have in place in case the Supreme Court invalidates the current structure of the Affordable Care Act tax subsidies later this year.

I hope that today can mark the beginning of a new chapter in the long, historic relationship between the IRS and Senate Finance Committee. I hope it is a good chapter, but, once again, that is ultimately up to you, it seems to me.

Let me just say that this is one-tenth of what we are talking about. This is a huge number of documents, and you can see the reason why I am a little bit concerned and maybe a little bit upset as well.

[The prepared statement of Chairman Hatch appears in the appendix.]

The CHAIRMAN. Senator Wyden, we will turn to you for your opening statement.

**OPENING STATEMENT OF HON. RON WYDEN,  
A U.S. SENATOR FROM OREGON**

Senator WYDEN. Thank you very much.

Mr. Koskinen, I share Chairman Hatch's concern about bringing our bipartisan inquiry to a halt, and to get that done, to complete it in a thoughtful and a bipartisan way, we are going to need these

documents. And as the chairman noted, we thought we were going to get some, and we are going to need them and need them quickly.

Whenever I talk with Oregonians in meetings or town halls, the conversation nearly always comes down to the same core issue: the struggling middle class. Years after economists first said that the recession officially ended, too many middle-class Americans feel like they are standing on quicksand because the recovery has yet to reach them. So the challenge facing policymakers is putting America's middle class on solid economic ground, growing their paychecks, and ensuring that our recovery reaches every one across America.

That challenge is going to be top of mind at each of the three hearings, colleagues, that we hold this week. Tomorrow and Thursday, the committee will talk with HHS Secretary Burwell and Treasury Secretary Lew about the administration's plan to save Americans money on health care, create jobs, increase wages, and invest in the middle class. Today the committee has an opportunity to discuss the status of America's accounting department, the Internal Revenue Service, with the Commissioner, John Koskinen.

With W-2 forms in the mail and the tax season beginning, our country's annual headache is now setting in. And I want to emphasize that, today, taxpayers reside in two separate worlds. In one world, a middle-class office employee pays taxes directly out of her wages, and she is subjected every spring to the painstaking process of filing returns.

Colleagues, for that office worker, there are no complicated tax avoidance strategies at her disposal. She does not have any shelters. She does not have any vehicles for her to hide her income. Meanwhile, in the other tax world, teams of accountants go out to pry open loopholes that are hidden in the tax code, and the line between right and wrong is murky at best.

The inherent unfairness of America's tax system is a blow that falls hardest on the middle class, and it takes a number of forms. The most obvious is that, every year, families spend more time and money filling out their taxes. People are worried about compiling all their records, completing all the forms, and then filing them correctly.

Unfortunately, the tax code itself has not gotten any simpler, and the lack of resources at the IRS has slowed service in a number of instances to a crawl. Nina Olson, who is the independent IRS Taxpayer Advocate, says, and I quote here, "This is the most serious problem facing taxpayers."

When Americans call into IRS help lines, they often sit in long queues listening to hold music. Protections against identity theft are delayed. Taxpayers who worry they might be victims of scams cannot end up getting the timely assistance that they need. Families that depend on a refund to help cover the mortgage or tuition get left waiting.

Now, there is a second issue to consider today. According to the Internal Revenue Service, nearly \$400 billion in taxes go unpaid each year. That is the tax gap. One of its biggest causes is the dishonesty of tax cheats and scammers who avoid paying what they owe. And it is important to reflect on who gets the short shrift as



a result. It is the middle-class wage earner once again whose taxes come straight out of their paycheck.

Honest taxpayers have to make up the difference when the scoff-laws dodge their responsibilities, and that is wrong. But until Congress simplifies and restores fairness to the broken tax code, multinationals and those with high-priced accountants can continue to find loopholes.

There is no question that the IRS can make better use of the resources it has. That is true for every Federal agency, every private business, and the Congress itself, and it has been acknowledged by Commissioner Koskinen and his predecessor. Meanwhile, policy-makers cannot lose sight of the biggest challenge today, which is putting our middle class on solid economic ground.

There are going to be many more opportunities for this committee to work on a bipartisan basis with the Commissioner and the IRS to make the system work better for middle-class families, including through comprehensive tax reform. The ultimate goal ought to be fairness. And as I wrap up, I want to come back to the fact that taxpayers should not be divided into two worlds, one of which today carries a much heavier burden than the other.

Commissioner, we look forward to working with you and our colleagues to make that a reality.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator Wyden.

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

The CHAIRMAN. Our witness today is IRS Commissioner John Koskinen. Commissioner Koskinen has been serving as the head of the Internal Revenue Service since December 2013.

Mr. Koskinen has broad public-sector experience, including having served as Chairman of the Board of Freddie Mac, City Administrator for the District of Columbia, and Deputy Director for Management of the Office of Management and Budget, three really difficult and trying positions.

Mr. Koskinen also has extensive private-sector experience, including working as the president of the United States Soccer Foundation and as the president and CEO of Palmieri Company.

Mr. Koskinen graduated with a JD from Yale University School of Law and a BA in physics from Duke University.

We want to thank you, Mr. Commissioner, for being here today. Please begin with your statement.

**STATEMENT OF HON. JOHN A. KOSKINEN, COMMISSIONER,  
INTERNAL REVENUE SERVICE, WASHINGTON, DC**

Commissioner KOSKINEN. Chairman Hatch, Ranking Member Wyden, and members of the committee, thank you for the opportunity to discuss the IRS budget and current operations. As the chairman noted, we at the IRS value our working relationship with this committee, with the chairman and the ranking member, and we look forward to a productive dialogue and constructive working relationship over the next 2 years of this Congress.

First of all, I am pleased to report that the 2015 tax filing season opened on schedule on January 20th and is going well so far. We have accepted more than 16 million tax returns, and we have start-

ed issuing refunds. And in fact, to show you how much people care about the refunds, we have accepted 16 million returns and already had 8 million hits on our *Where's My Refund?* app on the website.

Opening the current filing season on schedule was a major accomplishment given the challenges we faced. This achievement is a direct result of the dedication, commitment, and expertise of the IRS workforce.

Along with normal filing season preparations, there were significant challenges and extra work to get ready for the tax changes related to the Affordable Care Act and the Foreign Account Tax Compliance Act. We also had to update our systems to reflect the tax extender legislation passed in December.

Despite this success, I remain deeply concerned about the agency's ability to continue to deliver on its mission in light of significant reductions in our budget. Just a month ago, the agency's fiscal year 2015 budget was set at \$10.9 billion, \$346 million less than 2014, and really \$600 million less than last year when another \$250 million in mandated costs and inflation that we must absorb are counted. Plus, that is on top of a \$600-million cut the IRS had already taken as a result of government-wide sequestration in 2013. The IRS is the only major agency that was not subsequently restored to the pre-sequester level.

These funding cuts are so significant that efficiencies alone cannot make up the difference. We continue to find efficiencies wherever we can and are presently saving \$200 million a year as a result of significantly reduced office space, printing and mailing, and use of contractors. But we have reached the point of having to make very critical performance tradeoffs.

In allocating our limited resources for 2015, we tried to keep in mind the needs of both taxpayer service and enforcement to avoid overly harming one part of our mission while attempting to do another.

Rather than going into greater detail about this, let me respond quickly to the points the chairman raised. First, with regard to the Earned Income Tax Credit, we are concerned about the high level of improper payments and the volume. The agency has been working for over 10 years struggling with this challenge, and, as I have testified before this committee before, we are asking Congress to give us additional tools to deal with the problem. They would include legislation to provide us with W-2s earlier. We should be able to get them at the same time employees do so that we could match them and find fraud and improper payments earlier.

If we had correctable error authority, we could correct errors in returns, particularly EITC returns, when we have data that show that the returns are erroneous; but the only way we can correct them now is by doing an audit.

And finally, if we had the ability to require minimum standards of tax preparers—over half of the EITC returns are prepared by preparers, the vast majority of whom do a great job. A reasonable number are stymied by the complications of the Act, and a small number of preparers are actually crooks who take advantage of taxpayers and seize all or some portion of their refunds. This committee and Senator Wyden have a bill that would restore our ability to require minimum standards for tax preparers, just the way

there are minimum standards for everybody from hairdressers to others who provide public services.

With regard to spending, as I have noted, we have taken actions wherever we can. The famous convention that was held inadvisably 5 years ago no longer could be held. Every expenditure of \$50,000 or more for training or conferences has to be signed off personally by me and reviewed and signed off by the Treasury Department. So I am confident that those situations are not going to arise again.

With regard to the 501(c)(4) investigation, we represented to you last spring that we had completed the production of documents related to the determination process. Since then we have provided hundreds of thousands of pages of additional documents requested by any one of the six various investigations going on.

The documents you have received are not more documents about the determination process. They are documents that have been requested by different committees, particularly in the House, or more information about other peripheral players in the program and other detailed documents with regard to e-mails from those participants.

All of those are responsive to requests we have had. Virtually none of them have anything to do with the determination process, but we have been pleased to provide them in an attempt to answer any question that anybody has and requests for documents on any matter. Our cover letter I thought explained where these documents came from. They are not, in fact, inconsistent with the earlier representations we have made.

My time is running out. I will be happy to answer questions about the President's budget for 2016, which would go a significant way toward restoring our ability—if I had a little additional time, that would be very helpful.

The other point you raised was with regard to our payment of performance awards to those who are delinquent on their taxes. First of all, I would like the record to note that the IRS has the highest compliance rate of any agency in government, including the Congress. Over 99 percent of our employees are compliant with their taxes, and that is because they take it seriously. It is an important responsibility for anybody who works for the Internal Revenue Service to be current on their taxes.

Those who are not compliant include those who are making installment payments, who are working toward compliance. But it is clear, and it is clear to our employees that if you willfully do not pay your taxes, not only are you not eligible anymore for an award, you are subject to disciplinary action, including, in some cases, severance from the Service, and we do that on a regular basis. So I am confident that performance awards are only going to go to those who are eligible for them.

Let me talk just a minute about the President's fiscal year 2016 budget. The request totals \$12.9 billion and is consistent with recommendations the President has made over the last several years. The level of funding would provide substantial support for our mission and help the agency move ahead in a number of critical areas. For example, we would be able to raise our phone service level to nearly 80 percent and significantly reduce the inventory of taxpayer correspondence.

With respect to information technology, we would be able to properly maintain our current IT infrastructure. The funds would also help us work toward our goal of providing taxpayers with the same experience dealing with the IRS online as they now have with their financial institutions.

On the enforcement side, the President's budget proposal would allow us to reverse the decline in individual audit coverage and increase document matching programs, which are critical to ensuring high rates of voluntary tax compliance. We would also be able to expand programs to prevent refund fraud related to identity theft and to improve international tax compliance.

Using the resources provided by the President, we estimate that our efforts to improve enforcement will generate \$60 billion in additional revenue over the next 10 years at a cost of \$19 billion, thereby reducing the deficit by \$41 billion.

We would also use a portion of the funding request to continue implementing legislative mandates, including the Affordable Care Act, the Foreign Account Tax Compliance Act, and the newly passed ABLE Act. As I noted in my complete testimony, the irony did not escape me that we were assigned new responsibilities under the new ABLE Act, and the pay-for for it, which is a program for professional employer organizations, is the same bill that cut our budget by \$350 million.

I want to stress, though, that we are required to implement these laws. So, if we do not receive necessary funding, we will have to continue to take funds from taxpayer service, enforcement, or IT. That is because we believe that we have an obligation to enforce and implement statutory mandates, and we will do that with the ABLE Act and with the Professional Employer Organizations provisions.

Along with providing the IRS with adequate funding, Congress can also help improve tax administration by enacting several proposals in the administration's 2016 budget request, which include the proposals I mentioned earlier with regard to earlier provision to the IRS of third-party information returns, such as W-2s, which would allow us to match the documents, and also if we could correct errors without having to audit returns, we would become much more efficient in terms of stopping improper payments.

That concludes my statement. I appreciate the additional time. I will be happy to take your questions.

The CHAIRMAN. Thank you, Mr. Koskinen.

[The prepared statement of Commissioner Koskinen appears in the appendix.]

The CHAIRMAN. Your fiscal year 2015 budget is about 3 percent lower than your fiscal year 2014 budget, which has been decreasing since the high water mark of 2010.

Now, we may disagree about how best to spend taxpayer dollars, but we will stipulate the fact that your agency has been forced to absorb budget cuts, although, as you will see in the chart behind me, your budget fluctuations look a little less dramatic when we do not use 2010 as the baseline.

I have another chart that I think reveals the true problem. It is not IRS's budget. It is an ever-growing set of tax laws and an ever-

increasing number of Federal programs the IRS is charged with administering. A lot of that is our fault, as I view it.

Instead of only focusing on spending more money, we should instead focus on what is driving that need for bigger budgets, and that is the growing complexity of the tax code. The length of the tax laws has more than tripled since 1975. American families and businesses spend an estimated 6.1 billion hours, that is with a "b," and \$163 billion each year simply complying with the tax laws.

Now, we should not blame you for this. Congress is the one that keeps adding to your growing responsibilities, and Congress enacted the poorly designed and bureaucratically unmanageable behemoth known as Obamacare, or should we use the other term, quote, "Affordable Care Act," unquote.

Congress enacted the labyrinth of new rules known as the Foreign Account Tax Compliance Act. But I hope you can recognize that there are two sides to this coin: the amount of money that Congress gives you to do your work and the amount of work that Congress gives you to do.

I would love to hear you talk about the latter and not just the former. I want to hear your thoughts about the growing number of programs and policies your agency is tasked with that you have to administer.

Will you work with the committee on ways we can reduce the burdens of tax compliance and streamline the number of growing responsibilities placed on your agency?

Commissioner KOSKINEN. Yes. I appreciate that. As I have told our employees as I have visited offices around the country (I have now talked with over 13,000 IRS employees), in many ways, even with the background noise and challenges the agency faces in some charges, it is instructive that, as you note, Mr. Chairman, the IRS continues to be asked to implement new programs.

To some extent, that is because there is some confidence that if you give the program to the Internal Revenue Service, it will get done, and it is a can-do agency. And, as I have noted earlier, we are committed to implementing whatever statutory proposals the Congress provides.

But you are correct that the tax code has gotten to be extremely unwieldy. And I always preface any remarks I make by saying that tax policy is the domain of the Treasury Department, the White House, and the Congress. We are in the tax administration business. You tell us what the tax laws are, and we will do our best to administer them.

Having said that, as I have also, I think, made clear to you in our meetings and also publicly, I am a great believer in tax simplification for the very reasons you mentioned. If we could simplify the tax code, it would, on the most important basis, make life simpler for taxpayers. It would be easier for them to determine how much they owe and how to pay it.

Our experience is, most taxpayers want to do the right thing, want to be compliant. They are spending those 6 billion hours simply trying to determine what the right amount of tax is to be paid. To the extent we could simplify the code, it would make their lives simpler, and it would clearly make our life much simpler.

So the two things we look at, as you say, beyond where we are in terms of budget cuts are, first, if the tax code were simpler, it would allow us to function more efficiently with the resources we have without adding back.

The other thing I would emphasize, which I mention in my testimony, is we feel strongly that we need to look to where we want to be in 3 to 5 years, what should the taxpayer experience be 3 to 5 years down the road. And, if we had the funding provided in the President's budget, we would continue to build our online capacity, ultimately hoping to provide taxpayers with the same online account with us that they have with their banks or their financial institutions.

They should be able to come online, be properly authenticated, look at previous tax returns, and look at the status of their filings. We should be able to immediately communicate back to them when they file without having to write a letter or have them call us and say, "Did you forget this? We have another schedule here that is not in your return." And they should simply be able to make that correction without even filing an amendment. It should be able to be done quickly and efficiently.

If that happened, we could obviously run much more efficiently and effectively. The people who called us would be people who needed to get specific information, not people calling as a regular matter of course.

So I think on both counts, if we could actually build toward a better taxpayer experience from our standpoint, if we had a simpler tax code, taxpayers would have a much easier time determining what they owe and filing, and we would have a much easier time and be more efficient running the tax administration.

The CHAIRMAN. Thank you. We are going to try to do that. It is going to be difficult with this Congress, but we will do the best we can.

Senator Wyden?

Senator WYDEN. Thank you, Mr. Chairman.

Commissioner, let us talk about the middle class in this filing season. Senator Cardin and I, we are going after these unscrupulous tax preparers. And the combination of that and Nina Olson's comment about the shrinking resources you have, particularly to go after tax cheats, the costs of those things get heaped onto the middle class.

What should the middle-class taxpayer expect this filing season?

Commissioner KOSKINEN. As I noted, we are delighted that the filing season thus far, 3 weeks into it, has gone smoothly. We encourage people to file electronically. Over 85 percent of people filed electronically last year. We have said, "Collect all of your information; make sure, to the extent you can, your return is accurate." If you file an accurate return online, it will be processed quickly. Your refund will be processed within 21 days. Your filing experience should be a positive one.

The difficulties come where people often inadvertently file incorrect returns, which causes us to have to write them. They have to write us back, they have to call, and we end up with a significant amount of work for us and a certain amount of concern on the part of taxpayers.

But I would stress, overall we expect to process 150 million individual tax returns this year. We expect that the vast majority of those will go through without a problem. Over 80 percent of people under the Affordable Care Act, for instance, will simply check a box and say they have coverage.

But most importantly, the vast majority of those people, particularly the 85—we hope it will be higher—percent of people who will file electronically, will simply file and that will be it.

Senator WYDEN. Another concern of middle-class families is the growing problem of identity theft. And the Internal Revenue Service is supposed to issue these PINs, identity protection PINs, to taxpayers who have been the victims of identity theft.

But I am hearing from taxpayers in Oregon that many of them have not received these PINs, and I am also hearing stories in my State that some victims of identity theft are already being revictimized this filing season, as the fraudsters go out and file tax returns with their Social Security numbers while they wait day after day for the IRS to send them these identification PINs.

I think it would be very helpful if you could tell the committee when Americans are going to receive these PINs and, particularly, what to do to help these people who otherwise could be victimized again.

Commissioner KOSKINEN. I would say it is an important problem that is at the top of our list. We have been fighting refund fraud and identify theft for several years now.

With regard to the identity protection PINs, we expect to issue about 1.5 million of those.

Senator WYDEN. And when will that happen?

Commissioner KOSKINEN. The PINs will all be out at the end of this week in the mail. Our problem has been, we are running an antiquated IT system.

Part of the question has been, why do we spend so much on IT? The real question is, how come we cannot spend more? We are running applications we were running when John F. Kennedy was President. That is how antiquated this system is.

We had a problem over the last couple of weeks with the part of the system that issued IP PINs. Every year, if you have an IP PIN, you get a new one. It has to be authenticated, and we mail it to you. The system had difficulties. We have solved those difficulties. But they are difficulties that should not exist. It should be a straightforward issue.

In any event, they will be in the mail before the week is out.

Senator WYDEN. One last question with respect to the Affordable Care Act. We are starting to get a lot of questions with respect to people filing their tax returns to comply.

What are you all doing to inform and assist taxpayers with these requirements?

Commissioner KOSKINEN. We have spent the last 9 months trying to spread the word about how the Affordable Care Act was going to operate. We were concerned starting in the spring that anyone who bought a policy through the marketplaces and was getting an advance payment paid to the insurance company for their premium, to help them with their premium, needed to make sure that, if there was a change in their circumstance—their spouse got

a job, they got an increase in pay, their family situation changed—they went back immediately to the marketplace to correct that information so they would not be surprised during filing season.

We have provided a special section on our website devoted totally to the Affordable Care Act. We have met with tax preparers around the country, tax attorneys. We had tax forums with 10,000 preparers last summer who were given—we had 40 seminars at those gatherings about the Affordable Care Act. We have over 100 YouTube videos.

We have already had about 800,000 hits on the Affordable Care Act part of the website. When you call us, while you are waiting to get through, one of the things we have put in is an information channel that you can dial into. It will give you all of the frequently asked questions and answers about the Affordable Care Act.

We have been sharing information with all of your offices so, when your constituents call, you will be able to work through what are the basic questions, what are the answers.

So we have flooded the zone with information.

Senator WYDEN. My time is up, Commissioner. I just hope that you all will recognize that taxpayers who received assistance last year, of course, are going to have some questions about the steps to take to comply this year, and I hope there will be a special effort to reach out to them. Thank you.

Thank you, Mr. Chairman.

The CHAIRMAN. Senator Cornyn?

Senator CORNYN. Thank you. Mr. Commissioner, no doubt you have a daunting responsibility, but American consumers and middle-class families whom the ranking member alluded to several times have had to make do with less during the years following the Great Recession and when middle-class wages have been stagnant.

So the question is, why can't the government do more with less, and, specifically, estimates are that about a quarter of Earned Income Tax Credit payments in fiscal year 2013 alone were paid in error. This means that about \$15 billion—\$15 billion—was wrongly paid. But if you spread it over 10 years, from 2003 to 2013, obviously, that is a big number too. It is \$150 billion of improper EITC payments.

It appears that the improper payment rate has remained relatively unchanged and the amount of EITC claims paid in error has grown despite the efforts that your agency has made. On top of that, as you know, it appears that the improper payment rate for the Additional Child Tax Credit is similar to the Earned Income Tax Credit. According to the Inspector General, at least a quarter of all ACTC payments for fiscal year 2013 were improperly made, with potential improper payments totaling as high as \$7.1 billion; so, just in 1 year, 2013, more than \$22 billion in improper payments by the Internal Revenue Service.

And then there is the issue that I know you are familiar with about the tens of millions of dollars that the agency spends on union members who perform no work that benefits the taxpayer. It is estimated that in 2013, roughly 500,000 hours were spent at a value of roughly \$23.5 million. Again, these are union members who represent their union in the workforce there at the IRS who perform zero work that benefits the American taxpayer, and yet



their appears to be no real concern about how to cut down that cost and redirect more of that money to doing the IRS's job.

So I would just ask you this question. Given the amount of money that the IRS pays out improperly, some \$22 billion just in 2013 alone, and given the money spent on nonproductive activity, at least in terms of that benefitting the taxpayer, due to the union activity, not to mention employee bonuses and the like, how do you think that the American people will feel about your coming here and just asking for more money?

It seems to be, as the chairman points out, a historically established activity where bureaucrats come in and ask for more money without cleaning up their own house and taking care of their business. It seems to me that if you are coming here asking for more money, we would be more likely motivated to provide more money if, in fact, the IRS was spending the money that it currently gets to deal with things like these improper payments.

Commissioner KOSKINEN. It is a good point. I would note that we are not asking for more money over history. We are asking for money back that has been taken away. Our budget has been cut, in absolute terms, \$1,200,000,000 since 2010.

As the chairman notes, the tax code has gotten more complicated. We have 7 million more taxpayers. We are charged with implementation of the Affordable Care Act, the Foreign Account Tax Compliance Act, and tax extenders as they go forward. So we are actually doing significantly more with significantly less.

There comes a point at which you have to do less with less, and we have reached that point. We have, as I said, saved \$1 billion over that 5 years in efficiencies, with less office space, fewer contractors, less printing.

We have worked very hard, as we have talked about, on the Earned Income Tax Credit. Part of our problem is, we do not have the resources—we have declining resources to audit in that area. We have 5,000 fewer revenue agents, revenue officers, and criminal investigators than we had 5 years ago, and that is solely because of the decline in expenditures.

Senator CORNYN. And you have asked for roughly 9,000 more, or the President's budgets asks for roughly 9,000 more employees for the IRS to implement the Affordable Care Act. Correct?

Commissioner KOSKINEN. The 9,000 employees would not be to implement the Affordable Care Act. The 9,000 employees—if we got 9,000 back, we would replace some of the 5,000 revenue officers we lost. We would replace all of the 3,000 fewer people we have answering phone calls than we had 5 years ago. The number of phone calls has gone up significantly, as you can imagine.

With regard to union time, first of all, it is part of the bargaining relationship with our union, the way it is in every government agency across the government. That work benefits taxpayers to the extent that it represents workers and works with them to ensure that their working conditions are appropriate.

We have, in fact, cut those with the union, cut that time that is being spent by over 10 percent, and we continue to work with them to make sure that that time is spent effectively. But we are not the only agency that does that. That is a program that exists every place there is a union across the government. We find that the

union is an effective partner with us in terms of trying to improve the operations of the agency.

But I would conclude by saying we have done significantly more with significantly less. But my concern for the last year has been that we are beyond the point of being able to do more with less. We are at a point where we have no choice but to do less with less.

Senator CORNYN. Mr. Chairman, I would just ask for your help perhaps. I know Representative Boustany over in the House had sent a letter to the Commissioner in September 2014 asking him specifically to respond to some questions about the union activity at the IRS, and its alleged benefit to taxpayers, and there has been no response. That has been since September 2014.

So if we could get an answer to that letter and some of those questions, it would be very helpful to our understanding of what you are talking about.

Commissioner KOSKINEN. I would be delighted. I am not aware of that letter. My operating assumption, as the chairman knows, my commitment was that I read every letter I get, and we try to respond as quickly as we can, and no later than a month.

The CHAIRMAN. I appreciate that. Let us have Mr. Boustany resend him the letter, directly to him, and let us see if we can get that answered.

Commissioner KOSKINEN. In fact, I have met with Congressman Boustany a couple of times. We have what I think is a good working relationship, and I am very surprised to find out there is a letter that has not been answered for that period of time, because that is not our present mode of operation.

In fact, the chairman—

The CHAIRMAN. We will get that letter resubmitted, and maybe you can get us an answer.

Commissioner KOSKINEN. I would note that the chairman last week sent me two different letters, and I hope to have an answer to those letters to you in the next few days.

The CHAIRMAN. That would be great.

Senator Cardin?

Senator CARDIN. Thank you, Mr. Chairman.

Mr. Commissioner, I want to thank you. This is a tough job, and you continue to serve your country in this capacity, and I thank you very much for your willingness. You are the right person. I wish you had more support.

It seems to me there are two things that this committee—the Senate and particularly this committee—should be doing. First, we should look at our tax code and make it simpler and more predictable, and I know the chairman and ranking member are working to see whether we cannot find common ground in that regard, and that would certainly help a great deal. If we gave Americans more confidence in the tax code, I think taxpayers would appreciate that, and that would make your job a lot easier.

The second thing is that this committee particularly should be an advocate for you having the resources you need in order to carry out the mission. I remember—I guess it has now been a decade ago—working, when I was in the House of Representatives, with then-Congressman Portman following up on the study that was done at the IRS at the time, and it was the Ways and Means Com-

mittee and the Senate Finance Committee that said to the appropriators, you have to have resources to modernize. And it lasted about 1 year before the cuts came back.

So this committee should be your advocate for adequate resources. Instead, as you pointed out, you have sustained real cuts while your missions have increased dramatically.

And we want to have tax compliance in all sections. I listened to Senator Cornyn's concerns about the Earned Income Tax Credit. The Earned Income Tax Credit is an extremely important provision in our tax code that offers fairness to middle-income working families. And yes, we want to make sure it is complied with, and Senator Wyden and I are going after, and hope to give you the authority to go after, paid tax preparers who are not doing the right thing in that regard.

We want to give you those tools. But it is interesting that I do not hear the same strength on behalf of compliance with the high-income provisions that Senator Wyden mentioned in his opening comments that are available to high-income people or on business income. I know there was an IRS study that showed that, in some cases, over 50 percent of business income is not being reported.

So, how do you decide with these limited resources how you are going to be able to get tax compliance when it is complicated and you are going against, particularly in the business side or high-income side, individuals who have tremendous resources to try to minimize their tax liability?

How do you make those judgments? I would just urge you to spend more effort dealing with those who have sophisticated services that are not paying their fair share of taxes.

Commissioner KOSKINEN. It is the challenge we have. Ultimately, we are all concerned with the compliance rate, to make sure we collect \$3 trillion a year. My concern is that when the compliance rate drops by 1 percent, it costs the government \$30 billion a year.

The two sides of the compliance coin are enforcement and taxpayer service. And our challenge, as our budget is cut, is to try to make sure that we maintain as much effort in all of those areas as we can.

But even in the area of auditing, we cannot take one area of the tax-paying public and say, well, we are not going to bother with you because there are other people out here who have more revenues, because, if you look at where the revenues come from, they come from across the spectrum.

So our challenge is to continue, in our exam plans and our audit plans, to try to maximize the enforcement activities of the agency. But as I noted, we have 5,000 fewer people doing that now. So inevitably, our audit rates are going down, and our concern about that is that at some point that is going to affect the overall compliance rate.

Senator CARDIN. I would just make the point that if you had the additional resources, we would not only get better compliance—which is our responsibility, to make sure we have compliance—we would get greater revenue, which would help those taxpayers who are paying their taxes get the relief, so they are not over-taxed while other people are not paying their fair share.

So it seems to me what this Congress has done in cutting your budgets makes no sense, and I am disappointed that this committee has not been a stronger advocate on your behalf, on the agency's behalf.

One last point I would make. You are now implementing the Affordable Care Act and the provisions under the Affordable Care Act in this tax season. Booz Allen, which has a large presence in my State, has given high marks to the program you are using in regard to the refundable tax credit. What reactions are you receiving as you have tried to implement this as to the tools available to IRS to try to make the tax season as friendly as possible?

Commissioner KOSKINEN. Thus far, we have had no significant challenges, although I would stress that we are at the front end of the return process. We expect the month of February will see a significant increase in the volume of returns.

One of the best things we have going for us is that 91 percent of the tax-paying public uses software, either with a paid preparer or they buy the software, and we have worked with software providers. So the software will take people through the application of the Affordable Care Act in whatever way it applies to the taxpayer, whether it is simply showing coverage, applying for an exemption, or reconciling the advanced payment they have gotten.

Again, as I have noted, we have calculators on our website that will allow people to make the determinations that need to be made, and thus far we have had positive responses. But I would stress we are at the front end of what is going to be a very interesting filing season.

Senator CARDIN. Thank you. Thank you, Mr. Chairman.

The CHAIRMAN. Senator Coats?

Senator COATS. Thank you, Mr. Chairman.

Mr. Koskinen, first of all, I want to state that what the chairman and vice chairman have stated relative to our unbelievably complex tax code has to be addressed, and I know both the chairman and vice chairman are committed to that process, and I hope all of our colleagues here are committed to that process, because it is clearly having a negative economic impact on us.

The complexity of just simply going through the process of paying your taxes every year and the money that is spent and the hours that are spent, we just simply cannot keep pushing this down the road.

So your response to that is that you applaud that very act, and I appreciated that. And I know you are concerned about the amount of money you have to spend and the burdens that you have. I would like to just give you a little bit of what I think might be some quick relief. This is a small ball thing.

But Senator Cardin, who just spoke, and I are going to be introducing, this week, legislation that I hope you will be able to support. It is legislation that addresses the notification—it is called the NOTICE Act—legislation that will give charities, 501(c)(3)s and so forth, notice if their status is going to expire.

A few years ago, the law was changed so that if the applicant's information, information required by the IRS to keep the status, was not supplied over a period of time, they would be automatically dropped from the qualification of tax-exempt status.

Now, there are a bunch of little—I mean, there are tens of thousands of small charitable organizations out there that simply do not have the back room for this, do not have lawyers waiting and plowing through the regulations and advising them of what they need to do and when they need to do it. And so it seemed to us, Senator Cardin and I—this is a bipartisan effort here—it seemed to us that a simple fix on this would be simply to provide them sufficient time of notice that, hey, your status is going to expire because we have not received your paperwork relative to annual reporting.

What has resulted is thousands of hours and tens of millions of dollars to reinstate tax-exempt status, which I think imposes a significant burden on the IRS. And so what we are really calling for here is—well, let me just give you an example.

There is a small women’s auxiliary in Indiana that had filed for and received tax-exempt status. They had some leadership changes during that time. They wanted to raise \$15,000 to help with the volunteer fire department, and, because of the leadership changes and because they did not really have somebody in the back room to give them notice and they did not have the money to hire lawyers and accountants and so forth and so on, they hit the deadline, and they were automatically then denied their tax-exempt status. It cost them \$10,000 to reinstate, a lot of paperwork, and months and months and months of waiting. I think the figure is something like 80,000 to 85,000 of these that have had to reapply.

Our act would just simply require IRS to provide notice. Now, I would think in today’s digital age, you probably have all these 501(c)(3)s listed somewhere in the database and it would be simply a matter of adjusting that so that, say, within 90 days out or 100 days out, you hit a button, notices go out, whether it is by mail or by e-mail or both, to these, saying “warning” or “take notice,” you did not file your information report and your tax-exempt status is going to expire unless you respond and file that. That is just one piece of paper. But it would save, I think, thousands of hours and months and months of delay and significant cost to these small charities if we could do that.

So I would like to just put that on your plate. It is a small ball thing. It is just one step toward finding efficiency and effectiveness, which I think we can use, and it is needed so much throughout government, which is still doing a lot of things the old-fashioned way—a lot of files, a lot of paperwork, rules that do not seem to make much sense.

I do not know if you want to comment on that. My time is about to run out. But we are going to introduce that, and, if you could work with us on that, we would appreciate it.

Commissioner KOSKINEN. We would be delighted to work with you on that. We have about 1,600,000 outstanding tax-exempt organizations. So it is a big ball number when you look at it that way.

We were concerned—it was before I got here. We streamlined the reinstatement process for entities. They could simply send us their notice. They hopefully did not have to spend \$10,000.

For small organizations, we have also streamlined the application process. You can now apply with a 3-page application rather

than the 26-page application, because our concern is, for a lot of small charities out to do very good things, for them to have to spend \$5,000 or \$10,000 simply to get certified, if they are a very small organization, does not make much sense.

We are delighted to work with you on this. I think there are thousands of these organizations out there. And you are exactly right. For a lot of them, the secretary moved, the president changed, they lost track of it, and we need to make sure that we streamline the process for any reinstatement necessary.

We are continually trying to streamline the process for the application so we can have people out there doing good work.

Senator COATS. That is good for going forward. I am told that—a staffer just told me that the simplified application is not available to charities that need retroactive reinstatement. So this would address retroactive reinstatement.

Commissioner KOSKINEN. And we would be delighted to work with you on it.

Senator COATS. Terrific. Thank you.

The CHAIRMAN. Senator Brown?

Senator BROWN. Thank you, Mr. Chairman, very much for doing this hearing to clarify a lot of issues that are out and about in the media all over this country.

I want to talk for a moment—a number of people have brought up the Earned Income Tax Credit and the Child Tax Credit. The chairman did, Senator Cardin did, Senator Cornyn did.

Let us not forget what this is about. The Earned Income Tax Credit began as a temporary program with President Ford and was made permanent by President Carter. It was expanded dramatically by President Reagan and has been supported by Presidents of both parties for—I believe this is the 40th anniversary this year.

So we know that they collectively—EITC and CTC—have reduced poverty for 32 million people, including 13 million children. We should not forget that as we talk about this.

Now, we hear of the 23-percent fraud rate. Many call it the fraud rate, others say it is an error rate. That factor assumes a bunch of things. That 23 percent assumes that all audited returns are fraudulent. It does not factor in underpayments.

The Office of the Taxpayer Advocate, an independent office within the IRS, has found that findings of fraud were overturned in 40 percent of cases where a taxpayer was accused of alleged EITC fraud and then sought the advocate's assistance. We know that people who file for EITC are less likely to have a strong advocate whom they employ to fight for them. We know all of that.

Now, when you take into account those factors, what is the incidence of genuine fraud for EITC? How would the actual loss of revenue to the Treasury look if EITC also counted underpayments, because underpayments are part of that 23 percent is my understanding?

Commissioner KOSKINEN. As you note, it is a complicated issue. That is why it is called the improper-payment question rather than fraud, because only a portion of the money that goes out is—

Senator BROWN. But many here call it fraud.

Commissioner KOSKINEN. Right. But it is an improper-payment issue derived, to some extent, by the complexity of the statute deter-

mining where children are resident and who has authority over them. There are inadvertent errors made by taxpayers filing on their own without a lot of background.

As I have noted, one of the reasons we support the provision of the act to require tax preparers to have some minimum level of competence and understanding of the law is that over 50 percent of those filing for the EITC rely upon preparers, and many of them, as you note, are lower-income or middle-income families who rely on somebody in the neighborhood. And our hope is that the somebody in the neighborhood ought to be able to file for them a correct return as we go forward.

So as I have said, we have asked for additional statutory authority which would allow us, particularly if we got W-2s earlier, to check whether there is under- or overstatement of income before we actually make the payment, which would help significantly.

Also, in some cases, we know that there has been an error. When somebody thinks they have three children and our database shows two, we ought to be able to correct that rather than making the payment or holding the payment and having to go audit, which is now the only way we can make that change.

If we could make the change, the taxpayer could still come in and say, "Wait a minute, I really do have three children," and they would not lose anything. We would simply be able to get much more at the heart of the range of improper payments.

The overall issue is that, even within this, we have this duality. We just had EITC Awareness Day in which we tried to make sure that everybody eligible for the program actually participates. But our estimate is about 80 percent of the people eligible participate, but 20 percent do not.

So we have this dual obligation, on the one hand, to make sure people participate, are aware of the program, and, on the other hand, to make sure that the payments are appropriate and that we are actually paying the right amount to the right people.

And if we had the additional legislative authority that we are asking for, I think we could actually give a greater—

Senator BROWN. That 23 percent would markedly be reduced.

Commissioner KOSKINEN. It would be reduced. We will probably never get it down to zero, but we have been concerned—I have been concerned since I started—that that level has been pretty constant over the last 10 years, notwithstanding all of the activities the agency has done.

So I had the meeting early in my tenure, and I said, I want everybody who knows about this to sit down to figure out what would help. And it turns out the legislative proposals we have made were the consensus of things we need to do to be able to attack this problem going forward.

Senator BROWN. I echo the comments that Senator Cardin made in his comments and questions, that there is so much less attention paid in the halls of Congress to the fact that we are not auditing as many upper-income people as you were just because of budget issues and that we seem to pay a lot less attention to the fraud of upper-income taxpayers than we do to EITC.

It is a peculiar kind—the worst kind, in my mind—the worst kind of class warfare by people who are paid good salaries and get

good pensions and health care from the government. Members of Congress spend an awful lot of time attacking a program that has brought literally millions of people out of poverty and has had a long, long, long, good history of support from Presidents of both parties across the liberal to conservative spectrum.

Mr. Chairman, thank you.

The CHAIRMAN. Senator Thune?

Senator THUNE. Thank you, Mr. Chairman.

Commissioner, welcome. I joined with other members of this committee last year on a letter to you after it was reported by the Inspector General for Tax Administration that more than 1,100 IRS employees with Federal tax compliance issues have been awarded over \$1 million in cash awards and more than \$10,000 in hours of time-off awards. In your response last May, you stated that the IRS was working toward trying to address this problem across the entire IRS, but you made no commitments nor did you set any deadlines for making certain this does not happen again in the future.

I know that you have talked a little bit about this already this morning, but I just wanted, for the record, to get you to speak clearly on this issue, because it seems to me it is awfully hard to go to the hardworking American taxpayers and ask them to comply with the tax laws when you have employees in your own organization who do not comply and, more than that, who are getting bonuses, hours off, additional benefits, payments, and cash bonuses when they have tax-compliance issues.

So can you commit to me that you are going to fix this problem and ensure that it is not going to happen again in the future?

Commissioner KOSKINEN. We have already adopted policies to address the problem. Anyone who willfully is not complying with their tax obligations is not only ineligible for awards, but is subject to disciplinary action.

That number of employees there who are viewed as, quote, “not compliant” includes employees who were engaged in installment agreements, who are becoming compliant, but we still count those as noncompliant. We say you will have to be—if you are going to be counted as compliant, you have to actually be current today with your taxes. Even if you are current with an installment agreement, that does not count. But that is not a willful violation.

There have been proposals and suggestions where, if you willfully do not file your taxes with the IRS, not only are you not eligible today for a bonus—and we have a program and we are making sure that that applies as we look at performance awards—but as I say, under section 1203 of the code, if you willfully are in violation of not being compliant, it is grounds for dismissal, and we take disciplinary action against employees.

Over 99 percent of the employees are compliant and they understand. Anybody who signs onto the IRS understands part of their obligation, because we are the tax administrators for the country, part of their obligations individually is to be compliant.

But I would remind everybody we have a lot of GS-4s, GS-5s who are not tax attorneys, tax accountants, or CPAs, and they are capable of making the same mistakes, not willfully, but inadvertently, as everybody else does. We count those people as not compli-



ant, but they are not people who, in fact, are willfully trying to cut corners or not pay their taxes.

So our policy is in place, and it includes issues about other disciplinary actions. We firmly and totally agree that for you to be eligible for a performance award, you should be performing well, and that includes being compliant with your taxes, not willfully avoiding them, and you should not have any major disciplinary action going on at the same time, and that is a new policy.

Senator THUNE. I would just say, whether it is willful or not, voluntary or involuntary, just with absolute clarity, without any ambiguity, make it clear, because, as you know, the agency has a huge trust issue, a huge credibility issue with the American people. It needs to be crystal clear that people within the agency, the IRS employees, are not in any way going to be rewarded either through cash bonuses or time off if they have tax-compliance issues. It just has to be that crystal clear. Otherwise, I do not know how the American people can expect anything less when it comes to that issue.

In your testimony, you cited the recent decline in IRS funding as a cause for poor customer service and insufficient tax enforcement. But there is also in the budget a request, in your 2016 budget, a request for \$490 million and over 2,500 employees, full-time equivalents, to implement and administer Obamacare.

Now, I think it is needless to say that none of these employees would be necessary had Congress not chosen to enact all the mandates and taxes in the law. But is it not time to admit that the increased burden on the IRS is from Obamacare and not simply lower funding?

I mean, we have funding issues, I understand. That is what you are here to talk about. But it strikes me at least that the resource issue is the result of a shift away from customer service and other core IRS functions and toward Obamacare.

Commissioner KOSKINEN. As I have stated from the start of my tenure, it is exactly clear that our responsibilities have grown. It is not only the implementation of the Affordable Care Act. It is the implementation of the Foreign Account Tax Compliance Act. It is about to be the implementation of the ABLE Act and the related Professional Employer Organization responsibilities, where we are being asked to start new programs. All of those are resource-intensive. So it is not—if we did not have any of the statutory mandates we have to implement, we would have more resources available for both enforcement and taxpayer services, obviously.

But I have stated from the start, and I agree with you, that every time there is a new program that is given to the IRS, it does not get done out of whole cloth. It is a mandate that we will pay attention to, but it takes resources away from either enforcement, services, or information technology advancement.

The CHAIRMAN. Senator Heller?

Senator HELLER. Mr. Chairman, thank you.

Commissioner, thank you for being here today and spending time with us.

I want to thank Senator Thune for his questioning. It was one of the issues I wanted to talk about, obviously, the bonuses to the employees.

Mr. Chairman, if I could request that we get a copy of the agency policy on this issue so we can take a look at it, I would appreciate it.

Commissioner KOSKINEN. That is fine. We will be happy to provide that.

Senator HELLER. Also, I would like to mention what National Taxpayer Advocate Nina Olson said in a recent report to Congress. She said, "Taxpayers this year are likely to receive the worst level of taxpayer services since at least 2001 when the IRS implemented its current performance measures."

I guess I want to ask you if this is a fair assessment.

Commissioner KOSKINEN. I am not an expert on what 2001 looked like, but it clearly is going to be a difficult filing season, and the service is going to be if not miserable, abysmal. Whatever it is, it will be a level of service that none of us believes taxpayers deserve.

Senator HELLER. So "miserable" is a word that you guys use quite a bit. That would be a reasonable assessment of what taxpayers can expect.

Commissioner KOSKINEN. Right.

Senator HELLER. You said multiple times during the hearing today that you are doing significantly more with significantly less.

Could you quantify "significantly less"? You have mentioned it several times, but quantify it. Is it 3 percent less, 5 percent less? What are we talking about?

Commissioner KOSKINEN. In terms of our ability to perform?

Senator HELLER. What are you talking about when you say "necessary budget cuts," "significantly less"? What is the dollar amount or percentage we are talking about?

Commissioner KOSKINEN. Of the budget cuts?

Senator HELLER. Yes.

Commissioner KOSKINEN. Since 2010 the budget has been cut by \$1,200,000,000. At the same time, all of the—

Senator HELLER. What percentage is that?

Commissioner KOSKINEN. Pardon?

Senator HELLER. What percentage is that?

Commissioner KOSKINEN. That is—what?—10 percent or 12 percent.

Senator HELLER. Ten or 12 percent. So we would argue that the average taxpayer family also has to do significantly more with significantly less, so perhaps the IRS should also.

Commissioner KOSKINEN. We are doing significantly more with significantly less. As just discussed, we have significant statutory mandates we have been given that we have no choice but to implement. In fact, as I noted, it is ironic that, at the same time in the bill that cut our budget, we were given yet two new programs to set up, start, and initiate.

So it is not a question of our doing the same amount of work with less money; we are doing significantly more work.

Senator HELLER. And I would argue that the average taxpayer is out there doing the same thing.

Commissioner KOSKINEN. Right.

Senator HELLER. The chairman of Ways and Means recently introduced legislation—I believe it is called the Stop Targeting of Po-

litical Beliefs by the IRS Act—that would bar the IRS from changing the guidelines for tax-exempt 401(c)(4) groups until the end of 2017.

I think the IRS, if I am not mistaken, is expected to reissue new rules. Could you be more specific as to when those new rules would come about?

Commissioner KOSKINEN. We do not have a timeline for those. As I have noted, one of the Inspector General's recommendations—about a year and a half ago when he made the report about the use of what were, he termed, improper criteria for identifying organizations applying for tax-exempt status—said that we should review and clarify what the facts and circumstances would be that would determine how much political activity was allowable.

The first proposal put out by the IRS and Treasury before I started managed to sort of aggravate people across the entire spectrum and generated 160,000 comments. We have worked our way very carefully through those comments. I have read over 1,000, 1,200 pages of the most thoughtful and detailed comments. Our goal is to make sure that we end up with a standard that is clear, much clearer than the present standard, fair to everybody—we are looking at which organizations it should apply to—and easy to administer.

To the extent we can, we would like to get out of the determination of political activity one way or the other and have a standard that is clear not only for us, but a standard that is clear for organizations as they are operating. They ought to have a clear, much clearer than facts-and-circumstance standard so they are comfortable that what they are doing is appropriate and that nobody is going to second-guess them and suddenly say they are no longer tax-exempt because they have exceeded vague, hard-to-understand terminology.

But at this point, I cannot give you a deadline.

Senator HELLER. Commissioner, thank you. I want to go back to Nina Olson's recent report. I was disturbed that that report, in assessing the IRS, said that it lacked a clear rationale of resource allocation. Specifically, Ms. Olson said the agency has said that it would not answer complex tax laws on the phone or at walk-in centers. Further, after tax season, employees are being told not to answer any tax law question despite the fact that 15 million taxpayers will have obtained filing exemptions.

I guess the question is, how do you expect taxpayers to adequately comply with the complex tax laws under Obamacare or FATCA since they have no resources to help them implement it?

Commissioner KOSKINEN. It is a significant challenge and one that we are concerned about. My only disagreement with Nina on that is that we have actually carefully looked at how we can provide the best service we can with the resources we have.

And the decision was made last year that if we continued to answer, which we used to do, complicated calls, by definition, the queue would get longer. And so, therefore, we told employees that they needed to answer straightforward questions. For complicated questions, the taxpayer would have to go to our website or elsewhere.

The people who care most about that are our employees. As I wandered around the country last year visiting offices, their question was, "We know the answer, why can we not help?" And the answer I gave them was, if you take longer to answer a complicated call, the number of people in line gets longer, the waiting time gets longer. Trying to minimize the inconvenience to taxpayers as much as we can, we had no choice.

Senator HELLER. Is that significantly more or significantly less from expectations of the taxpayers?

Commissioner KOSKINEN. I think the taxpayers have a right to expect that they can call the IRS, get an answer, get on the phone with an assistor within 2 to 5 minutes, get their questions answered satisfactorily so they can file. That is not something that our resources allow, and all I am saying is, as has been said—

Senator HELLER. It sounds like significantly less.

Commissioner KOSKINEN. It is significantly less.

Senator HELLER. Not significantly more.

Commissioner KOSKINEN. What is happening now is we have significantly less resources, and our service is significantly less—

Senator HELLER. But you just told me you were doing more.

Commissioner KOSKINEN. We are doing more. We are answering more calls than we have answered before with our people. But because of the fact that there are even more calls, the demand is up, the level of service is down, and that is simply because we do not have enough people.

It is not because they are not dedicated. It is not because they do not care. They care substantially about it.

Senator HELLER. And I am not arguing that point.

Commissioner KOSKINEN. Right.

Senator HELLER. Commissioner, thank you.

Mr. Chairman, thank you.

The CHAIRMAN. Thank you. Senator Scott?

Senator SCOTT. Thank you, Mr. Chairman.

Thank you, Commissioner, for being here with us today.

Some of this, of course, started before your tenure. Much has been made about the 3-percent reduction in resources. But at the height of your agency's high staffing levels and robust budgets, your employees started targeting religious, pro-life, and conservative groups, groups in my State, including Tea Party groups, whose members are mostly hardworking, everyday Americans who decided to simply exercise their First Amendment rights.

And in response, in what some have perceived as a coordinated effort between the IRS and liberal groups aimed at targeting these Americans and their groups in an election year, we saw an absolutely chilling effect on certain types of supposedly free speech.

I want you to understand and know that the actions of the IRS hurt my constituents.

My first question is, has the IRS stopped targeting churches and religious organizations with oppressive and intrusive interference with their operations?

Commissioner KOSKINEN. I have said from the start, and I think it is a fair question, that those were mistakes that were made. They should never have been made, and they should not be made again.

And I have said that we are committed to trying to ensure the best we can that taxpayers are confident when they deal with us, wherever they deal with us, that they are going to get treated fairly no matter who they are, no matter what organization they belong to, no matter who they voted for in any election in the past. And we need to be able to do that, because it is critical for the confidence of taxpayers in the fairness of the system.

So I am as troubled as anybody else is by the events that took place in 2010—well, after 2010. The Inspector General, a year and a half ago, almost 2 years ago, revealed that. We have implemented every one of the Inspector General's recommendations to try to do our best to ensure that it never happens again.

One of those recommendations was to try to clarify the standard that is in the regulations now so that people would have a better—externally and internally—would have a better idea of what is permissible, what counts, and what does not count.

Senator SCOTT. I appreciate your answer. Certainly, I am hopeful that we are moving in the right direction, but I hope you understand and appreciate my concern about the issue. I have a letter dated December 22, 2014 from the ACLJ where they represented 41 different conservative groups, and they are still working their way through the process. I think all but five have received their tax-exempt status. Unfortunately, some of those groups were in South Carolina, and it took more than 4½ years to get their tax-exempt status.

One of the questions I have, as well, goes to the IT challenges that you all face at the agency, Commissioner. Congress gives you hundreds of millions of dollars to modernize your IT system: \$290 million this year, \$300 million in 2013 and 2014, \$330 million in 2012, \$260 million in 2011, \$260 million again in 2010, \$230 million in 2009. I can go on and on, but I will not. Your total IT spending is over \$2 billion each and every year, and last year included, as I said, \$300 million in IT spending for the ACA alone.

In your written testimony, you told the committee that the IRS is operating with antiquated systems and still has applications that were running when John F. Kennedy was President. You said your agency still uses the computer programming language COBOL, which was invented, of course, in 1959.

Commissioner, the IRS has been spending nearly \$1 million a day in the last year or two to modernize its IT system, and that is a lot of money. Can you please help me understand how in the world you are still operating with antiquated systems that go back to the Kennedy administration after we have spent over \$2 billion of resources to get it there?

Commissioner KOSKINEN. Our system, all of it was customized and developed in the 1950s and 1960s when there was no off-the-shelf software. As I have frequently referred to it, it is like driving a Model T that now has a great GPS system and a wonderful sound system, has a rebuilt engine. So we have replaced a significant amount of that antiquated system with those expenditures.

But we still have over 50 applications that need to be replaced. But to show what we have been able to do, that refund app, *Where's My Refund?*, got 200 million hits last year. A hundred and fifty million returns are processed; 85 percent of them are now

processed electronically. That was not only not possible, it was inconceivable 15 years ago.

So we have made substantial strides, but the \$300 million on the Affordable Care Act, the \$100 million we are spending on the Foreign Account Tax Compliance Act, are all challenges for us. Fortunately, the filing season this year is going smoothly because all of that has been implemented.

We have 145,000 foreign financial institutions about to provide us data under the Foreign Account Tax Compliance Act. All of those systems had to be built and rebuilt to absorb that data.

If we could continue to get the resources we need, we would get rid of a lot of these systems. Taxpayers would be able to just go online, as they do with Bank of America, Wells Fargo, or Fidelity, and deal with us without paper, without calls. They would be able to do all their transactions easily and efficiently.

We are not talking about, as I said, going to the moon. We are talking about, “Can I catch up with where financial institutions are?” And to do that, we have to keep spending the money.

Senator SCOTT. I certainly would like to—I know my time is up, so I will make this my last question, 53 seconds late.

How much did it cost for that last technological advancement in the “get the refund,” whatever the last thing you said was?

Commissioner KOSKINEN. I do not have the answer to that, but I will get it for you.

Senator SCOTT. My thought is that the new software is relatively cost-effective. I will not call it inexpensive, that might be an overstatement, but it simply does not cost that much to add in new software to create an expedited process. I might be wrong.

Commissioner KOSKINEN. No, no, no. You are exactly right. But part of our problem is, we have data from 150 million returns plus the returns you have had historically. All of that is stored in antiquated systems that we are starting to process and go forward with in what is called CADE 2, for Customer Account Data Engine.

We are trying to build a relational database so all the applications can reach the data rather than having to hunt for the return. Right now we have automated the return as if it was being processed as paper. We need to automate the process so we actually deal with data as it goes forward.

But I would be delighted to chat with you, and our IT people would be more than delighted to explain the roadmap we have trying to get from here to there. But you are right. If we could ever get there—

The CHAIRMAN. Senator, your time is up.

Senator SCOTT. That would be helpful. Thank you, sir.

Commissioner KOSKINEN. Sure.

The CHAIRMAN. Let me just make a couple of comments here at this time which I think are appropriate.

The committee takes the allegations of misconduct by the IRS with respect to applications for tax-exempt status very seriously. Maybe you did not hear that. I will just repeat that. The committee takes the allegations of misconduct by the IRS with respect to the applications for tax-exempt status very seriously.

We have been investigating this matter since May of 2013. Our staff has interviewed over 30 IRS and Treasury officials and re-

viewed over 1 million pages. Last year, Senator Wyden and I were almost ready to ask the committee to release the final report, and, in fact, we had a draft at that time. However, right around that time, we learned that IRS could not produce all e-mails to and from Lois Lerner, a key figure in the investigation, because of what the IRS claimed was a crashed hard drive.

As a result, Senator Wyden and I decided to give the Treasury Inspector General for Tax Administration, TIGTA, time to investigate that particular matter. And I was pleased to recently learn the TIGTA apparently has recovered some or all of the missing e-mails. TIGTA expects they will be able to start providing the recovered e-mails to our investigators as early as 2 weeks from now. As soon as we have reviewed the e-mails, we are hoping to renew the effort to move forward with the report, and at that time members of this committee will have ample opportunity to explore the IRS matter in great detail.

We will have to do this carefully because of the restrictions imposed by section 6103 of the tax code, which generally prohibits the release of taxpayer-specific information. In the interest of efficiency and caution, I urge all members to save their questions on the investigation of IRS tax-exempt organizations, on that matter, until they have had a chance to review the final report.

Senator Wyden, do you have any comments about that?

Senator WYDEN. Just very briefly, Mr. Chairman and colleagues.

This is the only bipartisan inquiry that has been conducted or is being conducted on this issue. So thank you, Chairman Hatch, for your statement. I want to emphasize that we are working very closely to finalize the IRS tax-exempt inquiry.

I personally think it will be more productive and more efficient in terms of our time use to focus on this issue in the context of the upcoming release of our report. I just want to emphasize, as Chairman Hatch did in his statement, that we are working very closely together, and, colleagues, we are committed to making sure that this will be the one bipartisan inquiry on this important topic.

Thank you, Senator Hatch.

The CHAIRMAN. Senator Casey?

Senator CASEY. Mr. Chairman, thanks very much.

Mr. Commissioner, I am grateful to have you here and grateful for your work. You have a very tough job, probably among the toughest in this town.

I want to ask you a couple of questions regarding a letter I sent you about a week ago. But before getting to that, I want to focus a little bit on this budget question, because I am a great believer that if we point out problems in an agency or program and ask for reforms and change and better service, we have to be willing to support the resources to get the IRS there, to get any other agency where they need to go.

I was struck by—and I know we have a long list of examples—but I was struck by what you said on page 3 of your testimony. You said, and I am quoting, under the enforcement cuts category, “We estimate the agency will lose about 1,800 enforcement personnel through attrition through fiscal year 2015 that we are not able to replace.” When you go down that list of cuts and consequences, one of the results of that is middle-class families and very vulnerable

folks out there having to navigate a complex system with little help.

So your challenges in the budget become problems down the road for the middle class and for vulnerable families. So I support your efforts to get the resources you need to be able to do your job. It is not good enough for us to just say, there is a problem and we are not going to help you solve it.

But I want to ask you about the letter I sent a little more than a week ago, last Monday, on the 26th, regarding—and everything has an acronym, as we know, but this is the TFOP, the Tax Forms Outlet Program, where, as many folks know, free tax forms and instruction booklets are sent out.

I know in Pennsylvania—and I do not know if this is true in every State—but in Pennsylvania, we are getting a high, high volume of calls and communication regarding the fact that, because of the budget cuts, the distribution of that material is limited.

One of the most significant parts of this problem for our State is our rural communities. We have literally millions of people who live in rural areas in Pennsylvania. So it is a big issue.

So I would ask you—and some of the questions, obviously, are outlined in the letter I sent—what additional resources or tools or support would allow you to maintain the past year's level of service regarding these forms and instruction booklets?

Commissioner KOSKINEN. It is an important question, and we take it seriously, because people have relied on those forms.

One of the things we are trying to make clear to people—and I had hoped to have an answer to your letter before the hearing, but we will get you the answer before the week is out—is that forms are all downloadable from our website. So everybody has access to the forms through the website.

Now, we recognize there are some people who do not have access to the Internet—

Senator CASEY. That is a problem.

Commissioner KOSKINEN [continuing]. And the challenge for libraries—many of which provide a great service to people because they allow you to, in fact, use their computers—is that they can download those forms, but there is a cost to that. They have to run their printers, and they are running on tight budgets. So we do not underestimate the significance of that problem.

Overall, our concern has been—we try to figure out where to minimize the impacts as much as we can. We have historically sent out large volumes of paper both to libraries and our walk-in sites. As we track them, only about 10 percent or 15 percent of those papers are used.

So we are producing a huge volume of paper that never gets used. We have tried to, therefore, figure out which forms get used so we can produce those. But it is directly a result of trying to avoid shutting the place down, where can we cut costs as much as we can.

So it is only a matter of a few million dollars to be able to produce all that. We have cut back over time, as part of our \$200 million we saved. We used to send every taxpayer a copy of the instructions and the return. Nobody gets those anymore, and we save



about \$60 million a year in printing and mailing costs because of those and other attempts to go forward.

But we are anxious to work with libraries and others—we have no choice, being where we are this year—to try to figure out what the right mix is for them so that they can have copies for people who need them and not burden the libraries with this cost. But that is, in effect, what has happened, to some extent: that cost burden has been shifted to them, and we are concerned about that, but there is not a lot we can do about it at this time.

Senator CASEY. Well, as quickly as you can, get an answer for my letter, because we are getting a lot of calls on this. And one of the problems is—and I know I am out of time—but one of the problems is, the IRS gave an 800 number, and when they call the 800 number, they say we are going to have this problem solved in 4 weeks, 5 weeks, 6 weeks. That is not enough time.

We have something on the order of 20 million people in the country, 14 percent of the total, who do not file electronically. So the faster you can get answers to this and get those forms to people, the better.

Commissioner KOSKINEN. On that point, part of our problem with the production of printed forms, while you can download them today, is that the tax legislation that passed got passed late, so it throws our printing process off, and that is why, by the end of this month, we will, for people who call the 1-800 number, be able to mail them their returns.

But I understand when you call in the middle of January and are told it is the end of February, that seems like forever, and especially if people are trying to file for refunds. But we will have those forms available and printed, back from the printer, before the month is out. But I will get you the answer to that letter this week.

Senator CASEY. Thanks very much. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator.

There is a vote on the floor at noon, but we are going to continue to hold this hearing during the vote. So I would like to make sure all members are able to ask their questions.

Senator Nelson, you are next.

Senator NELSON. Thank you.

Almost \$5 billion a year is going out as a result of criminals using somebody else's Social Security number. You answered, in a previous question, that you hoped to introduce the personal identification number next week for those who request it.

You have a pilot study going on in three jurisdictions: Florida, Georgia, and the District of Columbia. You are doing it in Florida, in large part, because I have raised a ruckus as a result of a lot of these criminals.

Street crime is actually reduced, because they find using a laptop enables them to achieve their goal of stealing people's money by putting in a false tax return, much to the annoyance and heartache of the legitimate taxpayer. And unless the taxpayer can get that PIN, personal identification number, they cannot get the system to operate, because the IRS says, oh, you have already filed a tax return, and they cannot get their legitimate taxpayer return filed and their refund, if they have one due. So I thank you for getting out those PIN numbers next week.

But in those three jurisdictions, you have a pilot study going for a permanent PIN number. And since one of those jurisdictions is my State, I am going to apply for a permanent personal identification number and see how the system is, and I am filing this week legislation to set up a personal, permanent PIN.

Now, the next and most egregious part of this is that a lot of these false tax returns are being filed by inmates in the prisons, in the Federal prison system, as well as the States.

We brought this to the attention of the IRS a couple of years ago. You all implemented and we passed a law that gave you temporary authority so you could then break your confidentiality and share with the prison systems the fact that someone had filed a false tax return and, indeed, it was an inmate. We then followed up that temporary authority with a permanent authority in law 2 years ago, but it has yet to be implemented.

Can you help us, please?

Commissioner KOSKINEN. It is now implemented with the Federal prison system, and so the number of prisoner returns fraudulently filed has dropped significantly. We were down to about 53,000 last year, which is still a lot, but not compared to where it was.

You are exactly right. A lot of this began with prisoners. We have to work memorandums of understanding with State prison authorities, and we are trying get them all to sign up, because it is in their interest as well to find out whether prisoners are actually engaged in illegal action.

And so the statutory support from the Congress was critical to us, and it has already made a big impact. But you are right, we need now to have all the State prison authorities enter into the MOUs with us to go forward.

Senator NELSON. So you have the memorandum in place with regard to the Federal prison system.

Commissioner KOSKINEN. Yes. The Federal prisons, we exchange data with them, and we know what the rolls are like, and we are there. It is really at the State level where we need State authority and State agreements.

Senator NELSON. Then I want to utilize this hearing here today for the word to go out to the respective 51 prison systems that if you want your folks to get mad, just let them know that prisoners are filing false tax returns, cheating the system, getting lots of money back. The State prison systems ought to get on the ball and sign this memorandum of understanding.

I also want to use this hearing to encourage your people to get those MOUs. When a State steps forth and wants an MOU, get it done.

Commissioner KOSKINEN. I would like to correct one thing, just because, as you go online, you will discover that, while we are actively pushing the pilot program in the three States you note, when you get an IP PIN, identity protection PIN, we give it to you for 1 year. It is a permanent process—you are protected—but each year you will get a new PIN, because otherwise we are concerned that the PINs will be stolen.

So what it is is a way of updating every year. So when you get yours—some people I know personally, me, have discovered that it is a very good program.

The reason we have not launched it nationally is simply that we want to see what the burden is on taxpayers, what the cost is for us, and how efficiently it goes. So we hope this year as many people as possible in Florida, Georgia, and the District of Columbia will sign up for IP PINs. It does significantly increase the protection they have against having their refunds stolen or their identity used against them in the Internal Revenue Service.

Senator NELSON. Well, you just had another person sign up—me. Commissioner KOSKINEN. Good.

The CHAIRMAN. Senator, your time has expired.

Senator Roberts?

Senator ROBERTS. Thank you, Mr. Chairman. For nearly 30 years, the IRS did not apply the gift tax to contributions made to charitable organizations of any type. Beginning in 2011, at the same time the IRS began targeting (c)(4) applicants, the IRS began gift-tax audits of individuals who had made contributions to various tax-exempt organizations.

These audits were contrary to congressional policy and legal precedent. When we got wind of this, several members of the Finance Committee, including myself, sent a letter to the agency questioning these audits. The IRS stopped auditing these contributions. But since this is a very complicated area of the law, the IRS said that it would issue administrative guidance to ensure that the IRS audits would not be ramped up again.

It has been about 3 years. We have yet to see any guidance or information. It is important to provide certainty to our citizens that the IRS is not going to select for audit gift tax assessments based on politics.

So my question is, when do you plan to provide guidance on these audits, or would you be in favor of Congress codifying existing IRS policy with respect to application of the gift tax to (c)(4) and other tax-exempt organizations?

Commissioner KOSKINEN. It is in consideration. We are taking a look at it across the board, because it is related to the whole question of the tax-exempt status of organizations across the spectrum.

But in response to your question, anytime Congress would like to legislate in this area would be fine with us. We would be happy to have the IRS making as few decisions as possible in the area of political activity and exemptions and gift taxes related to that.

So if the Congress would like to, on this particular question, create a statute that created whatever policy the Congress thought was appropriate, that would be helpful. But in the meantime, we want to make sure that whatever we do is, as I say, fair to everybody, and is clear and easy for people to understand.

And so it is tied up with the entire question of tax-exempt organizations across the board—

Senator ROBERTS. Well, we will try to be of help to you.

Commissioner KOSKINEN. Good.

Senator ROBERTS. I am sort of fascinated by the amount of money that you feel would be appropriate so you could do a better job. I understand you want \$67 million more. Is that the number?

Commissioner KOSKINEN. Actually, the President's budget for this year would be—our present budget is \$10.9 billion. The President's request is for, in effect, a total of \$12.9 billion; \$12.3 billion through appropriations and about \$600 million through a program integrity cap adjustment.

Senator ROBERTS. You said "fair to everybody." According to Senator Brown and Senator Cardin, I wish they were here, they really want to use the money that you are not receiving now for 9,000—you indicated 9,000 enforcement employees.

Commissioner KOSKINEN. No. Actually it would be—we have lost 5,000 enforcement employees. The actual increase in the budget would allow us to restore employees, not totally because we are down 13,000, headed to 16,000 down, but it would allow us to hire, for instance, 3,000 employees in the service centers answering phone calls, so our level of service would go back to—

Senator ROBERTS. So this is answering phone calls. This is not enforcement employees knocking on doors with regard to audits, so on and so forth.

Commissioner KOSKINEN. No. Some of the 9,000 would be enforcement employees as well. As you say, overall—

Senator ROBERTS. Are you going to just really aim at sophisticated rich people?

Commissioner KOSKINEN. No. We cannot afford to aim.

Senator ROBERTS. I know some rich people who are not sophisticated.

Commissioner KOSKINEN. We cannot afford to aim at any particular segment of the tax-paying population. Everybody paying taxes—most people want to be compliant. So we are anxious to—

Senator ROBERTS. Exactly.

Commissioner KOSKINEN. We divided the world into two kinds of taxpayers. If you are trying to become compliant, we are going to work very hard with you to—

Senator ROBERTS. Well, what I am worried about is, everybody wants to talk middle class and class warfare. And the idea that was promoted by my colleagues was about 9,000 enforcement people who would just really focus on the rich. I do not know who is rich. Who is rich? Is that \$250,000? I mean, is there a number there?

Commissioner KOSKINEN. We do not divide it that way.

Senator ROBERTS. Good. Good. Good.

Commissioner KOSKINEN. We look at the entire spectrum.

Senator ROBERTS. Good. Good. Fine. But rich and sophisticated. In other words, they could hire somebody because they have a myriad of problems, they cannot figure it out, and so this is supposed to be a target.

I just want to let you know there is one Senator who does not agree with that. I appreciate that. And thank you for coming and thank you for trying to get the trains to run on time. That is what you told me when you first came to my office.

Commissioner KOSKINEN. We are still working on it.

Senator ROBERTS. All right. Thank you so much.

Senator GRASSLEY [presiding]. Mr. Commissioner, you have said some good things about the IRS whistleblower program.

Commissioner KOSKINEN. Yes.

Senator GRASSLEY. I am not worried about what you said. I am worried about whether or not your words at the top are getting down. Particularly, I am interested if they heard you at the Office of Chief Counsel.

So what I am going to do on that issue is not ask you to answer questions for me right now, but I would like to raise with you questions and points about that program and submit them for answer in writing and give you an opportunity to give very complete answers.

And I would just ask now for your commitment to provide a complete and thorough response for the record on that issue of whistleblowers.

Commissioner KOSKINEN. I would be delighted to do that.

Senator GRASSLEY. My next issue is EITC and immigration. I would like to have you help me better understand the tax implications of the President's executive action on immigration.

Congress established the EITC program to encourage and reward work. Obviously, since those in the United States who are undocumented are not legally allowed to work, it makes no sense to provide them a subsidy to work.

Current policy reflects this by requiring those claiming the EITC to provide a Social Security number for themselves, their spouse, and any children. However, the IRS Chief Counsel advice issued March of 2000—not now, 2000—suggests that individuals granted deferred action will be able to amend returns for the previous years to claim the EITC for years they worked illegally in the United States once they obtain a Social Security number.

So, Mr. Commissioner, can you confirm that those granted deferred action will be eligible to benefit from the EITC for years in which they were working without papers in the United States once they obtain a Social Security number?

Commissioner KOSKINEN. The way the program works is, those without a Social Security number—and there are thousands who file with ITINs every year—people paying their taxes even though they are not legally here, they are not eligible for the Earned Income Tax Credit program.

Once you get a Social Security number, however, whatever the programs are, then the program allows you to file for Earned Income Tax Credits.

In terms of whether you can do that retroactively, the normal statute of limitations would apply as to when you can apply and file an amended return, in effect.

Underneath all that is the requirement that you have to have filed returns in the past. As I say, there are thousands of people here illegally who have ITINs and regularly pay income taxes. If you did not pay the income taxes, obviously you cannot now file a return and say, I am eligible for something else because I did not file when I was required to file.

Senator GRASSLEY. Now, I am not going to argue with you about what you said, because I think you stated it the way it is. But this is a problem you get into. The IRS's interpretation of the EITC eligibility requirements undermines congressional policy of not awarding those to workers illegally in the United States.

Does the IRS have any intention of revisiting the 2000 Chief Counsel advice in light of the President's executive action on immigration?

Commissioner KOSKINEN. At this point, I am not aware that we are going to do that, but I would be happy to look into that further and get back to you.

Senator GRASSLEY. I am suggesting to you that it should be done, because congressional policy is that you do not reward those who come here undocumented. But with the President taking his action to legalize some people, to get Social Security and the ability to retroactively claim something would undermine the congressional policy. So I would ask you to look at that and respond in writing.

Commissioner KOSKINEN. I would be pleased to do that.

Senator GRASSLEY. My last question will have to be this. I have been investigating charitable hospitals that are suing their low-income patients when they cannot afford to pay for care. As part of the tax-exempt status, charitable hospitals are required to offer a community benefit. Also, the law requires hospitals to have financial assistance policies to help low-income patients afford care.

What is the IRS doing to identify hospitals that are not meeting the requirements to create financial assistance policies, or hospitals that are not following their own policies when it comes to low-income care?

Commissioner KOSKINEN. We take this issue seriously. As you know, we have had additional regulatory guidance for hospitals as to how to meet their requirements, which are required. At this point, we audit tax-exempt organizations on a regular basis. Without sounding the old refrain, obviously, we have fewer people able to do that.

One of our hopes is, by streamlining the application process for small 501(c)(3) organizations, we both make it much easier for them to qualify and give us more efficient use of our resources to audit at the back end.

So we think the points you have been raising are very important ones. These are, in many cases, significant financial institutions that are tax-exempt, to some extent, because they have a requirement to provide community services.

And it is an important area for us to be aware of and for hospitals and those running them to understand what their responsibilities are. And it is our responsibility across the entire tax code to make sure that we undertake enough audits and enforcement activities to reinforce the need for compliance.

Senator GRASSLEY. Senator Portman, you are next.

Senator PORTMAN. Thank you, Mr. Chairman.

Thank you, Commissioner, for being here. I was here for part of your testimony and responses to questions, but you have a tough job. And as you know, I co-chaired the IRS Restructuring and Reform Act process with Senator Kerry now 17 years ago, and we made a lot of progress.

If you look at the increases in the budget during that time, I think they are reflected in the fact that the IRS undertook some reforms that people on this side of the aisle and that side of the aisle thought were appropriate. And I think we are in a situation now where people are looking for a commitment by the IRS to do

a better job on the probably dozen things that have been raised today. I have heard about four or five of them while I have been here. And maybe with that, there is a willingness to provide additional funding.

After that process with the IRS Restructuring and Reform Act, I know that the image of the agency improved. It is a tough agency to love because it is taking away your hard-earned dollars, but the standing of the agency improved because taxpayer service improved.

And I am very concerned with what I hear about this tax filing season. So I think we do have to figure out how to have the IRS run more efficiently. One thing that we always pushed with the IRS Restructuring and Reform Act, long before the Internet was used as extensively as it is now, was more technology.

And one of my concerns has been a specific program that would help in terms of this budget issue that you have talked about today. There was a decision made by your managers that has significantly raised costs for the agency, but also for practitioners, and also for taxpayers. It has resulted, as I understand it, in an additional 370,000 calls being dropped into your practitioner phone queue—and I am referring to the Taxpayer Advocate's report on this recently—your decision to shut down the online e-services disclosure authorization electronic account resolution applications.

This was a service that allowed practitioners to go online and to get the power of attorney, access client information online, and for them it took a matter of hours. Now it is taking 10 to 20 days, on average, which costs everybody more, again, not just the practitioner and the taxpayer, but the IRS.

I would think, with your manpower being stretched and your resources being stretched, that you would not want to make a decision like that that would cost the agency so much and be harmful to taxpayers.

So my question to you is, I guess, is this type of Internet-based solution that the e-services program provided something that you are intending to get back involved with, and are you going to implement it more effectively next time? Why did you shut it down? The IRS has received over \$190 million for business systems modernization in the fiscal year 2014 budget.

Can you make assurances to us today that using available resources, you are going to reestablish those e-services applications, that that would be a priority during this fiscal year?

Commissioner KOSKINEN. I am happy to take a look at it, because I agree with you, as you know. My goal is—and we are trying to get people to understand what the world would look like 3 to 5 years out if we could actually better use technology as we go.

We do not have any flexibility left this year to do almost anything beyond the minimum that we are doing, but I do think this is an important area. We have heard those same concerns.

Our concern is making sure that the program runs efficiently, that the authentication is satisfactory, so it is in fact not available to—we talked earlier about refund fraud and identity thefts.

You have to understand, as you know, we are dealing with criminal syndicates here and around the world now. We have gotten al-

most 2,000 people put in jail. So a lot of the amateurs, the people who used to do it by themselves, are not there.

What we are really dealing with is people who are very sophisticated, have systems more sophisticated than ours. But I can commit to you that we are concerned overall about the practitioners. Our practitioner priority line, as I said, is almost an oxymoron anymore, because it takes so long to get through. And practitioners are critical of us because they often represent more than one taxpayer, and if they have a question we could answer, it would make a whole series of returns more likely to be accurate, and with less work.

So practitioners are really at the highest level of our concern, and whatever we can do to make the system work better for them, we will. But as I say, we are constrained as to what changes at all we can make this year. We talked earlier about how even the production of forms to libraries is a problem for us.

Senator PORTMAN. And the library problem is one we have had back in Ohio. Constituents have come to us and said, "We cannot get the forms we normally could get by going to the public library."

I think there are certain things like the e-services program that are going to save you so much money and hassle over time, and not just for, again, the taxpayer and practitioner, but for your people and for downstream costs.

In terms of identity theft, this is something that I have a strong concern about, and I think you talked about this earlier today with some folks.

Let me give you an example. We get a call from a constituent. It is a woman. She is a mom. She has a child. She has applied for EITC, and she has claimed the child on her EITC filing. She finds out her child has already been claimed by somebody else. So the IRS is telling her, "I am sorry, you are not going to get your EITC even though you are working, even though you meet all the other requirements, because your child has already been claimed."

So we are working through that with your agency. I am not asking you to get involved in that one, because I think we are going to work that out with some of your folks. But the Social Security number apparently got into the wrong hands.

What is the agency doing to combat that kind of identity theft? And what options do we, as legislators, have to help you with that? Because it is a growing problem.

Commissioner KOSKINEN. Well, as I said, if we could get W-2s earlier, that would help deal with some identify theft and fraud, because we will be able to see the returns. Particularly children's Social Security numbers are attractive to criminals because, oftentimes, children are not filing a return, and, if you are not claiming them on the return, they are an easy target. That is why the death files used to be where this all started, because there was nobody filing a return for someone who had died.

We have increasingly sophisticated filters designed to identify where those returns are coming from. We stopped about \$15 billion worth of fraudulent returns from going out last year, but we are still dealing with several billion dollars that got through those filters.



Part of our problem is that, with our famous antiquated system, we have upgraded to the extent we can, but the people filing these returns are not filing one or two. They are filing hundreds of them and then reverse-engineering the process to see what our filters are doing, and then they are end-running them.

And so this year for the first time—it started last year—we can actually update our filters on an ongoing basis rather than once a year, which was where we were 2 or 3 years ago.

Senator Wyden [presiding]. This is a very important issue, but Senator Menendez has been very patient. And since I asked about it earlier today as well, I am interested in working with my colleague.

Senator PORTMAN. Thank you, Mr. Chairman. I appreciate it. Thank you, Commissioner.

Senator WYDEN. Senator Menendez?

Senator MENENDEZ. Thank you, Mr. Chairman.

Thank you, Commissioner. Look, I know the IRS is not the most popular agency in government, and it is politically popular for some to take shots at you and your workers. But at the end of the day, the main purpose of the IRS is to enforce the law and serve the American people. And when we try to punish the IRS, as some do, by cutting their budget, it is the American taxpayer who suffers the collateral damage through reduced service and efficiency.

According to the National Taxpayer Advocate's annual report to Congress, and I will quote from it, "The budget environment in the last 5 years has brought about a devastating erosion of taxpayer service, harming taxpayers individually and collectively." The report goes on to estimate that taxpayers will have to wait at least an average of 30 minutes on hold before they will be able to speak with someone and less than half of those calling in will be able to reach a representative. Less than half.

Like you, I think this is completely unacceptable, not to mention that, for all who work hard and pay their taxes to support our Nation collectively, it really allows those who cheat to get away with it, to some degree, when you do not have the ability to ultimately enforce the law.

So let me ask you, is there any way to reduce wait times and increase customer service by reallocating resources to that critical purpose, and if so, what would be the consequences of reprogramming funding away from other functions?

Commissioner KOSKINEN. We have looked, as I said, at trying to be as even and fairly balanced as we can, because enforcement is a big part of our responsibilities, as is taxpayer service. Part of the limitation of saying, well, let us give up on enforcement and turn everybody to answering the phones is that the people who are revenue agents and officers are not trained to deal with, in fact, call center operations, just as our call center operators are not trained to become revenue agents overnight. Clearly, we could train them over time.

So our judgment has been to kind of lower everything. As I say, we have 5,000 fewer revenue agents, officers, and criminal investigators. At the same time, we have 3,000 fewer people answering the phones, and this year we have 2,000 fewer temporary people available for the phones.

Seventy-five percent of our budget is people, and they are spread across enforcement, operations, taxpayer service, and information technology. So there is no magic hidden pool that we can access that would move some people into taxpayer service and would go unnoticed.

Senator MENENDEZ. So at the end of the day, people who are calling and trying to find out exactly how to abide by the law, get information so that they can be a responsible filer, get delayed, and those who cheat on their taxes, to the detriment of all those who pay, are made less likely to be found out because you have less agents. Is that a fair characterization of what happens?

Commissioner KOSKINEN. That is a fair characterization.

Senator MENENDEZ. Let me turn to another subject that I am very seriously concerned about. That is the Child Tax Credit, its refundable portion, the Additional Child Tax Credit, which is being criticized based on allegations of fraud.

While fraud in any tax program must be addressed, a focus solely on one anti-poverty tax program that is threatening to completely deny an economic lifeline to needy children, in my mind, is not a meaningful solution.

So there is a lot of talk about combating fraud in the Child Tax Credit, particularly among low-income immigrant families, and so I have a couple of questions that hopefully you can answer in short order.

Is fraud in the CTC and ACTC a significant contributor to the \$450 billion tax gap?

Commissioner KOSKINEN. It is not. It is a problem we take seriously, but it is not at the core of the tax gap.

Senator MENENDEZ. By what percent would the gap be narrowed if there was zero fraud in the CTC program?

Commissioner KOSKINEN. It might be narrowed by a percentage.

Senator MENENDEZ. Are unscrupulous tax preparers a significant cause of this fraud?

Commissioner KOSKINEN. We are very concerned about unscrupulous tax preparers. As I would stress, the vast majority do a good job, know what they are doing. A smaller percentage of them mean well, but do not know really a lot of what they are doing. And then there is a percentage who are crooks, and they are the ones who are a major part of the problem of fraud across the board.

Senator MENENDEZ. And do you believe that denying the credit to anyone without a Social Security number is merely fraud prevention or a significant policy change that will deny this important credit to families that are currently eligible today?

Commissioner KOSKINEN. No. Obviously, we would love to move everybody off Social Security numbers and just do an identity protection PIN someday, but at this juncture, the issue of fraud is one that applies to ITINs, it applies to any identifier. People are forever stealing identification information from taxpayers to, in fact, generate fraud.

Senator MENENDEZ. Well, I will close, Mr. Chairman, and say I find it interesting that with \$450 billion in tax avoidance and fraud occurring every year, some colleagues have focused solely on poor children and families, which make up a mere fraction of the overall problem. In fact, businesses underpaid taxes by approximately

\$122 billion in 2006 alone, yet we do not seem to hear the same level of outrage in that regard.

So I am for rooting out the fraud everywhere, but at the end of the day, I am not for denying individuals who legitimately have the right to get the credit who, because of the way that it is being pursued here, would be denied that right, and I think that approach is fundamentally flawed and there has to be a better way.

Thank you.

The CHAIRMAN. Thank you, Senator.

Senator Wyden?

Senator WYDEN. Thank you, Mr. Chairman.

Commissioner, I have one question, but I think you want to correct something for the record in a discussion that you had with Senator Nelson.

Commissioner KOSKINEN. Senator Nelson focused on an important problem, which is our exchange of information with prisons, and I noted we are working on developing MOUs with States, and I stated we had an MOU with the Bureau of Prisons. Actually, we get automatically, as a result of support from the Hill, the information from the Bureau of Prisons about the prisoner rolls, and we are able to, in fact, cut down significantly on prisoner fraud. But we do not actually have an MOU, as such, with the Bureau of Prisons.

Senator WYDEN. I want to talk to you now about what I consider to be a decade's worth of foot-dragging at the agency, and I am using that word very deliberately, because it has just not been possible to get some answers and get this resolved.

As you know, because we have talked about it, there are some hedge funds that masquerade as insurance companies, and then they go to places like Bermuda and the Cayman Islands where they are not taxed and where their earnings are sheltered from U.S. taxes.

Now, the IRS has been onto this for over a decade, since 2003, has issued guidance: we have to scrutinize this. There are many responsible hedge funds that have offered suggestions on how to correct this. Every time I bring it up, you all say it is the Treasury's doing, that they are not getting at it, and Treasury says it is IRS that is not getting at it.

I am going to bulldog this until this is resolved. I think this is outrageous that this has gone on for more than a decade, Commissioner, more than a decade since that guidance. And just to go back and forth between you all and the Treasury as I have is just unacceptable. These are people who are taking advantage of the law-abiding taxpayers we have talked about.

So what is it going to take to get this actually resolved?

Commissioner KOSKINEN. We have actually prepared guidance and are working with Treasury on putting it into final form, to a significant extent as a result of conversations you and I have had over the last few months.

Our people and Treasury's have met with the insurance associations to get their suggestions and ideas on what would work and not work. The concern everybody has is, there are legitimate reinsurance companies that have large reserves because their claims

are episodic. But within that context, we ought to be able to move this forward, and we are committed to doing that.

And as I say, we are working with Treasury to get those regulations out.

Senator WYDEN. So guidance was issued in 2003. When do you think this is actually going to get accomplished? Can you give me a date this morning? Because otherwise it just sounds like more of the same, more of what everybody has talked about since 2003: we are talking to our colleagues, it is going back and forth. Yes, there are legitimate hedge fund companies, we all acknowledge that, and legitimate insurance.

These are people who are ripping taxpayers off. So give me a date when I can expect that this is going to be completed.

Commissioner KOSKINEN. Well, as you know, I do not control that because ultimately regulations come out of both agencies. All I can commit to you is that we are pushing very hard to get this done.

Senator WYDEN. Ninety days? Can I expect this will get done in 90 days?

Commissioner KOSKINEN. Ninety days has a nice ring to it.

Senator WYDEN. Good.

Commissioner KOSKINEN. Let us say we will do our best to get it done in 90 days. It will help to have a deadline out there.

Senator WYDEN. But let us get it done in 90 days, Commissioner. After 10 years, 10 years plus 90 days seems to be enough time.

Thank you, Mr. Chairman.

The CHAIRMAN. Thank you, Senator.

Thank you for your patience here, Mr. Commissioner. We appreciate you, and we appreciate you coming to the committee and being open to all these questions that have been asked of you.

Let me just say a couple of things and ask a couple of questions.

The President has indicated that he would be for corporate or business tax reform. Has anybody in the administration contacted you about how you think that ought to occur? It is a Treasury issue, but have they contacted you or talked to you about it?

Commissioner KOSKINEN. I am not personally aware of any contact about that, but we have, with inversions and all of the issues that are kicking around, an ongoing set of reviews with the Treasury Office of Tax Policy about regulatory advice and development of programs.

So, within that ongoing exchange, we meet every 2 weeks. I am not aware of a specific focus on what the policies would be or the recommendations would be, although my understanding is that in the budget presentation, there were going to be basic principles provided to you as to where they were going.

But as always, tax policy, as I have said, belongs in the domain of Treasury, the White House, and the Congress. We are tax administration. But as such, we are anxious to cooperate with anybody thinking about tax reform, because it has to be administrable.

The CHAIRMAN. That is right. And have they consulted with you about these tax proposals that the President is making in his budget that he filed here yesterday?

Commissioner KOSKINEN. As I say, we do not have communications with the White House on—

The CHAIRMAN. Why not? I mean, it seems to me you would know more about it than they do.

Commissioner KOSKINEN. We do, but ultimately, for all the reasons we have talked about over the last year and a half, we are involved in tax administration. And so in discussions about tax policy, certainly at the very higher level of policy, not the drafting of the statutes, we usually are not consulted and do not reach out to them.

But as you move forward, as I say, whatever the policy is that people are considering, it has to be administered, and it has to be administrable. And so we are very anxious to cooperate with anybody looking at reform or simplification of the code.

The CHAIRMAN. Well, we appreciate you being here today. I want to thank you for appearing here today. I also want to thank all the Senators who participated. It has been a good hearing, in my opinion, and any questions for the record should be submitted no later than Tuesday, February 10th.

So with that, the committee will adjourn until further notice.

Commissioner KOSKINEN. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you. I appreciate you being here.

[Whereupon, at 12:40 p.m., the hearing was concluded.]



## APPENDIX

### ADDITIONAL MATERIAL SUBMITTED FOR THE RECORD

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PREPARED STATEMENT OF HON. ORRIN G. HATCH, A U.S. SENATOR FROM UTAH,  
CHAIRMAN, COMMITTEE ON FINANCE

WASHINGTON—Senate Finance Committee Chairman Orrin Hatch (R-Utah) today delivered the following opening statement at a committee hearing on the President's FY 2016 budget request for the IRS:

The committee welcomes Internal Revenue Service Commissioner John Koskinen, who comes before us today to discuss his agency's budget and operations. We will also be discussing President Obama's fiscal year 2016 budget proposal.

Commissioner Koskinen, this morning's hearing continues a long tradition of the close relationship between the Senate Finance Committee and your agency.

More than 152 years ago, the Finance Committee received a letter from George Boutwell, who President Lincoln had appointed as the first Commissioner of Internal Revenue. The letter came in response to an inquiry from the committee, seeking information about the commissioner's organization, his budget, and the activities of his office.

Does that sound familiar?

In his letter, dated January 21, 1863, Commissioner Boutwell tried to answer the committee's questions, but started by first asking Congress for more money.

Specifically, he wrote, "Before proceeding to estimate the expenses of assessing and collecting the revenue, I desire to express the opinion that an increase in the pay of assessors is very important, if not absolutely necessary."

That part sounds familiar to me.

As you and I continue this historic and important relationship, I hope we can begin the 114th Congress on new footing. The issues before us are too great for that relationship to be anything but open, honest, and productive.

We will certainly disagree a lot—on your agency's implementation of Obamacare, on the application of premium tax credits to federal exchanges, and on IRS spending, just to name a few issues. Sometimes, the relationship will be contentious. Sometimes, it will be congenial. I hope it will be more the latter than the former, but that will depend on you.

When we look at the IRS's operations, there are handful of basic principles the agency must follow in order maintain its good working relationship with this committee. Today, I'm going to talk about three of those principles.

First, the IRS must spend taxpayer dollars wisely.

As the agency that collects taxes from American workers and businesses, your agency will continue to be under especially tough scrutiny when it comes to how it spends the money Congress appropriates. And, unfortunately, the IRS's operations do not appear to be able to withstand such scrutiny.

When you reverse the positions of your predecessors and award bonuses to employees who have not paid their taxes; when your agency throws lavish conferences; and when you spend tens of millions of dollars on public sector union activity, the public loses faith in your ability to spend money wisely.

When your agency pays tens of billions of dollars in improper payments every year; when the IRS mails thousands of fraudulent refund checks to a single home address; and when a quarter of all Earned Income Tax Credit payments are improper, the public loses faith in your ability to protect tax dollars carefully.

Second, the IRS must treat taxpayers fairly and respect their rights.

Recent scandals have given Americans reason to doubt that the IRS will treat them fairly. While the targeting of applicants for tax-exempt status may have happened before your tenure, taxpayers must have confidence that those days are over.

Just before you became Commissioner, the IRS and Treasury Department released a proposed regulation that would limit the ability of social welfare organizations to engage in speech about matters of public importance. After an outcry from all sides of the political spectrum, the proposed regulation was withdrawn.

But, now I hear you plan to reissue it.

This would be a mistake—and I hope you do not go down the path of trying to limit political speech. That would only further entangle your agency in needless political debate and controversy.

Third and finally, the IRS must be open and honest with this committee. We must have mutual trust between us.

I believe you to be an honest man and when you tell me something, I take you at your word. But it's because of this trust that I am concerned about a recent development in the committee's investigation of political targeting at the IRS.

Last July, your agency told the committee that it had completed its production of documents regarding Lois Lerner, the central figure in the investigation. Then, late last month, as the committee worked to finalize its investigative report, your agency delivered 86,000 pages of new documents, including 30,000 pages of new Lois Lerner documents, including new emails. Thirty thousand pages of new documents.

Emails that fill eight boxes, and I have here about a tenth of those. These documents are central and relevant to the committee's investigation, and were given to us without notice or explanation roughly twenty months after we made our initial document request.

This is not the way to build trust with this committee. This prolongs the committee's investigation and raises more questions than it answers.

We will be following up on this matter more after today's hearing.

Commissioner Koskinen, we are here today to discuss your agency's operations and the President's budget proposal. There is much to discuss on these two topics, and I look forward to hearing your testimony and answers.

In your opening remarks, I'd appreciate it if you took the time to address three specific concerns that I have.

First, I'd like to hear what the IRS plans to do to address the consistently high levels of fraud and overpayments for the Earned Income Tax Credit.

Second, I'd like to hear what specific changes you plan to make in the agency's spending habits to deal with the budgetary shortfalls you've publicly decried.

Third, I'd like to hear about any contingency plans you have in place in case the Supreme Court invalidates the current structure of the Affordable Care Act tax subsidies later this year.

I hope that today can mark the beginning of a new chapter in the long, historic relationship between the IRS and the Senate Finance Committee.

I hope it is a good chapter, but, once again, that is ultimately up to you.

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PREPARED STATEMENT OF HON. JOHN A. KOSKINEN,  
COMMISSIONER, INTERNAL REVENUE SERVICE

Chairman Hatch, Ranking Member Wyden, and Members of the Committee, thank you for the opportunity to appear before you today to discuss the IRS's budget and current operations.

After just over a year as IRS Commissioner, it remains an honor for me to lead this great institution. My respect for the agency's role and admiration for its work-



force continue to grow. I'm pleased to report that the 2015 tax filing season opened on schedule on January 20, and is going well so far.

Opening the current filing season on schedule was a major accomplishment, given the challenges we faced. I attribute this achievement to the dedication, commitment and expertise of the IRS workforce. Along with normal filing season preparations, there was a significant amount of extra work to get ready for tax changes relating to the Affordable Care Act (ACA) and the Foreign Account Tax Compliance Act (FATCA). We also had to update our systems to reflect the passage of the tax extender legislation in December.

Even with the demonstrated capacity of our work force to successfully meet these challenges to open filing season on time, I remain deeply concerned that the significant reductions in the IRS budget will degrade the agency's ability to continue to deliver on its mission during filing season and beyond. In fact, one of my highest priorities since becoming Commissioner has been to advise Congress about the ramifications of continued substantial cuts to our funding, and that is what I will focus on in my testimony today.

IRS funding has been reduced \$1.2 billion over the last five years, from \$12.1 billion in Fiscal Year (FY) 2010 to \$10.9 billion in FY 2015. Just over a month ago, the agency's FY 2015 budget was cut by \$346 million from FY 2014, to \$10.9 billion. But the total reduction from last year is actually closer to \$600 million when the \$250 million increase in mandated costs and inflation are counted.

The IRS is now at its lowest level of funding since FY 2008. When inflation is taken into account, the current funding level is comparable to that of 1998. Since then, however, the number of individual and business tax filers has increased by more than 30 million, or 23 percent, along with the number of legislative mandates that the IRS is required to implement.

It is important to point out that prior to this year the IRS was already reducing costs in order to absorb the reductions to our funding that began in FY 2011. This has not been easy because labor costs are by far the largest portion of the IRS budget. In fact, approximately 75 percent of our budget represents staffing, which is critical to providing adequate levels of taxpayer service and maintaining robust compliance programs. Moreover, it is not possible to shift enforcement personnel into service jobs, or vice versa, without providing them with substantial training, which of course is resource-intensive.

Nonetheless, the IRS has for several years been working hard to reduce costs and find efficiencies in our operations. The IRS has implemented significant reductions in its non-labor spending. In an effort to promote more efficient use of the Federal government's real estate assets and to generate savings, the agency in 2012 began a sweeping office space and rent reduction initiative. We estimate that these measures have reduced rent costs by more than \$47 million each year and reduced total IRS office space by more than 1.8 million square feet.

During the last several years, the agency generated annual savings of \$60 million in printing and postage savings by eliminating the printing and mailing of selected tax packages and publications, and by transitioning to paperless employee pay statements.

We will continue our efforts to find savings and efficiencies wherever we can. But as I said in my testimony to the Appropriations Committees almost one year ago, the cuts to the IRS are so significant that efficiencies alone cannot make up the difference. Now, we are at the point of having to make very critical performance trade-offs. There is simply no way around the severity of these budget cuts without taking some difficult steps. We have been attempting to cope by protecting the core operations of the agency, in the belief that we must not hollow out the organization. We must identify the things that absolutely need to get done, and do them well.

Our determination to protect the core operations of the agency has led us to the decision that we need to continue to invest in our workforce. The ability of the IRS to fulfill its mission depends on the experience, skills and dedication of our employees. We need to do everything we can to ensure that every employee has the leadership, systems and training to help us retain good employees, to support them in their work and to allow them to perform at the highest levels, whether they are involved in customer service, compliance programs or information technology (IT) infrastructure and operational support.

As part of this investment in our workforce, the IRS will continue to recognize qualifying employees who do exceptional work. Performance awards are necessary

incentive to motivate the workforce and retain highly qualified employees, and in that regard, I firmly believe they provide the agency and taxpayers with a good return on the dollar. This investment will ensure that highly qualified employees have an incentive to stay with the agency and improve performance. As a result of negotiations with the National Treasury Employees Union (NTEU), the overall pool for awards was reduced to about 1 percent of the bargaining unit (BU) employee salary base, which is significantly less than the 1.75 percent provided to these employees in previous years.

I recently worked with IRS senior leadership to determine how to allocate our limited resources in FY 2015. We reviewed our operations to determine where we could make cuts that would have the smallest possible impact on taxpayers and tax administration. In making these decisions, we strove to maintain a balanced and fair approach, keeping in mind the needs of both service and enforcement, to avoid overly harming one part of our mission in the attempt to maintain another.

Let me now describe for this Committee the difficult decisions we made to absorb the latest round of budget cuts, and the impacts of those decisions. They include:

- **Delays to critical IT investments of more than \$200 million.** We anticipate that these delays will reduce taxpayer service and cost-efficiency efforts as well as reduce outside contractor support for critical IT projects. For example, we will not be replacing aging IT systems, increasing the risk of downtime and negatively affecting taxpayer service. In addition, we will not be able to invest up front money to gain future operational savings, such as moving to a shared cloud infrastructure and reducing data center space.
- **Enforcement cuts of more than \$160 million.** We estimate the agency will lose about 1,800 enforcement personnel through attrition during FY 2015 that we are not able to replace. We anticipate the result will be fewer audits and resources focused on collection. We estimate that as a result of these enforcement cuts the government will lose at least \$2 billion. In addition to the revenue loss, the curtailment of enforcement programs is extremely troublesome because these programs help create a deterrent effect that is the key to preserving high levels of voluntary compliance.
- **Reductions in staffing during filing season totaling more than \$180 million.** Normally, IRS uses employee overtime and temporary staff to provide the extra resources needed during the busy filing season. However, IRS will be reducing overtime and seasonal staff hours during FY 2015. We anticipate that these cuts will result in delays in refunds for some taxpayers. People who file paper tax returns could wait an extra week—or possibly longer—to see their refund. Taxpayers with errors or questions on their returns that require additional manual review will also face delays in getting their refunds. It is also expected that the taxpayers will have to wait longer to get an answer to their questions from the IRS. In addition to responses to written correspondence taking longer, taxpayers will have more difficulty getting through to the IRS on the phone and in person. We anticipate that about 50 percent of callers will be able to get through to an assistant and as we get further into the filing season, the telephone level of service will continue to deteriorate, dropping below 50 percent. This means that for every person who tries to reach IRS by phone, only half will end up getting through. That is significantly below the FY 2014 average of 64 percent, which was itself below desired levels. The 50 percent who reach the IRS will face extended wait times that are unacceptable to all of us.
- **Continuing the agency hiring freeze.** The IRS is extending the exception-only hiring freeze begun by the IRS in FY 2011 through FY 2015. As a result, and assuming normal attrition rates, the IRS expects to lose approximately 3,000 additional full-time employees in FY 2015. That would bring the total reduction in full-time staffing since FY 2010 to over 16,000. The resulting reduction in staffing will have negative impacts on taxpayer service and enforcement as noted above.

Even with all of these reductions, the IRS still faces a significant budget shortfall for FY 2015. So at this time, the agency is contingency planning for the possibility of a shutdown of IRS operations for two days later this fiscal year, which will involve furloughing employees on those days. If this does become necessary, our goal will be to minimize disruption to taxpayers, employees and our operations. We will continue to do the best we can to avoid taking this drastic action. In fact, these dates will be very late in the fiscal year to give the agency time to do everything

possible to avoid a shutdown and, if one is necessary, to do it at a time that causes as little disruption as possible.

The concerns I have about the IRS's funding level relate not only to the negative impact these cuts have on the present operations of the agency, but also the impact on our ability to advance the agency into the future and provide a more up-to-date and efficient tax filing process for the taxpaying public.

To the extent possible within our budget constraints, the IRS has already made some significant improvements in its technology to better serve taxpayers. For example, one of the most popular features on IRS.gov is the *Where's My Refund?* electronic tracking tool, which reduces phone traffic IRS receives regarding questions about refunds. Another good example is IRS Direct Pay, which provides taxpayers with a secure, free, quick and easy online option for making tax payments, reducing the need for IRS to process payments by check. Still another example is Get Transcript, a secure online system that allows taxpayers to view and print a record of their IRS account in a matter of minutes, saving taxpayers time and reducing IRS resources needed to process paper requests for transcripts.

In looking to the future, we believe that it is not an option to stay at our current level of funding, given the extent to which both taxpayer service and enforcement will suffer as a result. It is very troubling to me that these cuts prevent us from fully improving and modernizing our IT infrastructure and operations support. This hurts taxpayers and the entire tax community.

Earlier in this testimony I described some examples of IT projects that must be deferred as a result of budget reductions in FY 2015. But the problem is much broader. We are operating with antiquated systems that are increasingly at risk, as we continue to fall behind in upgrading both hardware infrastructure and software. Despite more than a decade of upgrades to the agency's core business systems, we still have very old technology running alongside our more modern systems. This compromises the stability and reliability of our information systems, and leaves us open to more system failures and potential security breaches.

In regard to software, we still have applications that were running when John F. Kennedy was President. And we continue to use COBOL programming language. COBOL was considered outdated back when I served as chairman of the President's Council on Year 2000 Conversion and it is extremely difficult to find IT experts who are versed in this language. I give our IT employees a tremendous amount of credit as keeping things going in the face of these challenges is really a major accomplishment.

It is important to point out that the IRS is the world's largest financial accounting institution, and that is a tremendously risky operation to run with outdated equipment and applications. Our situation is analogous to driving a Model T automobile that has satellite radio and the latest GPS system. Even with all the bells and whistles, it is still a Model T. Our core IT systems are not sustainable without significant further investment over the next few years.

The President's 2016 Budget provides \$12.3 billion in base discretionary resources, an increase of \$1.3 billion from FY 2015 to make strategic investments in the IRS to continue modernizing our systems, improve service to taxpayers, and reduce the deficit through more effective enforcement and administration of tax laws. The Budget also proposes a \$667 million cap adjustment to support program integrity efforts aimed at restoring enforcement of current tax laws to acceptable levels and to help reduce the tax gap. This multi-year effort is expected to generate \$60 billion in additional revenue over the next ten years at a cost of \$19 billion, thereby reducing the deficit by \$41 billion. In addition, there are several important legislative proposals in the President's FY 2016 Budget related to tax administration. Specifically, let me highlight the following proposals:

- **Acceleration of information return filing due dates.** Under current law, most information returns, including Forms 1099 and 1098, must be filed with the IRS by February 28 of the year following the year for which the information is being reported, while Form W-2 must be filed with the Social Security Administration (SSA) by the last day of February. The due date for filing information returns with the IRS or SSA is generally extended until March 31 if the returns are filed electronically. The Budget proposal would require these information returns to be filed earlier, which would assist the IRS in identifying fraudulent returns and reduce refund fraud, including refund fraud related to identity theft.

- **Provide correctable error authority.** The IRS has authority in limited circumstances to identify certain computation or other irregularities on returns and automatically adjust the return for a taxpayer, colloquially known as “math error authority.” At various times, Congress has expanded this limited authority on a case-by-case basis to cover specific, newly enacted tax code amendments. The IRS would be able to significantly improve tax administration—including reducing improper payments and cutting down on the need for costly audits—if Congress were to enact the Budget proposal to replace the existing specific grants of this authority with more general authority covering computation errors and incorrect use of IRS tables. Congress could also help in this regard by creating a new category of “correctable errors,” allowing the IRS to fix errors in several specific situations, such as when a taxpayer’s information does not match the data in certain government databases.
- **Authority to regulate return preparers.** In the wake of court decisions striking down the IRS’s authority to regulate unenrolled and unlicensed paid tax return preparers, Congress should enact the Budget proposal to provide the agency with explicit authority to regulate all paid preparers. The regulation of all paid preparers, in conjunction with diligent enforcement, would help promote high quality services from tax return preparers, improve voluntary compliance, and foster taxpayer confidence in the fairness of the tax system.
- **Streamlined critical pay.** The IRS Restructuring and Reform Act of 1998 increased the IRS’s ability to recruit and retain a handful of key executive-level staff by providing the agency with streamlined critical pay authority. This allowed the IRS, with the approval of the Treasury Secretary, to hire well-qualified individuals to fill positions deemed critical to the agency’s success, and that required expertise of an extremely high level in an administrative, technical or professional field. This authority expired at the end of FY 2013. The President’s budget request proposes renewing this authority, which is essential to ensuring that the IRS has needed expertise in a number of important areas, including IT—in particular, cyber security—as well as international tax compliance and operational support.
- **Simplify large partnership audits.** Auditing of large partnerships has become a very challenging area for the IRS, in part because the number and complexity of partnerships has grown significantly over the last several years, and also because of inefficiencies in the partnership audit rules contained in the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA). The procedures set up under TEFRA were designed to improve tax administration by making it possible for the IRS to conduct audits at the partnership level, instead of auditing each individual partner. But TEFRA was enacted when partnerships generally were smaller than they are today, and before they had complicated tiered structures. Therefore, having to follow the TEFRA procedures is now more of a burden for the agency than a help. Congress could ease this situation by enacting the Budget proposal to streamline audit procedures for large partnerships.

Chairman Hatch, Ranking Member Wyden, and Members of the Committee, thank you again for the opportunity to discuss the IRS budget and current operations. Given the impacts we are already seeing on our ability to deliver on our mission, I believe it is vital that we find a solution to our budget problem, so that the IRS can be put on a path to a more stable and predictable level of funding. I look forward to working with Congress to do just that. This concludes my statement, and I would be happy to take your questions.

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QUESTIONS SUBMITTED FOR THE RECORD TO HON. JOHN A. KOSKINEN

QUESTIONS SUBMITTED BY HON. ORRIN G. HATCH

DISCRETIONARY FUNDING

*Question.* This year, your agency has almost \$800 in resources outside of appropriations, including nearly \$400 million in user fees alone. Can you give the Committee better insight into the decision-making process at IRS, and how the agency prioritizes its discretionary funding between taxpayer services, enforcement, employee bonus awards, and other spending?

*Answer.* The IRS senior leadership uses a deliberate decision making process to determine priorities based on the hierarchy of statutory, regulatory, and Department/Service-directed requirements. The Service then allocates available appro-

priated resources against those requirements. We then determine the unfunded mission critical requirements and identify what additional resources are available from other sources, such as user fees, and allocate those resources against the Service-wide requirement.

#### PROCUREMENT AND SPENDING PRACTICES

*Question.* Reviews by the Treasury Inspector General for Tax Administration (TIGTA) found the IRS is ineffectively managing its software licenses by failing to adhere to industry best practices and failing to maintain agency-wide policies or procedures.<sup>1</sup> As a result, the IRS may have wasted between \$81 and \$114 million on unused software licenses and annual license maintenance. Further, the IRS may have over-deployed licenses valued between \$24 and \$29 million, and it has not been able to account for whether these licenses were ever used.

How much is the IRS currently spending on software asset management?

*Answer.* The IRS estimates expenditures of approximately \$16.7 million on software asset management, including contractor support, software operations and maintenance, infrastructure support, and IRS labor to support its software asset management capability. While there are various software asset management processes, capabilities, and tools in place to support asset management for desktops/laptops, servers, and mainframe computers, some of the tools and associated processes are not yet fully integrated and institutionalized. We would like to reach an industry standard level of asset management known as Information Technology Infrastructure Library (ITIL) Level III capability. The IRS has chartered an Enterprise Software Governance Board (ESGB) to provide guidance and oversight in the development of software asset management processes, specific support centers for development of internal audit processes for software licenses, development of software asset management tool(s) requirements for an integrated asset management capability, and overall governance processes.

*Question.* In light of TIGTA's findings, why should spending levels be increased?

*Answer.* The IRS's 2016 infrastructure initiative requires investment in three elements: people, processes, and technology. Although TIGTA's estimates of underutilized software spending and over-deployed software are dramatically higher than the IRS's estimates, the IRS does agree with TIGTA that there are significant benefits to be realized with an enterprise-wide software asset management capability that meets more mature ITIL and industry best-practice standards. In the future and after a resource review, the IRS can build on existing processes, capabilities, and tools to deliver an enhanced software asset management structure, enterprise-wide inventory, and software license management tools that are in line with TIGTA's recommendations. While there are some capabilities and tools currently in place, funding for this enterprise-wide effort has been significantly reduced due to budget reductions in FY 2014 and FY 2015. Without additional resources, we continue to cobble together the existing discovery tools, harvested data from various repositories, spreadsheets, and direct contact calls to manage our software assets. While the IRS has realized some significant savings following our existing processes, there is room to improve to rise to the level of industry standards and obtain the associated results.

Within the FY 2016 President's request the IRS could backfill key positions that have been vacated due to natural attrition and retirements and to bring in external industry experts to begin to implement the recommendations made by TIGTA and the ESGB. Those resources would be used as appropriate to optimize existing software agreements as well as to implement the processes and procedures necessary to manage an overall effort at an enterprise level. The IRS believes there is a large upside potential for savings if appropriate staffing and funding can be allocated to this effort.

*Question.* What structural reforms has the IRS implemented to improve software asset management and avoid irresponsible and wasteful spending of taxpayer money in this area?

*Answer.* The IRS has chartered the ESGB, which is a collaborative effort with key stakeholders from all functional areas of IT that are overseeing the implementation of new processes and procedures for Software Asset Management. The ESGB is bringing together all ongoing software asset management capabilities at the IRS,

<sup>1</sup>Treasury Inspector Gen. for Tax Admin., Additional Consideration of Prior Conduct and Performance Issues is Needed When Hiring Former Employees (Dec. 30, 2014), 2015-10-006.

such as the Infrastructure Currency (N/N-1) effort. The IRS enterprise system software is on average 3 releases behind industry standards, and in some cases it is 4 or more releases behind. Our goal is to have software remain current (N) or one version from current (N-1). The N/N-1 team recently used Lean Six Sigma methodologies to assess and develop a plan that leverages existing software asset management capabilities and tools to ensure all installed versions of commercial off-the-shelf software remain N or N-1. This effort identified many opportunities to improve software management processes to gain efficiencies and quantifiable results.

The roles and responsibilities of the ESGB also include selection of an enterprise tool(s) for software asset management, implementation of internal audit procedures for software agreements, and implementation of software asset management policies and governance.

There is good momentum on the ESGB with the right level of executive leadership at meetings to move forward on this effort. However, continued lack of funding to build out an enterprise management structure and implement the policies, processes, and tools will jeopardize the effort.

*Question.* How much investment is needed to accomplish this goal?

*Answer.* The investment requested in the President's FY2016 budget to sustain IRS's Critical IT infrastructure includes resources that will allow the IRS to restore mainframes, servers, laptops, network devices and communications equipment to keep the IT infrastructure (hardware and software) current for existing and newly developed IT systems. This includes updating and replacing infrastructure components that are no longer operating reliably or need additional capability that is not available through an upgrade; that are being retired because of non-support; and that are unable to support the latest release of software, growth of current application demand or meet the latest federal security configuration standards. This also includes movement toward the goal of having software at N or N-1. These funds will also enable IRS to hire 157 qualified FTE, and contract for external subject matter experts, to build out its planned integrated capability for software asset management and to operate and maintain infrastructure components.

#### HIRING PRACTICES

*Question.* A TIGTA review found that between January 1, 2010 and September 30, 2013, the IRS hired 824 employees who had "substantial employment issues" during previous employment with the IRS.<sup>2</sup>

For fiscal year 2013 and 2014, how much did the IRS pay these 824 employees in salary and benefits?

*Answer.* The IRS is following up with TIGTA to identify the methodology used to enumerate 824 employees in the report, to ascertain the identities of the employees, and to coordinate the response to this question about how much the IRS paid these employees in salary and benefits for fiscal year 2013 and 2014.

*Question.* According to TIGTA, "The IRS stated that, during the process of evaluating qualifications of applicants, prior IRS conduct and performance issues do not play a significant role in deciding the candidates who are best qualified for hiring." Is this an accurate statement of IRS policy? If it is, why does the IRS believe that these factors are not relevant when rehiring former employees?

*Answer.* The IRS considers prior conduct and performance issues before hiring or rehiring employees, and believes it has sufficient legal basis to consider past conduct and performance at any time during the hiring process.

*Question.* Although the IRS revamped its hiring process in 2012, TIGTA believes that "the IRS needs to reassess its current process to more fully consider prior conduct and performance issues before rehiring employees." Does the IRS have sufficient legal basis to implement this recommendation? If not, what changes to the law are necessary to allow the IRS to more fully consider prior employment and performance issues when rehiring employees?

*Answer.* Yes. The IRS believes it has sufficient legal basis to consider prior conduct and performance issues at any time during the hiring process, and it currently does so.

<sup>2</sup>Treasury Inspector Gen. for Tax Admin., Additional Consideration of Prior Conduct and Performance Issues is Needed When Hiring Former Employees (Dec. 30, 2014), 2015-10-006.

## EXEMPT SECTOR ENFORCEMENT

*Question.* The IRS's fiscal year 2015 budget request provides funding for expanded criminal investigation capabilities and addresses compliance issues in the tax-exempt sector, including exempt organizations. In 2014, TIGTA found that the IRS had improperly disclosed confidential taxpayer information, which is protected under the Internal Revenue Code, in 21% of surveyed Freedom of Information Act (FOIA) and Privacy Act requests. Unauthorized disclosure occurred in 16.4% of surveyed requests in the previous year's audit.

Describe the extent to which IRS employees suspected of tax code violations, including the unauthorized disclosure of Section 6103 information, were appropriately investigated. How will these sorts of investigations change based on the IRS's fiscal year 2015 budget request?

*Answer.* The IRS takes violations of section 6103 very seriously. Any and all IRS employees suspected of tax code violations, including the unauthorized disclosure of section 6103 information, are investigated to determine if a violation of the tax code occurred, and if so, an appropriate level of discipline. Managers are responsible for ensuring employees understand their obligations and do not improperly disclose taxpayer information. When improper disclosures are identified, managers are required to report those incidents to TIGTA and follow IRS incident-management procedures. TIGTA makes a determination to investigate based on the egregiousness of the incident and will, as appropriate, take action to pursue criminal charges. Non-criminal disclosures of taxpayer information, records, or taxpayer-privacy violations are adjudicated in accordance with the IRS Guide for Penalty Determinations and result in discipline ranging from a written reprimand to removal.

The improper disclosures of confidential information noted in the most recent TIGTA annual review of FOIA compliance were determined to be inadvertent disclosures, not negligent or reckless. The findings report included an acknowledgment by TIGTA that the 13 occurrences of unauthorized disclosure found in their review were inadvertent and all were properly reported as unauthorized disclosures as required. TIGTA did not make a separate finding in this area because training was previously done to educate the staff in the errors noted and TIGTA included an acknowledgement in its report that all employees received that training.

In fiscal year 2014, 129 employees were found to be in violation of section 6103 disclosure and security rules. Despite the changes in the IRS fiscal year 2015 budget request, the IRS will continue to investigate any and all employees suspected of tax code violations.

## RECORDS MAINTENANCE AND PROCESSING

*Question.* From fiscal year 2009 to 2012, the IRS consistently reduced its backlog of FOIA requests. Yet, in fiscal 2013, there was an 84% increase in the number of backlogged FOIA requests at the IRS.<sup>3</sup> Halfway through fiscal year 2014, the FOIA backlog increased an additional 16%. In over 11% of surveyed requests, the IRS over-withheld information to which requesters were legally entitled because of improper redactions or inadequate search methods.

As a percentage of its budget, how much has the IRS spent annually on FOIA and Privacy Act request processing since fiscal year 2013? If the share of spending is decreasing, which programs received additional budget allocations that would have otherwise been allocated for the processing of records requests?

*Answer.* The IRS does not separately track costs related to FOIA and Privacy Act request processing.

*Question.* What is the IRS's spending plan to improve statistics concerning improper redactions or withholdings on FOIA and Privacy Act records? What does the IRS foresee as the cost for properly training FOIA and Privacy Act officers to avoid improper practices with respect to records processing? Why have prior training efforts or investments failed to remedy what appears to be an ongoing, if not worsening, problem?

*Answer.* The IRS processes thousands of Freedom of Information Act (FOIA) requests each year that require labor intensive searches of paper and electronic files. Many requests involve hundreds, and some involve millions, of pages of responsive documents. Additionally, because of the advent of the electronic age combined with

<sup>3</sup>Treasury Inspector Gen. for Tax Admin., Fiscal Year 2014 Statutory Review of Compliance with the Freedom of Information Act (Sept. 17, 2014).

the increasing complexity of the tax law, the number, volume and complexity of FOIA requests have significantly increased. First quarter FY 2015, FOIA receipts are 25% higher than the same period in 2014, and our complex inventory has increased over the last fiscal year by 53%. Therefore, the IRS is pursuing a technology solution to improve our ability to process, search and, when needed, redact necessary information in responsive documents. An automated solution is necessary to address the increased volume of electronic records and improve our ability to provide all responsive documents and reduce errors. Any potential automated solution, however, will still require human intervention and oversight to ensure accuracy and avoid inadvertent and inappropriate disclosures.

The IRS agrees that training is critical to ensure the effectiveness and efficiency of the FOIA program. The IRS allocated \$74,000 for the training of FOIA and Privacy Act officers in fiscal year 2015. In addition, to improve records processing we are holding a series of low-cost, high-impact virtual technical updates to address emerging case processing issues and questions.

The IRS has always offered intensive, face-to-face technical training specifically for Disclosure employees, as well as Disclosure Awareness sessions to all IRS employees. Challenges remain because of significant attrition in our FOIA professional ranks. The current level of funding does not address the needs resulting from increased FOIA volume and complexity and years of attrition. A hiring freeze prevents replacement of staff due to attrition throughout the IRS, in order to meet restrictive funding cuts over the last several years. Hiring authority alone is not an immediate solution, however, due to the time, attention and oversight necessary to bring replacement staff up to the expert level required to properly process complex FOIA and Privacy Act inquiries.

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QUESTIONS SUBMITTED BY HON. ROB PORTMAN

CONTRACTOR PERFORMANCE

*Question.* Mr. Commissioner, a lot of the discussion today has focused on how the IRS spends the money that it is allocated, so let me continue on that theme and ask about how your agency measures contract performance. As you know, last month the Department of Health and Human Services' inspector general found that CMS did not always meet contracting requirements when hiring outside contractors to help create the healthcare.gov website. This ended up with the government spending \$800 million to build what we all found out was ultimately a very flawed product.

Among other things, the report found that:

- CMS failed to appoint anyone to coordinate the efforts of the 33 contractors who helped develop the healthcare.gov website;
- Only two of the six key contracts underwent CMS Contract Review Board Oversight prior to award;
- CMS did not conduct thorough reviews of past contractor performance; and
- CMS chose a contract type that placed the risk of cost overruns solely on the U.S. government.

Looking at the IRS's current list of contracts, it appears that the agency has awarded over \$150 million in contracts with outside groups to administer the Affordable Care Act alone, and over \$800 million in overall IT contracts.

Given these past problems in other areas of the government, particularly when implementing the ACA, what can you tell us about the IRS's contracting process?

*Answer.* The IRS IT contracting process uses best practices in acquisition management and uses a six-phase strategic sourcing model. Each of the phases provides critical planning, execution, and control of the overall contracting process, and is integral to the success of the IT contract and contractor performance. The phases include the following.

**Requirements Planning** involves the process of identifying which business needs can be best met by procuring products or services outside the organization. This process involves determining whether to procure, how to procure, what to procure, how much to procure, and when to procure. This phase includes defining the procurement requirement, conducting market research, and developing preliminary budgets and cost estimates.



**Solicitation Planning** involves the process of preparing the documents needed to support the solicitation. This process involves documenting program requirements and identifying potential sources. This phase includes selecting appropriate contract type, determining procurement method, and determining proposal evaluation criteria, and contract award strategy.

**Solicitation** is the process of obtaining information (bids and proposals) from the prospective sellers on how project needs can be met. This phase of the contracting process includes conducting a pre-proposal conference (if required), conducting advertising of the procurement opportunity, or providing notice to interested suppliers, and developing and maintaining a qualified bidder's list.

**Source Selection** is the process of receiving bids or proposals and applying the proposal evaluation criteria to select a supplier. The source selection process includes the contract negotiations between the buyer and the seller in attempting to come to agreement on all aspects of the contract, to include cost, schedule, performance, terms and conditions, and anything else related to the contracted effort. This source selection process includes applying evaluation criteria to management, cost, and technical proposals; negotiating with suppliers; and executing the contract award strategy. At this point, IRS obtains independent cost estimates to assist in evaluating supplier proposals and conducting a price realism analysis on each supplier proposal.

**Contract Administration** is the process of ensuring that each party's performance meets the contractual requirements. The contract administration process includes conducting a pre-performance conference, monitoring and controlling risk, managing the contract change control process, measuring and reporting the contractor's performance (cost, schedule, performance), and conducting project milestone reviews.

**Contract Closeout** is the process of verifying that all administrative matters are concluded on a contract that is otherwise physically complete. The contract closeout process includes processing property dispositions, conducting final acceptance of products or services, processing final contractor payments, documenting the contractor's performance, and conducting a post-project audit.

*Question.* Does anyone coordinate actions between the contractors?

*Answer.* Shortly after the Affordable Care Act (ACA) legislation was enacted, the IRS Information Technology (IT) organization established the ACA IT Program Management Office (PMO), which serves as the primary integration point for the multiple ACA releases of functionality and coordinates the work completed by contractors supporting IT in developing and testing software applications related to the ACA. All contractors supporting the IRS IT organization in software development, including those supporting the ACA software development efforts, must follow the established IT processes, procedures, and controls that govern how software applications are built, tested, integrated, and deployed. Program governance and controls are in place to guide and manage the IT ACA software delivery, including a program governance board with frequent program reporting using dashboards and status reports that report task status, progress, performance, risks, and issues. The IRS has an established Enterprise Life Cycle (ELC), which is a foundational and repeatable set of controls for software development, testing, and deployment. IRS IT contractors are required to adhere to these IT controls.

*Question.* Does the IRS have a Contract Review Board?

*Answer.* Within the IRS, Contract Review Boards are established in accordance with the Department of Treasury Acquisition Procedures (DTAP) 1004.7203, and governed by IRS policy.

*Question.* What goes in to reviewing prior contractor performance?

*Answer.* In accordance with the Federal Acquisition Regulation, the IRS reviews contractor performance both prior to awarding new contracts and before the IRS exercises options to continue performance. Reviewing contractor qualifications is governed by FAR Part 9, Contractor Qualifications, which prescribes, among other things, policies, standards, and procedures pertaining to prospective contractors' responsibility; debarment, suspension, and ineligibility; and organizational conflicts of interest. In making the determination of responsibility, the contracting officer is required to consider information in the Federal Awardee Performance and Integrity Information System (FAPIIS), including information that is linked to FAPIIS such as from the System for Award Management (SAM) Exclusions, the Past Performance Information Retrieval System (PPIRS), and any other relevant past perform-

ance information. The contracting officer is required to consider all information in PPIRS and other past performance information when making a responsibility determination, and is required to document the contract file to indicate how the information in PPIRS was considered in any responsibility determination, as well as the action that was taken as a result of the information.

Additionally, past performance can be evaluated as part of a technical evaluation. The contractor is required to provide information on their past performance with their offer; this information is reviewed and evaluated as part of an acquisition, as appropriate. The information contained in PPIRS is governed by FAR Subpart 42.15, Contractor Performance Information, which requires past performance information regarding a contractor's actions under previously awarded contracts, including the contractor's record of—

- (1) Conforming to requirements and to standards of good workmanship;
- (2) Forecasting and controlling costs;
- (3) Adherence to schedules, including the administrative aspects of performance;
- (4) Reasonable and cooperative behavior and commitment to customer satisfaction;
- (5) Reporting into databases, as necessary;
- (6) Integrity and business ethics; and
- (7) Business-like concern for the interest of the customer.

#### COUNTRY-BY-COUNTRY REPORTING

*Question.* Mr. Commissioner, we have heard concerns from the business community about the potential effects of country-by-country reporting requirements that may come from the OECD's Base Erosion and Profit Shifting (BEPS) project. Essentially, companies would be required to provide their complete financial information to tax authorities in each country where they do business. Do you have concerns about these reporting requirements from an administrative perspective?

*Answer.* Country-by-country reporting will require multi-national enterprises (MNEs) to report annually and for each tax jurisdiction in which they do business the following: revenue, profit before income tax, income tax paid and accrued, total employment, capital, retained earnings, employees, tangible assets, and the business activity in which each entity within the group engages. The requirement only applies to MNEs with annual consolidated group revenue of at least 750 million euros (equating to approximately 1 billion dollars at the time the threshold was established). This standard will exclude approximately 85 to 90 percent of MNE groups (and approximately 93 percent of US companies) from the filing requirement, while still covering MNE groups that control approximately 90 percent of corporate revenues. We are working with the OECD and G20 to ensure that the concerns and burdens of businesses and tax administrations are kept in mind as guidelines are developed regarding these reporting requirements.

This reporting will require the IRS to build systems to obtain, transmit, store and analyze the data; develop new forms and a legal framework to obtain and exchange the information; determine how to best use the information; and train and deploy appropriate personnel. In a time of significant budgetary constraints and diminished human capital and technology resources, these tasks, as well as meaningful evaluation and use of the information, will be difficult.

#### IRS VOLUNTARY RETURN PREPARER REGULATORY PROGRAM

*Question.* Following the Internal Revenue Service's loss last year in the *Loving* case, the IRS announced a new "voluntary" certification program under which tax return preparers who take a comprehension examination and complete 18 hours of continuing education each year would receive a Record of Completion and be listed in a publicly available IRS database showing return preparer qualifications. There are several aspects of this "voluntary" program that concern me:

*a.* Doesn't this new "voluntary" program of continuing education and knowledge assessment include the same components that the court in *Loving* ruled the IRS lacked statutory authority to implement?

*Answer.* No. The court in *Loving* found the IRS to be without statutory authority to mandate competency testing and continuing education. The court did not preclude voluntary continuing education efforts. The IRS's Annual Filing Season Program established in Rev. Proc. 2014-42 is a voluntary program focused on preparer education. It does not provide for competency testing.

*b.* Despite the “voluntary” label, won’t many return preparers actually feel compelled to enter the new program? Do you acknowledge that return preparers who do not get the official IRS listing could be placed at a competitive disadvantage, particularly since after 2015 they would lose the ability to represent their clients in administrative proceedings with the IRS regarding the returns they have prepared? Since the IRS lacks the authority to require return preparers to undergo continuing education and knowledge assessment, doesn’t it also lack the authority to coerce them into doing so?

Answer. Revenue Procedure 2014–42 establishes the Annual Filing Season Program as permitted under authority described in sections 7803 and 7805 of the Internal Revenue Code. The Annual Filing Season Program will aid in the administration of the provisions of Title 26 of the United States Code by enhancing return preparer competency, which will assist in increasing the accuracy of tax returns prepared by those preparers.

The goal of the Annual Filing Season Program is to encourage tax return preparers to improve their knowledge of federal tax law and return preparation. Approximately 12% of unenrolled tax return preparers have taken advantage of the opportunity to participate in the program and to obtain the Annual Filing Season Program Record of Completion. This participation rate does not suggest that unenrolled preparers have felt pressured into participating in the program. Moreover, as recognized by the district court in *AICPA v. IRS*, 2014 U.S. Dist. LEXIS 157723 (D.C. 2014) competitive pressure or economic considerations do not transform an otherwise voluntary decision into a coerced one.

With regard to whether Annual Filing Season Program participants who are listed in the Directory of Federal Tax Return Preparers with Credentials and Select Qualifications (the “Directory”) will have a competitive advantage over unenrolled tax return preparers who do not participate, many factors may contribute to competitive advantage. Inclusion in the Directory may be a factor, as well as market forces, individual preferences, cost of tax preparation services, overall experience and training of the tax return preparer, proximity of the tax return preparer to the taxpayer, or reputation in the community. It is difficult, if not impossible to determine which factor is the most important influencer for any taxpayer.

*Question.* Preparers who undergo the IRS program’s continuing education and testing will receive a “Record of Completion” and be listed in a publicly available IRS database.

*a.* Isn’t there a risk that this IRS imprimatur could be used by unscrupulous return preparers to lure unsuspecting clients?

Answer. The goal of the IRS in offering the Annual Filing Season Program Record of Completion is to encourage tax return preparers to remain current with federal tax law requirements. Obtaining a Record of Completion for the 2015 Annual Filing Season Program generally requires return preparers to have completed 11 hours of continuing education during 2014 (8 hours for those exempt from the refresher course), including 2 hours of ethics or professional responsibility. To obtain a Record of Completion for the 2016 Annual Filing Season Program generally requires return preparers to have completed 18 hours of continuing education during 2015 (15 hours for those exempt from the refresher course), including 2 hours of ethics of professional responsibility. The purpose of the Directory is to identify tax return preparers with active Preparer Tax Identification Numbers (PTINs) and a credential or some education that may qualify them to prepare a tax return and to assist taxpayers in choosing a preparer by listing credentials and qualifications. Making this information available will raise taxpayer awareness of the various kinds of tax professionals that offer tax preparation services.

*b.* Won’t the IRS designation of certain tax return preparers as having obtained a Record of Completion create significant consumer confusion? The official IRS listing of these preparers will suggest to consumers that unlisted PTIN holders lack the authority to prepare returns—which is flatly incorrect. The official listing will also create the false impression among consumers that returns from listed return preparers are more likely to go unchallenged by the IRS. Does the IRS have any plan to address the inevitable marketplace confusion?

Answer. To address concerns about potential confusion, the IRS in partnership with tax professional organizations launched a major campaign this filing season to help taxpayers choose tax return preparers wisely and help taxpayers understand the different categories of tax return preparers.

The education campaign was launched with a press release and a new web page, [irs.gov/chooseataxpro](http://irs.gov/chooseataxpro). The web page includes the following information:

- Which tax preparer is right for me? Explaining enrolled agents, CPAs, attorneys, and others.
- Do some tax return preparers belong to professional organizations?
- IRS tips for choosing a tax preparer.

When the IRS launched the new online Directory of Federal Tax Return Preparers With Credentials and Select Qualifications (the "Directory") on February 5, 2015, the message was reiterated to choose a tax return preparer wisely and understand the different types of return preparers.

IRS communications state clearly that anyone with a Preparer Tax Identification Number may prepare returns for compensation.

#### PREPARER TAX IDENTIFICATION NUMBERS (PTINs)

*Question.* To date, how much has the IRS collected from the mandatory fee (now \$64.25 for the first year and \$63 for renewals) for issuance of preparer tax identification numbers (PTINs)? Can you provide this committee a detailed accounting of how the IRS has spent those funds?

*Answer.* The IRS portion of the fee for new and renewed PTINs is \$50. The vendor charges \$14.25 for new applications and \$13.00 for renewals and remits the \$50 to a Treasury account designated for the Return Preparer Office (RPO) of the IRS.

All funds collected by RPO are by law required to be spent by the RPO and cannot be spent elsewhere or for any other purpose. The attached spreadsheet entitled "Return Preparer Office PTIN Collections, Expenses, and Available Cash" provides a breakdown of RPO receipts (i.e., user fees of \$50 for each new and renewed PTIN) and expenditures from fiscal year 2011 through January 31, 2015.

*Question.* Last year, the U.S. Court of Appeals for the District of Columbia ruled (*Loving v. IRS*) that the IRS exceeded its statutory authority in seeking to regulate tax return preparers. As a result of the court's decision, the IRS may no longer impose testing or continuing education requirements on tax return preparers. The *Loving* case did not preclude the IRS from requiring return preparers to have and use preparer taxpayer identification numbers ("PTINs") and to pay annual fees to renew their PTINs.

It is my understanding that return preparers filed suit against the IRS in September alleging that the PTIN registration fees are not authorized by law and, in any case, are excessive because they exceed the costs of issuing PTINs (as distinct from costs of maintaining the education and testing programs struck down in *Loving*). Do the annual PTIN fees in fact exceed the costs of issuing PTINs? If yes, how has the IRS used the excess funds? What authority does the IRS rely on for collecting these excess funds?

*Answer.* The IRS does not collect excess funds. The PTIN registration and renewal fees comply with the user fee requirements outlined in OMB Circular A-25. Under the OMB Circular, unless OMB provides an exception, the IRS like all government agencies must calculate a user fee to recover the full costs of services provided. Because the IRS cannot predict the exact number of PTIN registrations and renewals to be received in any given year the PTIN user fee was calculated recognizing that PTIN collections may exceed operating expenses in some years, while operating expenses may exceed PTIN collections in other years. As recognized by the district court in *Buckley v. U.S.*, 2013 U.S. Dist. LEXIS 184758 (N.D. Ga 2013) ". . . a government agency such as the IRS may permissibly spread its cost over multiple years." Additionally, the IRS is required and the PTIN registration fee complies with the rules for user fees in OMB Circular A-25. Because the IRS cannot predict the exact number of PTIN registrations we will receive, PTIN collections may exceed operating expenses, or operating expenses may exceed PTIN collections in any given year. The IRS is required to collect and maintain sufficient funds to:

- Fully fund fiscal years in which operating expenses exceed collections.
- Fully fund 25% of operating expenses for the subsequent fiscal year. At the end of each fiscal year sufficient amounts must be maintained to fund 25% of the anticipated operating expenses for the first quarter of the coming year.

The spreadsheet attached shows the funds maintained to fulfill these requirements.

Return Preparer Office PTIN Annual Changes to Cash

	FY 2011 Actual	FY 2012 Actual	FY 2013 Actual	FY 2014 Actual	FY 2014 Actual	FY 2011— FY 2014 Total	FY 2015		FY 2011— FY 2015 TOTAL
							Actual*	Projected**	
<b>Annual User Fee Collections</b>									
PTIN Collections	\$36,963,246	\$37,030,952	\$35,726,028	\$35,666,618	\$35,666,618	\$145,386,844	\$33,910,806	\$2,145,715	\$181,443,365
<b>Annual User Fee Operating Expenses</b>									
Salaries & Benefits	\$2,783,805	\$11,985,267	\$14,483,602	\$13,000,832	\$13,000,832	\$42,253,505	\$3,542,008	\$6,924,655	\$52,720,168
Contract Support	\$14,216,601	\$16,203,046	\$30,832,950	\$7,853,735	\$7,853,735	\$69,106,332	\$1,818,086	\$14,784,790	\$85,709,208
Misc Expenses—e.g., Travel, Printing, Supplies, etc	\$690,142	\$635,521	\$241,507	\$241,920	\$241,920	\$1,809,090	\$64,080	\$330,920	\$2,204,090
Salaries, Contracts, etc Expenses Total	\$17,690,548	\$28,823,834	\$45,558,060	\$21,096,487	\$21,096,487	\$113,168,928	\$5,424,174	\$22,040,365	\$140,633,466
PTIN Collections Less Expenses (Annual Increase (Decrease) to Available Cash)	\$19,272,698	\$8,207,119	\$9,832,032	\$14,570,132	\$14,570,132	\$32,217,916	\$27,464,538	\$8,591,983	\$40,809,899

\* As of 1/31/2015

\*\* From 2/1/15 through 9/30/15

## IRS EFFORTS TO ADDRESS PROBLEM RETURN PREPARERS

*Question.* Does the IRS have compliance or enforcement strategies in place to track returns by PTIN? If yes, what data has the IRS collected on PTIN holders since it first implemented the PTIN program at the end of 2010?

*Answer.* The current PTIN requirement gives the IRS an important and better line of sight into the return preparer community than ever before. With only a few years of data available, compliance efforts are still in their infancy, but PTINs allow the IRS to collect more accurate data on who is preparing returns, the volume and types of returns being prepared and the qualifications of those doing return preparation. Thus, the information obtained through the PTIN process helps us do more to analyze trends and spot anomalies, so that we have a much better understanding of the return preparer community as a whole, and can design more appropriate compliance and educational activities in response to the data we collect.

*Question.* In a September 2014 report, the Treasury Inspector General for Tax Administration found that almost half the complaints filed by taxpayers regarding return preparers hadn't been reviewed by the IRS. Of 8,534 complaints reported to the IRS between Oct. 2012 and Sept. 2013, 83 percent had no work done on them or were still being processed. 3,953 complaints, or 47 percent, had not had any work initiated whatsoever and no case processor reviewing the complaint. Of those, 1,920, or 49 percent, had been in the IRS's inventory for at least 60 days without any work being started.

In light of these findings, what steps has the IRS taken to ensure that it will promptly and effectively review taxpayer complaints about return preparers?

*Answer.* Having no baseline for the volume of complaints to be anticipated at the start of the Complaint Referral Program in December 2011, complaint volume quickly outpaced available resources to manage the workload. Prior to the start of TIGTA's review, the IRS had identified that a significant number of complaints had not been reviewed. Subsequently, the IRS eliminated all backlogged complaints by December 31, 2014, by focusing efforts on improving processes, by securing additional resources to address the backlogged complaints, and by conducting a dedicated effort to prioritize, evaluate, and resolve these complaints.

New investments proposed in the FY 2016 budget should help prevent future backlogs. In the Budget, the IRS requested an additional \$14.3 million to help ensure ethical standards of conduct of practitioners, including hiring more staff to handle complaints.

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 QUESTIONS SUBMITTED BY HON. CHUCK GRASSLEY

*Question.* As I mentioned at your hearing, I appreciate kind words you have given concerning the IRS whistleblower program and look forward to hearing back from you related to the issues I lay out below.

First, the payments to whistleblowers have slowed to a trickle at best. This is whistleblowers waiting for payment where dollars have been collected and the hold-up is with the IRS processing and checking the boxes for a payment. Often it is the whistleblower office waiting for someone in the field, or in senior management to move paper. I ask that that your office review all whistleblower cases pending payment and bring the Drano to unclog the holdup.

Second, I again find myself frustrated with an IRS Chief Counsel office that seems to wake up every day seeking ways to undermine the whistleblower program both in the courts and the awards. I am especially concerned that chief counsel is throwing every argument it can think of against whistleblowers in tax court. It appears at times that the Chief Counsel's office thinks its job is to come up with hyper-technical arguments and seek to deny awards to whistleblowers who have risked their lives to uncover big time tax cheats. I ask that your office and the director of the whistleblower office review the chief counsel's wasteful and harmful litigation positions that undermine the whistleblower program and go directly against your support for the whistleblower program.

Third, with tight budgets at the IRS it is all the more imperative that the IRS works with whistleblowers and their counsels on cases. The IRS criminal investigators have had great success using whistleblowers to go after banks and terrorist organizations, but the IRS civil division still hasn't gotten the message of working with whistleblowers. I note that the IRS hasn't been shy about paying outside law firms big money to help it in big examinations, yet ignores the possibility of har-

nessing whistleblowers and their lawyers who won't cost the IRS a dime from its budget.

Commissioner, I appreciate your willingness to provide detailed written response addressing these three points.

Answer. I have discussed with the Director of the Whistleblower Office the pace of award payments under section 7623, and have verified that he has made timely processing of claims for which an award is payable a top priority. Awards cannot be paid until the relevant taxpayer audit or investigation is completed (including any appeals), proceeds are collected, and the statute of limitations for filing a refund claim has expired. When those preconditions are met, the Whistleblower Office moves as quickly as possible to notify the whistleblower of a proposed award, obtain comments on the proposal, and make an award decision. To date, the Whistleblower Office has paid 12 awards under section 7623(b). The Director estimates that six to twelve additional 7623(b) awards will be paid in FY 15.

With respect to your second point, the IRS Office of Chief Counsel is responsible for defending the determinations of the IRS in the U.S. Tax Court, including those of the Whistleblower Office. The Office of Chief Counsel coordinates with the Whistleblower Office in defending its determinations before the Tax Court to ensure that Chief Counsel's litigating positions are consistent with the program's goals as well as the statutory and regulatory framework. In most cases before the Tax Court, the record of the case is sealed to protect both whistleblower and taxpayer interests. As a result, I cannot comment on specific arguments made in defending particular Whistleblower Office determinations that are subject to an order of the Tax Court sealing the record. The positions taken by the Office of Chief Counsel support the IRS's administration of the law.

The suggestion that the IRS can do more to work with whistleblowers and their counsel is one that the IRS takes seriously. In a memorandum dated August 20, 2014, the IRS's Deputy Commissioner of Services and Enforcement reinforced previous guidance on the importance of thorough debriefing of whistleblowers during the evaluation of their submissions. After the IRS begins an investigation based on whistleblower information, section 6103 provides limited authority to interact with a whistleblower since disclosure of taxpayer information would be necessary to gather additional information while pursuing the audit or investigation.

*Question.* During the hearing, I asked you about the ability of individuals receiving deferred action to amend tax returns and claim the earned income tax credit (EITC) as a result of the President's executive action. Your answer essentially confirmed that this is the case, but in doing so you also suggested that those receiving deferred action would have had to of already filed tax return for the year in question. However, a page on IRS's website titled "Claiming EITC for Prior Tax Years" would appear to suggest even if one failed to file a tax return in a previous year, they may now file a return for that year and claim the EITC.<sup>4</sup> Could you please clarify your remarks and address whether someone receiving deferred actually must have previously filed a tax return during the year in question to claim the EITC retroactively? Also, please verify, whether or if, the IRS intends to revisit the March 2000 IRS Chief Counsel Advice concerning the ability of individuals to amend their tax returns to claim the EITC once obtaining a Social Security Number.

Answer. To clarify my earlier comments on EITC, not only can an individual amend a prior year return to claim EITC, but an individual who did not file a prior year return may file a return and claim EITC (subject to refund limitations under section 6511 of the Internal Revenue Code). I would note that filing new returns for prior years would likely be difficult, since filers would have to reconstruct earnings and other records for years when they were not able to work on the books.

Section 32 of the Internal Revenue Code requires an SSN on the return, but a taxpayer claiming the EITC is not required to have an SSN before the close of the year for which the EITC is claimed. At your request, the IRS has reviewed the relevant statutes and legislative history, and we believe that the 2000 Chief Counsel Advice (CCA) on this issue is correct.

*Question.* The Affordable Care Act created tax credits that can go directly to your insurance company to pay for coverage. If the credits were more than a person was

<sup>4</sup>Internal Revenue Service, "Claiming EITC for Previous Tax Years." Available at: <http://www.irs.gov/Credits-&-Deductions/Individuals/Earned-Income-Tax-Credit/Claiming-EITC-Prior-Years>.

supposed to get, they were supposed to pay that back to the IRS at the end of the year. Last month the IRS decided that it would waive some of these overpayments.

How much money do you estimate this decision will cost?

Answer. Notice 2015–9 provides limited penalty relief for certain taxpayers who received excess advance payments of the premium tax credit through Affordable Insurance Exchanges (also known as Marketplaces). It provides relief only for the failure to pay penalty and the estimated tax payment penalty. Notice 2015–9 does not provide relief from the underlying tax liability or the associated interest related to excess advance payments. Because the Notice likely only affects a small number of taxpayers, and because it provides relief for modest penalty amounts, it is not estimated that the Notice will have significant fiscal impact.

*Question.* Will you report back to me after tax season has ended, to give me the exact amount of money the IRS waived?

Answer. As noted above, Notice 2015–9 does not provide relief from the underlying tax liability or the associated interest related to excess advance payments received through the Marketplaces. Rather, it provides relief only for the failure to pay penalty and the estimated tax payment penalty. Moreover the notice applies only for the 2014 tax year and is only available for taxpayers who are otherwise compliant with their filing and payment obligations.

Because the penalties to be abated under Notice 2015–9 are expected to affect a small number of taxpayers, in small amounts per taxpayer, it was decided to provide taxpayers seeking relief under the notice with a simple method of seeking relief. Taxpayers seeking relief from the penalty under section 6651(a)(2) for failure to pay were instructed to send a letter stating they are eligible for relief because they received excess advance payment of the premium tax credit; taxpayers seeking relief from the penalty under section 6654(a) for failure to pay estimated tax were instructed to file Form 2210, *Underpayment of Estimated Tax by Individuals, Estates and Trusts*, with a statement that they are eligible for relief because they received excess advance payment of the premium tax credit. Because of the simplified method provided to obtain relief, it is not administratively feasible to obtain precise data on the penalty amounts waived.

*Question.* How will the IRS determine whether people actually need a waiver, or just don't want to pay what they owe?

Answer. As noted above, Notice 2015-9 does not provide relief from the underlying tax liability or the associated interest related to excess advance payments received through the Marketplaces. Rather, it provides relief only for the failure to pay penalty and the estimated tax payment penalty. The eligibility requirements and the specific procedures by which a taxpayer can request penalty relief are outlined in Notice 2015–9. Generally, eligible taxpayers must complete existing IRS Form 2210 to seek relief from the estimated tax payment penalty and must assert, in response to IRS correspondence, that they are eligible for relief from the failure to pay penalty.

*Question.* I asked you about nonprofit hospitals and whether the IRS is doing enough to ensure they are complying with requirements, particularly financial assistance policy requirements in the ACA. Please describe the IRS's efforts to audit hospitals for financial assistance policy requirements in FY 2014 and FY 2015, and any planned activity the IRS intends to conduct in this area going forward.

Answer. The IRS reviews, at least once every three years, the Community Benefit Activities (CBA) of tax-exempt hospital organizations (estimated at more than 3,100 hospital organizations, many with multiple facilities) to which Internal Revenue Code (IRC) section 501(r) applies. Under IRC section 501(r), the IRS began conducting CBA reviews in March 2011 and has completed the first cycle of reviews of hospital organizations. In FY 2014, the IRS started the second cycle of reviews of hospital organizations and conducted 1,033 reviews during FY 2014. By February 20, 2015, the IRS had conducted 406 reviews. A total of 32,201 IRS labor hours have been spent conducting these reviews since they began.

The general requirements of the Financial Assistance Policy (FAP) have been effective for tax years beginning after March 23, 2010. On December 29, 2014, the IRS issued final regulations under section 501(r) that are effective for taxable years beginning after December 29, 2015. A comparative analysis of hospitals that have been reviewed twice since reviews began in 2011 shows the hospitals with an FAP have increased by 6.8% (1,362 to 1,466). In addition, the following observations have been noted from the hospital reviews:



1. 97.13% (1,390) of tax-exempt hospitals are using the Federal Poverty Guidelines (FPG) to determine the eligibility for **free care**.
2. 95.0% (1,312) are using the FPG to determine the eligibility for **discounted care**.
3. A comparison between first and second review responses to facility level questions (regarding eligibility criterion, FPG, and the basis of calculating amounts charged to patients, etc.) shows a significant increase, on average 25.4%, in positive responses. This may imply hospitals are providing more details in the FAP or a more complete FAP since the first reviews were conducted.
4. To date, 17 hospital organizations (for 49 tax years) have been referred for audit of non-ACA issues, including unrelated business income (UBI) tax, lack of profit motive, net operating losses (NOL), etc. None was referred for non-compliance with FAP requirements. Twenty-four of these examinations have been closed, with six resulting in change due to various issues including compensation adjustment, UBI, NOL adjustment, and FICA adjustment.

As the regulatory requirements become effective, the Exempt Organizations Examination office will expand the audits of organizations that have failed to meet the statutory provisions outlined in section 501(r)(1) including the assertion of the section 4959 excise tax associated with a failure under section 501(r)(3), Community Health Needs Assessment (CHNA). Training materials are being prepared for employees to enforce the final provisions of the section 501(r) regulations.

*Question.* Commissioner, in an email you sent to IRS employees you referenced the need to make tough choices given budget constraints and suggested employee furloughs may have to be implemented. Before you take such actions, I hope that you consider cutting back on the number of hours dedicated by IRS employees to union work while on the taxpayer dime, which reportedly topped 500,000 for fiscal year (FY) 2013. If the budget constraints are as dire as you contend, existing resources must be used efficiently and effectively as they can. IRS agents performing union work, when they could instead be assisting taxpayers, is certainly not the most efficient use of resources. What, if any, changes have you taken or do you plan to take to reduce hours spent on union time or "official time" given current budget constraints? Additionally, please provide me with the number of hours IRS employees dedicated to union work in FY 2014 and, as well the number of hours so far spent on union work in FY2015. Additionally, please include the number of IRS agents who have dedicated 50% or more of their working hours to union activities.

*Answer.* Congress found collective bargaining to be in the public interest and through 5 U.S.C. Chapter 71 required a grant of official time in many circumstances and binding collective bargaining in others. Because official time is mandated by statute and by collective bargaining agreements, IRS management does not have unilateral authority to control the amount of official time used. In addition, employees performing representational duties on official time are often able to resolve issues at early stages. Therefore, official time is an efficient use of resources particularly given the strain of overwork under which the current workforce is operating. Even so, the IRS and National Treasury Employees Union (NTEU) recently completed a round of negotiations through which IRS secured a new collective bargaining unit agreement designed to further reduce official time use over the next three years. The new agreement is expected to go into effect on October 1, 2015. These changes are expected to include:

- Establishing benchmarks for reducing per capita official time;
- Reducing the number of face-to-face formal meetings by combining multiple meetings into one and disseminating more information electronically;
- Reducing travel time and the number of full time stewards; and
- Creating an IRS-NTEU committee to implement official time mitigation strategies.

These newly agreed upon strategies supplement previously agreed measures, including: placing limits on the amount of official time that non-full time stewards may use in a year; incentivizing NTEU to better manage official time usage; and establishing official time coordinators, who can address any potential under-reporting of official time with NTEU.

There were 491,948 official time hours during Fiscal Year (FY) 2014 and 113,294 hours in the first quarter of FY 2015. Since 2011, the amount of official time hours has been cut by 16.7 percent. In FY 2014, there were 36 revenue agents that dedicated 50% or more of their working hours to union activities; in the first quarter of FY 2015, there were 37.

## QUESTIONS SUBMITTED BY HON. PAT ROBERTS

## TAX DELINQUENT IRS PERSONNEL—BONUSES AND REHIRING

*Question.* Mr. Koskinen, following up on your statements concerning Internal Revenue Service policy on IRS personnel who are delinquent in their federal income taxes, you state in your testimony that

Those who are not compliant include those who are making installment payments who are working toward compliance, *but it is clear—and it's clear to our employees—that if you willfully do not pay your taxes, not only are you not eligible anymore for an award, you're subject to disciplinary action including, in cases, severance from the service.* And we do that on a regular basis. So I am confident that performance awards are only going to go to those who are eligible for them.

Please provide the latest available information concerning the number of current IRS personnel who have been identified as delinquent in paying federal income tax and former IRS personnel who have been separated from employment with your agency, for the Fiscal Years 2010–2014 based on your stated policy concerning willful failure to pay taxes.

Answer.

## IRS Personnel Who Have Been Identified for Being Delinquent in Paying Federal Income Tax \*

FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
881	1,151	1,236	1,135	1,034

\*Includes employees who have been admonished, suspended, counseled, received last chance agreements for employment, and whose cases were closed without action. The numbers include current and former personnel.

## Former IRS Employees Who Have Separated, Been Removed, Retired Pending Action, or Resigned Pending Action for Delinquency in Paying Federal Income Tax

FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
23	31	38	27	36

The IRS conducts tax checks on all employees twice a year to ensure continued tax compliance. For the purposes of IRS employee tax compliance, delinquencies refer to a failure by the employee to timely file or pay any required tax returns. An employee is considered delinquent regardless of whether a balance is due or the return was subsequently filed, and covers delinquencies that were the result of both willful and non-willful intent. Section 1203(b) of the IRS Reform and Restructuring Act of 1998 requires the removal of employees found to have willfully failed to file any tax return or understated their Federal tax liability.

*Question.* Can you please also provide to me the full Internal Revenue Service policy on the provision of bonuses or other awards, including performance awards and promotions under I.R.C. Section 1203, for employees who are identified as delinquent in their federal income taxes, together with your current definition of “delinquent” for purposes of this policy?

Answer. The IRS has implemented measures to ensure that any IRS employee who violates section 1203(b) of the IRS Restructuring and Reform Act of 1998 is ineligible for a performance award. Attached is the IRS Bonus and Awards Recognition Program Policy applicable to all employee misconduct and tax compliance issues, excluding executives and other high-level officials. Also attached are two memos explaining the impact of disciplinary actions on performance-based pay adjustments, bonuses and awards for members of the Senior Executive Service and other high-level officials at the IRS.

No IRS employee will be eligible for a discretionary award or performance award (to include bilingual awards, and discretionary salary increases such as Quality Step Increases (QSIs) or manager performance-based increases) if a final agency decision is made that the employee violated section 1203(b), such as by the late filing of, or underreporting income on, a federal tax return. The ineligibility determination will apply to the fiscal year in which the final agency decision is made.

The IRS definition of “delinquent” when addressing employee tax noncompliance is the failure to timely pay his or her tax liability or balance due by April 15 of the year the return is due without incurring interest or penalties. Failure to timely pay, while not a potential section 1203(b) violation, is serious misconduct and subject to discipline up to and including termination of employment.

*Question.* Later in response to questions, you state

There have been proposals and suggestions if you willfully do not file your taxes—not—in the IRS not only are you not eligible today for a bonus—and we have a program that we are making sure that that applies as we look at performance awards—but, as I say, under section 1203 of the code, it’s grounds—if you willfully are in violation of not being compliant it’s grounds for dismissal. And we take disciplinary action against employees.

This statement is very concerning given information we have recently received from the Treasury Inspector General for Tax Administration (Report 2015–10–06) on the rehiring of former IRS personnel with prior disciplinary issues. In this report, TIGTA says that between January 2010 and September 2013, IRS has rehired hundreds of former employees with disciplinary issues associated with their prior IRS service. This includes well over a hundred employees with prior tax issues, including willful failure to file federal tax returns. In an understatement, TIGTA says this presents increased risk to the IRS. I think that this entirely unacceptable practice.

Can you assure the committee that if you are able to hire the additional 9,000 new personnel as you have requested in your Fiscal Year 2016 budget submission that none of these prospective personnel will be currently delinquent in paying their federal income tax liabilities?

*Answer.* The IRS is committed to ensuring all new hires, including the new employees referenced in the FY 2016 budget submission, are tax compliant at the time of hiring.

The IRS applies the Office of Personnel Management’s Suitability Processing and Handbook, 5 C.F.R. 731.103(d), to its hiring process. In addition to meeting government wide suitability standards, all IRS candidates must have filed all required tax returns during the prior three years, and either have paid or be current on all taxes due as a condition for receiving a final offer of employment.

The IRS maintains the most rigorous employee tax compliance program in the federal government. Though they may have had prior tax issues, all former employees included in the TIGTA study were determined to be tax compliant at the time of re-hire. This is verified during the suitability phase of the hiring process, prior to the employee being offered a position. Additionally, the IRS conducts tax checks on all employees twice a year to ensure continued tax compliance.

Historically, IRS employees have had very high tax compliance rates as compared to federal employees generally, including the civilian and military workforce. The IRS employee tax delinquency rate is less than one percent, compared with a rate of almost 9 percent among the general U.S. population.

#### Tax Delinquency Rates

Federal civilian	3.99 percent
Military active duty	1.41 percent
IRS employees, including full-time, part-time and seasonal	0.96 percent

Source: Federal Employee/Retiree Delinquency Initiative (FERDI) Annual Report, September 30, 2014.

#### FISCAL YEAR TAXPAYER SERVICES REQUEST

*Question.* While the IRS has had its overall budget reduced in recent years, so has virtually every other department and agency of the federal government. Notwithstanding this, the budget authority for the taxpayer services account has remained largely static since Fiscal Year 2009.

## Taxpayer Services (enacted except for FY16)

(dollars in millions)

FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16
2,293	2,279	2,293	2,240	2,136	2,157	2,157	2,409

Not including transfers and additional funding through (\$13 million in FY13; \$34 proposed FY14), the taxpayer services account has been reduced only about \$136 million from its most recent peak, and certainly not to the point where threats of service reductions are appropriate. Given that taxpayer services funding is close to its historic level, can you tell me what the appropriate funding level is for those services? Do you anticipate any additional transfers to the taxpayer services account, either from other accounts or from special programs?

Answer. The appropriate funding level for Taxpayer Services is \$2.409 billion as requested in the FY 2016 Congressional Justification. This level of funding would allow us to deliver an 80% level of service to meet taxpayer demand and continue delivering high-quality services to the taxpaying public. The IRS further anticipates augmenting Taxpayer Services funding with \$55 million in user fee collections in both FY 2015 and FY 2016.

While Taxpayer Services funding has been reduced to a lesser extent than other accounts, it is important to note that costs have risen over the same time period. Since FY 2011, the IRS has had nearly \$100 million in unfunded requests to maintain current levels (MCLs) of effort due to inflation in the Taxpayer Services appropriation, exacerbating the impact of the nominal \$136 million reduction since FY 2011. In FY 2016 alone, for example, MCLs are expected to be over \$53 million. As a result, full-time equivalent staffing in Taxpayer Services will decline over 9% (almost 3,000 FTE) from FY 2011 to FY 2015. At the same time, over 6 million new individual filers have entered the tax system, an increase of 4.6%.

Additionally, Taxpayer Services functions require corresponding funds in the Operations Support account which funds information technology, security, rent payments, and other administrative support. Reductions to Operations Support, therefore, precipitate reductions in effectiveness in Taxpayer Services.

## EARNED INCOME TAX CREDIT (EITC) ERROR RATES

*Question.* In responses to written questions asked during your confirmation process, you indicated that you didn't have information about the sources of improper EITC payments but you understood that 70% of EITC tax returns were prepared by paid preparers. You also indicated that you thought all EITC taxpayers should consider the same questions regardless of how they prepare their tax returns and that you were open to working with the tax software industry to identify problems and propose solutions. Well, IRS's own data indicates that the paid preparers now prepare only 58% of EITC returns and that the improper payment rate on self-prepared returns has skyrocketed. I understand that your agency has developed proposed changes to the Schedule EIC that should help reduce improper payments. Could you explain why these changes have not been implemented yet?

Answer. I would like to correct the record that the error rate on self-prepared returns has skyrocketed. Our updated compliance study for tax years 2006 to 2008, released in August 2014,<sup>5</sup> includes a detailed analysis of errors on EITC returns. It is based on the IRS's National Research Program (NRP) information which includes the results from a statistically valid, random sample of EITC tax returns. The study found that there was no difference in either the frequency of error or the dollar error percentage on returns prepared by paid preparers as compared to those prepared by taxpayers themselves.

Much of the difficulty in administering the EITC derives from the complexity of its statutory eligibility requirements, many of which are known only to the taxpayer and cannot be independently confirmed because there is no third-party corroborating data. Based on the most recent compliance study which examined the causes for erroneous EITC claims, the vast majority of improper payments are from inability to authenticate eligibility. They include errors associated with the inability to authenticate qualifying child eligibility requirements, mainly relationship and resi-

<sup>5</sup> Publication 5162 (8-2014) Catalog Number 66766H Department of the Treasury Internal Revenue Service.

gency requirements. They also include filing status errors, when married couples file as single or head of household; and income misreporting errors, when taxpayers misreport self-employment income that is not reported to IRS by third parties. Finally they include errors in rules for all taxpayers claiming EITC, when taxpayers claim the credit using an invalid SSN, or when the credit is claimed by a non-citizen who has not been in the US for the entire year, or when the taxpayer meets the rule to be a qualifying child for another taxpayer; none of which can be authenticated by IRS at time of filing.

The Compliance Study also estimates the rest of the improper payments are due to program design errors. These errors relate to income misreporting, tiebreaker errors, and joint return errors of qualifying children. These errors occur because information needed to confirm payment accuracy is not available at the time the return is processed and the refund is issued. For income misreporting, payer information is typically not available until after the filing season, therefore wages and other income sources cannot be matched against the return at time of filing. For tiebreaker errors and joint return errors of qualifying children, because returns are processed as filed, the IRS is unaware of a duplication of a qualifying child occurs when the first return is filed. The IRS cannot wait until all returns are filed to determine whether a child is claimed more than once and which taxpayer is actually entitled to claim the child, or to determine whether children claimed for EITC have filed a joint return.

Since the tax years in the study, the IRS has continued its outreach and compliance programs directed at taxpayers. The IRS has also conducted significant outreach to educate paid preparers on their EITC due diligence responsibilities as well as revising the Regulations, improving the preparer checklist, and delivering its EITC paid preparer strategy. The IRS also continues to believe that requiring minimum qualifications for paid preparers would improve the accuracy of all returns, including EITC returns, and we continue to support legislation that would allow the IRS to require minimum qualifications for paid return preparers.

The IRS has been following the trend in the decrease in paid preparer returns and corresponding increase in self-prepared returns that started with tax year 2007, likely facilitated by the availability of software. IRS data shows that for tax year 2012, 57% of EITC returns were prepared by paid preparers. Over the last several years, the IRS and the Treasury Department have considered new ways to ensure taxpayers preparing their own returns carefully consider EITC eligibility requirements. The IRS worked with our IRS/EITC Software Developers Working Group on proposals. The Department of the Treasury is currently conducting a pilot with a Free-File Alliance partner to test new ideas. Based on Treasury's test results and continued discussions, the IRS and Treasury will address potential changes that could improve areas of EITC noncompliance while taking taxpayer burden into consideration.

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## QUESTIONS SUBMITTED BY HON. DEBBIE STABENOW

### 1. TAXPAYER SERVICES

*Question.* The National Taxpayer Advocate's 2014 report to Congress describes the kinds of difficulties that families have faced and will continue to face as they file their taxes.

Of particular concern are the large number of taxpayers who are unable to actually be connected with a person at the IRS to get their basic tax questions answered. More than a third of calls end with the caller hanging up before having their question answered, receiving a busy signal, or being disconnected.

In recent years, the agency has lost more than ten thousand employees, including thousands of employees dedicated to helping taxpayers.

What can we do to improve the service that taxpayers receive from the IRS? Would granting the President's request for more money and more staff help you deliver better service?

*Answer.* The best thing that Congress can do to improve the service that taxpayers receive from the IRS is to approve the President's budget request in totality.

Funding for the IRS has been reduced by \$1.2 billion over the last five years, dropping to \$10.9 billion in Fiscal Year (FY) 2015. The IRS is now at its lowest level

of funding since 2008. If adjusted for inflation, the agency's budget is now comparable to where it was in 1998.

Since 75 percent of the IRS budget is personnel, the agency has been absorbing the budget cuts mainly by reducing our workforce. As a result, IRS ended FY 2014 with more than 13,000 fewer permanent full-time employees compared with 2010. The IRS expects to lose another 3,000 or more through attrition by the end of this fiscal year.

This year, the IRS was forced to substantially reduce hiring of extra seasonal help we usually have during the filing season. As a result, IRS's phone level of service at the start of the filing season was 54 percent, and dipped below 40 percent toward the end of filing season. That means many callers were forced to call more than once to get through, and more than six out of every ten calls did not reach a live assistant. Further, IRS expects to end the fiscal year with an average phone level of service of 40 percent. That is truly an unacceptable level of taxpayer service, especially given that the goal for phone service in a given year, if the agency were adequately funded, would be 80 percent.

To further illustrate how serious IRS's phone service difficulties have been, the number of taxpayers disconnected by IRS's phone system when it becomes overloaded with calls is substantially higher this year. The number of these disconnects has reached 8.1 million so far this year, as compared with 951,000 by this time last year. Additionally, taxpayers who have gotten through to an assistant have faced extended wait times that are unacceptable.

As for in-person assistance, during the filing season many taxpayers had to line up outside our Taxpayer Assistance Centers (TACs) hours before they opened in order to get service. This is not a new problem this year, but it has gotten worse over time. IRS encouraged taxpayers to utilize the resources and self-service options available online at [www.irs.gov](http://www.irs.gov) this filing season to help reduce the need for in-person assistance, but the problem persisted due to a lack of funding. Approving the President's budget request for the IRS in totality would allow the IRS to provide the staff, services, and infrastructure it needs to meet taxpayer demand, including restoring its toll-free level of service to 80 percent, providing adequate staffing to meet the demands of taxpayers at its TACs, and enhancing its web applications to provide a broad range of self-service options.

*Question.* Which taxpayers are affected the most by these cuts to services? It seems to me as though lower-income and middle-class taxpayers, who can't afford to hire accountants and lawyers to follow up with the IRS, suffer the most from these cuts to the important services the IRS provides.

*Answer.* As noted in your remarks, the IRS has lost several thousand employees dedicated to helping taxpayers. All areas are affected by the difficult choices budget cuts and increased responsibilities have forced us to make. In 2014, the IRS began prioritizing limited staffing and resources to help those taxpayers who must interact with us by phone or in person, while encouraging all those who can to use self-service or other, more efficient options.

As projected, many taxpayers and tax preparers would not be able to reach us by telephone or at our Taxpayer Assistance Centers (TACs) this filing season. Those who did experienced a considerable hold and wait time. While our service levels were lower than we would prefer, our employees worked hard again this filing season to help the nation's taxpayers.

We urge all taxpayers to take advantage of the many resources available 24/7 on [www.irs.gov](http://www.irs.gov). These resources include online forms and publications, tax law interactive tools and references, Get Transcript, Where's my Refund? and help understanding an IRS notice or letter—again, all available anytime on [www.irs.gov](http://www.irs.gov). Those without internet access can use their telephone to access automated response systems. We created the IRS Services Guide to help taxpayers locate the services they need (<http://www.irs.gov/pub/irs-pdf/p5136.pdf>). Additionally, taxpayers without internet access may be able to use a Facilitated Self-Assistance kiosk, available at a few of our TACs.

During filing season we answer basic tax law questions on our phone lines and at the TACs. Alternatively and during the rest of the year we encourage taxpayers to try the *Interactive Tax Assistant* [http://www.irs.gov/uac/Interactive-Tax-Assistant-\(ITA\)-1](http://www.irs.gov/uac/Interactive-Tax-Assistant-(ITA)-1) that takes them through a series of questions just like one of our customer service representatives would to determine exactly what help or information they need. Taxpayers can also look to tax return preparation software packages

since tax law help is included as part of software. We also offer more than 100 short instructional videos, tax tips, and other resources year-round through a variety of social media platforms. Taxpayers should find these automated services convenient and easy to use. Many are available any time, day or night.

Seniors and low-to-moderate-income taxpayers also have the option to get free help with return preparation through our Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) programs. These programs also serve persons with disabilities, those with limited English proficiency, and Native Americans. We leverage national and local partners to deliver free tax preparation and outreach programs to millions of taxpayers throughout the nation. As of April 13, 2015, over 90,000 volunteers prepared more than 3.37 million federal tax returns at 12,057 VITA/TCE sites, compared to 3.35 million returns as of the same time last year.

To expand the availability of alternative preparation and filing options, some of our partners offer taxpayers self-service options such as Facilitated Self-Assistance (FSA) and Virtual VITA. The FSA service option empowers taxpayers to prepare their own return with the assistance of a certified VITA volunteer. Virtual VITA helps our partners to provide free tax preparation services “virtually” to disabled, elderly and those with transportation or other issues.

## 2. CORPORATE TAX ENFORCEMENT

*Question.* Corporations have tax departments and can hire firms and consultants to take “aggressive” tax positions.

These aggressive strategies might involve claiming deductions or characterizing income in a way that the IRS may or may not agree with. It might also involve claiming deductions or characterizing income in a way that the IRS doesn’t have the manpower to catch. This means that some companies can avoid paying what they owe, while so many taxpayers are just trying to play by the rules.

In his budget request, the President has requested increasing the appropriation for enforcement by \$540 million.

What impact would this increased enforcement funding have on your ability to go over corporate tax returns?

Answer. The additional enforcement funds requested in the FY 2016 Budget support an array of examination, collection, investigation, and regulatory programs that focus on all taxpaying segments. Initiatives that will support improved compliance by businesses include implementing business document matching programs; improving the identification and audit coverage of large, tiered partnerships and strengthening the administrative procedures that apply to partnerships, S corporations and Real Estate Mortgage Investment Conduits with more than 10 members or partners under the Tax Equity and Fiscal Responsibility Act (TEFRA); expanding international compliance efforts, including offshore criminal investigations; enhancing large corporate compliance through improved issue identification; and acquiring network analysis tools to identify potentially abusive returns.

## QUESTIONS SUBMITTED BY HON. MARK R. WARNER

*Question.* I have heard from Virginia institutions of higher education about penalties for filing Forms 1098-T with incorrect or missing TINs.

The IRS started fining institutions for filing 1098-Ts with incorrect or missing PINs going back to the 2011 tax year. Although the IRS issued a blanket waiver for the 2011 tax year, they have declined to issue similar blanket waivers for subsequent years, even though institutions filed their Forms 1098-T for the 2012 tax year without knowledge of the penalties. Institutions must request a waiver each year, creating bureaucratic burden. In addition, institutions must rely on student-supplied information and they cannot use independent verifying programs to ensure that the Forms 1098-T contain the correct TINs.

For one Virginia college, the 2012 proposed penalty is \$800,000.

What is the IRS doing to fix the unnecessary confusion caused by the proposed penalties and come to a long-term solution that does not unduly harm or burden colleges or universities?

Answer. Accurate information reporting is critical to the IRS’s ability to administer the tax laws. The IRS provides guidance and regularly works with taxpayers to help them comply with the information reporting requirements.

IRC section 6050S requires colleges and universities to report to the IRS the amounts of qualified tuition and related expenses received or billed and provide a statement to the student containing the same information. This provision was enacted in 1997 for academic periods beginning after 1997. Under section 6050S(b)(2)(A), the educational institution is required to include the name, address, and TIN of the student on Form 1098-T and the student statement. Final regulations under section 6050S were published in 2002 after notice soliciting public comments; these regulations were effective for Forms 1098-T required to be filed after 2003.

Sections 6721 and 6722, enacted in 1986, impose penalties for failure to file correct information returns and failure to furnish correct payee statements respectively. The 1997 legislation amended sections 6721 and 6722 to apply the section 6721 penalties to Form 1098-T and the section 6722 penalties to the student statement. Regulation 1.6050S-1 details the information required to be reported on Form 1098-T, the penalties for failure to comply, and the grounds for obtaining relief from the penalties. The underlying law is not new, and colleges and universities filing these information returns should have been aware of their legal requirements under sections 6050S, 6721, and 6722 for many years. However, the IRS granted blanket waivers to colleges and universities for tax year 2011 from penalties under sections 6721 and 6722 as this was the first year Form 1098-T was included in the systemic penalty notice program.

The blanket waivers were designed to provide affected educational institutions with additional time to conduct the due diligence necessary to ensure the filing of correct information returns and compliance with the statutory provisions of the law. Although blanket waivers were not provided after tax year 2011, penalty relief is available under section 6724 if the educational institution acted in a responsible manner when soliciting tax identification numbers (TINs).

The IRS has undertaken a review of its procedures and communication tools. As a result of this review, the actions listed below are being taken to ensure that the IRS provides correct and complete information in communications and to ensure employees apply the correct criteria when considering penalty waiver requests from these institutions.

- Revise Internal Revenue Manual guidance.
- Revise Publication 1586, Reasonable Cause Regulations and Requirements for Missing and Incorrect Name/TINs.
- Revise Notice 972CG that is sent to the institutions proposing a penalty.
- Revising CPE training materials to include additional guidance on penalty relief for Forms 1098-T.

In addition, and as discussed below, the Department of the Treasury has proposed legislation to provide an exception to the limitation on disclosing tax return information to expand TIN matching beyond forms where payments are subject to back-up withholding. This would allow educational institutions to validate the accuracy of TINs included on Form 1098-Ts prior to filing, and if used, could be factored into reasonable cause penalty waiver considerations.

*Question.* Is the IRS willing to work with universities to help them verify TINs?

*Answer.* The IRS has always worked and will continue to work with taxpayer entities to help them comply with the law. Under current law, TIN verification is allowed for filers of information returns that report payments made by the filer that are subject to back-up withholding, such as dividends or other income. In such cases, the tax law allows the payor, before filing the return, to verify with the IRS the TIN furnished by the payee. Otherwise, the law precludes the IRS from disclosing a taxpayer's name, TIN, or other return information without specific authorization from the taxpayer. See IRC sections 3406 & 6103; Treas. Reg. section 31.3406(j)-1; Rev. Proc. 2003-9, 2003-8 I.R.B. 516.

Form 1098-T does not report a payment issued by the educational institution, like many information documents, but rather reports that the institution received or billed for tuition. The provisions of the law authorizing TIN verification do not, therefore, apply to Form 1098-T. Consequently, permitting TIN verification for Form 1098-T would require legislation. Accordingly, the Department of the Treasury has proposed legislation to provide an exception to the limitation on disclosing tax return information to expand TIN matching beyond forms where payments are subject to back-up withholding. See *Gen. Explanations of the Administration's FY 2016 Revenue Proposals* at pg. 217, <http://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2016.pdf>.



Without legislative action, the IRS remains bound to follow the law as currently prescribed.

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QUESTIONS SUBMITTED BY HON. BENJAMIN L. CARDIN

*Question.* As you know, the IRS has released a Form 1023-EZ as part of its effort to handle a large application backlog. While you should be commended for the streamlining work you've done at the IRS with limited resources thus far, I am concerned that the IRS may be missing important pieces of information from Form 1023-EZ filers. Exempt organizations that file the regular Form 1023 application must submit their organizing/governance documents at that time. Form 990 and 990-EZ filers must submit changes to those documents with those annual returns.

When a 1023-EZ filer "grows" to the level where they should be filing a Form 990-EZ or 990, will they be expected to file the basic organizing documents at that time?

*Answer.* When an entity that files a Form 1023-EZ, Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, files a Form 990, Return of Organization Exempt from Income Tax, or 990-EZ, Short Form Return of Organization Exempt from Income Tax, for the first time, the entity is not required to provide its organizational documents with its return. As is the case for other exempt organizations, if the entity files a Form 990 or 990-EZ and the entity's organizational documents have changed, it must describe any significant changes to documents on its Form 990 or 990-EZ.

*Question.* The Work Opportunity Tax Credit is an incredibly important incentive that is used by employers throughout Maryland. While WOTC is now expired, it was made available retroactively in 2014. For WOTC processing to begin, the IRS must issue guidance that recognizes that the program has been reauthorized and that provides some transition relief so that employers can submit WOTC paperwork for hires in 2014 to their state agencies. The need for guidance to come out quickly is especially great because the program has only been extended for one year.

When do you expect IRS to release guidance, similar to Notice 2013-14, that will enable the WOTC program to be efficiently implemented retroactively?

*Answer.* On December 19, 2014, Congress retroactively extended the Work Opportunity Tax Credit (WOTC) for the 2014 tax year. To claim the credit, an employer who hires a member of a targeted group listed in section 51(d)(1)(A) through (I) ordinarily has 28 days from the date of hire to submit to the Designated Local Agency (DLA) a Form 8850, Pre-Screening Notice and Certification Request for the Work Opportunity Credit. Recognizing the concern raised that because of the retroactive enactment of WOTC, employers who hired individuals during 2014 would need additional time to file the form, on February 19, 2015, the IRS issued Notice 2015-13 providing employers until April 30, 2015, to file the form with the DLA.

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QUESTIONS SUBMITTED BY HON. DEAN HELLER

*Question.* In my opinion, properly done tax reform would reduce the IRS to its core function of collecting tax revenues, not implementing new tax-related regulations and reporting requirements under Obamacare. How many full time equivalents (FTE) or what percentage of the agency are dedicated to implementing Obamacare this tax filing season?

*Answer.* The IRS projects requirements of approximately 2,828 full-time equivalents (FTE) related to the tax law changes included in the ACA for fiscal year 2015. This includes FTEs to implement both the Marketplace provisions (such as the premium tax credit provision) and non-Marketplace provisions (such as the fee on branded drug manufacturers). This level of FTE is approximately 2.5% of our FY 15 operating plan.

*Question.* Under the IRS's own estimates, Obamacare will cost individuals and businesses millions of hours. Do you have an estimate of how many hours (or percentage of the agency) are expected to be spent on implementing Obamacare this FY?

*Answer.* See the answer above, which tracks full-time equivalents, i.e. hours spent by IRS employees.

*Question.* On February 5, 2015, the IRS announced (IR–2015–22) its new online directory of Federal tax return preparers. The searchable directory includes attorneys, CPAs, enrolled agents and those who have completed the requirements for the IRS Annual Filing Season Program (AFSP). All of those listed in the directory have Preparer Tax Identification Numbers (PTINs). However, “Tax return preparers with PTINs who are not attorneys, CPAs, enrolled agents or AFSP participants are not included in the directory.”

*a.* Haven’t return preparers who obtained PTINs complied with the only mandatory requirements applicable to return preparers?

*Answer.* Individuals preparing federal tax returns for compensation are required to have a preparer identification number (PTIN). They are also required to provide that number on the returns they prepare, sign the returns they prepare, and furnish a copy of the prepared return to the taxpayer.

*b.* What is the rationale for excluding from the directory those who have PTINs but who are not also attorneys, CPAs, enrolled agents or AFSP participants?

*Answer.* The directory is a tool to assist taxpayers with finding a preparer or verifying credentials and/or select qualifications. As such, the preparers listed in the Directory have earned and maintained professional credentials (CPA, enrolled agent, or attorney) or have completed a certain number of hours of continuing education from IRS-approved continuing education providers in the specific categories of federal tax law topics, tax law updates, and ethics.

*Question.* The IRS website page for the directory search (<http://irs.treasury.gov/rpo/rpo.jsf>) contains the following statement: “Additionally, the IRS does not endorse any preparer or credential over another.”

*a.* How do you reconcile that statement with the fact that the official IRS return preparer directory excludes thousands of compliant preparers who are PTIN holders?

*Answer.* The description of the Directory on the IRS website (and information on linked webpages that include Information on Understanding Tax Return Preparer Qualifications and Credentials, and information on Choosing a Preparer) notes that anyone can be a paid tax return preparer as long as they have an IRS Preparer Identification Number (PTIN), and they sign and enter it on all returns they prepare. This information provides that tax return preparers who have PTINs but are not listed in the Directory may provide quality return preparation services, but cautions taxpayers to choose any return preparer wisely and to always inquire about their education and training.

*Question.* Please provide the following information about the return preparer directory (as of February 5, 2015):

*a.* How many return preparers are listed in the directory?

*Answer.* There are 312,298 return preparers listed in the directory, some holding more than one designation.

*b.* How many return preparers are listed in each of the six searchable categories?

*Answer.*

i. Attorney Credential .....	27,729
ii. Certified Public Accountant Credential .....	202,943
iii. Enrolled Agent Credential .....	48,322
iv. Enrolled Actuary Credential .....	350
v. Enrolled Retirement Plan Agent Credential .....	641
vi. Annual Filing Season Participant .....	41,863

*c.* How many PTIN holders are not listed in the directory?

*Answer.* As of February 6, 2015, 360,592 return preparers with PTINs only are not included in the directory.

*Question.* Has Congress ever specifically authorized the creation of this directory of return preparers?

*Answer.* The Directory is a tax administration tool and requires no Congressional authorization. More than 140 million individual tax returns were filed last year, and more than half of them were prepared with the help of a paid preparer. The Direc-

tory is a practical tool for the millions of Americans who rely on the services of a paid return preparer. The purpose of the Directory is to help taxpayers find a tax professional with credentials and select qualifications to help them prepare their tax returns. It is part of a broader effort to provide taxpayers with information to understand the different categories of return preparers and their representation rights so they can choose a qualified tax return preparer who best meets their needs.

*Question.* How much did the IRS spend in developing this online directory? What is the estimated annual cost to maintain it?

Answer. Total development costs for the directory were \$244,000 with an estimated annual maintenance cost of \$24,000.

*Question.* Last year, you acknowledged, in your April testimony that the vast majority of return preparers operate with the highest ethical standards. That said, the GAO and the IRS's own research have admitted that a large number of return preparers continue to engage in fraud. If this is true, how does urging thousands of return preparers to complete costly and time-consuming continuing education combat return preparer fraud?

Answer. The IRS and the National Taxpayer Advocate have long agreed that the professionalism of tax return preparers can be increased through a framework that provides for registration, testing, certification, continuing education, and consumer education. (See, the Return Preparer Review, IRS Publication 4832 (Rev. 12-2009) at pages 22-23) (<http://www.irs.gov/pub/irs-pdf/p4832.pdf>). See also, the Taxpayer Advocates 2015 Objectives Report to Congress (June 2014 at page 71) (<http://www.taxpayeradvocate.irs.gov/2015ObjectivesReport>). Absent the authority to require tax return preparers to have minimum qualifications or to mandate testing and continuing education, encouraging tax return preparers to maintain currency with federal tax law through continuing education improves compliance with the tax laws and filing requirements. Encouraging taxpayers to choose preparers wisely and to familiarize themselves with their preparer's qualifications also reduces opportunities for fraud to be perpetrated.

Given that more than half of all taxpayers rely on a paid preparer to complete their tax returns, accurate return preparation, improved compliance and effective tax administration necessitate that tax return preparers have a basic level of competency to complete federal tax returns. Sixty percent of all paid tax return preparers are uncredentialed. With the escalation of taxpayer fraud and identity theft, it is more important than ever that a taxpayer choose his/her tax return preparer wisely and that should mean a tax return preparer who is knowledgeable in the tax law and return preparation. Remaining current with the tax law and tax law changes through continuing education benefits the preparer, the taxpayer and tax administration.

*Question.* Over the past decade, the IRS Tax Division has obtained numerous injunctions against fraudulent tax return preparers. Despite these injunctions, I have seen alarming reports that the IRS is continuing to send out questionable refunds long after the IRS should have realized there was a problem. Can you list the steps the IRS is taking over the next year to block improper refunds from going out and increase its vigilance against return preparer fraud?

Answer. The IRS maintains an office whose primary responsibility is fraud detection/revenue protection activities, addressing millions of questionable returns each year. All refund returns flow through the Electronic Fraud Detection System (EFDS) and Dependent Database (DDb) which contain complex fraud models and filters developed from historical fraud characteristics used to identify questionable income, withholding, refundable credits and/or taxpayer identity. In addition to these systemic fraud checks, employees perform analysis and review groups of returns with similar characteristics that indicate refund schemes. These fraud prevention efforts occur all year long and the IRS has implemented the following improvements to further combat fraud:

- In January 2013, we rolled out a program allowing financial institutions to reject questionable refunds using a special code on current year direct deposit refunds when the name/TIN listed on the Treasury ACH file for the tax refund does not match the account holder information in the bank's records for a specified set of banking filters. An internal transcript is then generated in order to review the refund.
- In January 2015, we limited the number of direct deposit refunds that can be made to a single account to three (3) and any additional refunds are sent via paper checks. This change is expected to deter fraud and identity theft.

For the 2015 filing season, we also increased the number of identity theft filters over the previous filing season and utilize dynamic lists to update filters based upon current schemes, historical characteristics and/or patterns.

A major IRS project under development that will assist with pre-refund fraud detection, income verification and taxpayer authentication is the Return Review Program (RRP). This application will replace the EFDS, enhancing many aspects of IRS compliance activity. RRP will perform historical filing analysis and use improved complex programming to review all returns for fraud potential improving the IRS's ability to identify and treat fraud and Identity Theft filings.

Return preparer fraud is also addressed by IRS Criminal Investigation (CI). CI continues to investigate tax return preparers who promote schemes designed to obtain fraudulent refunds or to fraudulently reduce their clients' tax liabilities. CI will continue to investigate paid preparers who use invalid identifiers or fail to sign returns. CI will also increase its focus on preparers who promote schemes to US citizens living abroad.

Each year, CI uses information collected from various sources to identify return preparer schemes. CI uses investigative analysts in CI's Scheme Development Centers (SDCs), special agents in 25 Field Offices, and data base information on return preparers to identify and evaluate preparers for potentially fraudulent activity. Return preparers are evaluated on a set of characteristics representative of the set of returns submitted by individual preparers. CI uses a Return Preparer Analysis Tool to perform a collection of fraud tests on return preparer data in the returns that the IRS has determined may indicate a higher-than-normal probability of fraud. The research into the pattern of suspicious return preparer schemes provides insights into the following questions:

- Who is preparing the returns?
- Does the preparer only file during the filing season (January–April)?
- Do returns come in large batches?
- Does the preparer only send in returns in October?
- Where does the preparer conduct business?
- Where does the preparer live?
- What are the mailing locations of the returns?

For the 2015 filing season, CI is using a six prong approach to create an enhanced enforcement presence among tax practitioners, tax preparers, and other third parties in the return preparer community:

- Undercover special agent shopping activities.
- Coordinated legal and enforcement actions during filing season.
- Enhanced compliance partnerships with internal stakeholders.
- Enhanced partnership with external stakeholders.
- Outreach with the return preparer community.
- Coordinated cross-functional publicity.

CI continues to use undercover investigations as one of the most effective methods of uncovering and investigating questionable return preparer schemes.

CI continues to recommend appropriate e-file sanctions at the conclusion of any criminal investigation that involves an authorized e-file provider who has violated the requirements of the e-file program. Sanctions imposed may be a written warning, a written reprimand, suspension, or revocation of the Electronic Filing Identification Number (EFIN).

CI continues to support civil operations in the return preparer area by its many partnerships throughout the IRS to:

- Conduct Knock and Talk Visits with potentially abusive EITC return preparers;
- Conduct parallel investigations in order to deter preparer noncompliance (because they result not only in criminal convictions and publicity, but also civil injunctions and preparer penalties);
- Identify and investigate return preparers who do not readily identify themselves because they do not sign their clients' returns;
- Determine electronic filing suitability of all e-file applicants based on their criminal history; and
- Work CI cases that involve disreputable conduct before the IRS by an attorney, certified public accountant or enrolled agent.

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

DEPUTY COMMISSIONER

November 18, 2014

MEMORANDUM FOR SENIOR EXECUTIVE TEAM

FROM: John M. Dalrymple, Chairman, Executive Resources Board

SUBJECT: Impact of Disciplinary/Adverse Action on Performance-based Pay Adjustments, Bonuses, and Awards

Please be advised that pursuant to a September 24, 2014 Department of the Treasury policy transmittal number TN-14-003, entitled *Departmental Oversight for Executive Misconduct in Determining Pay Adjustments, Bonuses and Awards* (Enclosure 1), the following is effective immediately:

An Executive (including members of the Senior Executive Service (ES), Senior Leaders (SL), Streamlined Critical Pay employees (AD), or the equivalent, or IR-01 Executive Officers (i.e., "SES-in-waiting")), who is reprimanded or suspended, as result of any form of misconduct, is ineligible for the following:

A monetary performance-based award for the rating period in which the disciplinary action or adverse action was administered (e.g., performance bonus, Special Act Award, Quality Step Increase, Presidential Rank Award, a performance-based salary adjustment otherwise authorized under 5 CFR 534.404, etc.)

The Treasury-wide policy is already incorporated in the corresponding IRS policy, promulgated on March 14, 2014, via my memorandum entitled *Policy and Procedures for High-Level Personnel* (Enclosure 2).

Additionally, the following policy is effective immediately for all Executives and Executive Officers:

If there was a final Agency decision that an IRS Executive (including members of the Senior Executive Service (ES), Senior Leaders (SL), Streamlined Critical Pay employees (AD), or the equivalent, including IR-01 Executive Officers ("SES-in-waiting")) committed any act or omission set forth in 26 USC § 7804, note §§ 1203(b)(1)-(10) of the Internal Revenue Service Restructuring and Reform Act of 1998, such an employee shall not be eligible for a monetary performance award. If any final agency decision on a § 1203(b) finding is overturned by an administrative or judicial third-party, the third-party may order a retroactive award so long as such award is consistent with the Back Pay Act.

If you have any questions regarding this matter, please contact Dan Riordan, Human Capital Officer, at (202) 317-7600, or a member of your staff may contact Max Goodman, Manager, Executive Misconduct Unit, Workforce Relations Division, Human Capital Office, at (202) 302-7571.

Enclosures (2)

cc: All Executives  
Associate Chief Counsel (General Legal Services)  
TIGTA Deputy Inspector General for Investigations

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

HUMAN CAPITAL OFFICE

February 4, 2015

MEMORANDUM FOR SENIOR EXECUTIVE TEAM

FROM: Daniel T. Riordan, IRS Human Capital Officer

SUBJECT: Interim Guidance: Impact of Employee Misconduct on Awards, Bonuses, Performance-Based Pay Increases, and Quality Step Increases to be Paid in Fiscal Year (FY) 2015

This is to inform you that we will issue the attached interim guidance and procedures to the Embedded HR directors notifying them about the screening for Section 1203(b) violations that will be conducted in FY2015 before granting performance awards, bonuses, performance-based pay increases (PBI), and Quality Step Increases (QSIs).

This guidance applies to recognition to be paid or made effective in Fiscal Year FY2015 and applies to all bargaining (BU) and non-bargaining unit (NBU) IRS employees except executives and other high-level officials who are covered by *separate misconduct policy and procedures* approved by the Chair of the Executive Resources Board.

An employee shall not be eligible for covered recognition (excluding QSIs) to be paid or made effective in FY2015 if there has been a final Agency decision in FY2014 that a Section 1203(b) violation has occurred. Additionally, employees will not be eligible for QSIs paid in FY2015 if there has been a final Agency decision in FY2015 that a Section 1203(b) violation has occurred or a decision to impose any discipline with a penalty of suspension of 15 days or longer.

Further guidance will be issued regarding misconduct screening for recognition to be paid or made effective in FY2016. This guidance will incorporate recently issued Treasury policy once an agreement is reached with NTEU. This interim guidance will be in effect until the final policy is issued.

If you have any questions, please contact me or have a member of your staff contact Terri DeAngelis, Associate Director, Pay, Leave and Performance Branch at [teresa.a.deangelis@irs.gov](mailto:teresa.a.deangelis@irs.gov), or (215) 861-0775, or Marilyn Cain, Chief, Payband, Performance and Awards Programs at [marilyn.j.cain@irs.gov](mailto:marilyn.j.cain@irs.gov) or (512) 499-5431.

Attachment

cc: Human Capital Advisory Council  
FMA/PMA

**Attachment Interim Guidance:** HCO-06-1214-02-04-2015

**The following changes are effective immediately for IRM 6.451.1, Awards and Recognition.**

**New IRM Subsection:** Screening for Employee Misconduct Before Granting Covered Recognition.

- 1) **Covered Employees.** These procedures apply to all bargaining (BU) and non-bargaining unit (NBU) IRS employees except executive and other high-level officials who are covered by *separate misconduct policy and procedures* approved by the Chair of the Executive Resources Board.
- 2) **Covered Recognition.** These procedures cover the following types of recognition to be paid or made effective in Fiscal Year (FY) 2015.
  - a. BU employees: monetary and time-off performance awards, bilingual awards, and paybanded (IR) employees' performance bonuses and performance-based (pay) increases.
  - b. BU employees: monetary and time-off performance awards, bilingual awards, and monetary/time-off awards elected by BU employees instead of Quality Step Increases (QSIs) under negotiated provisions.
  - c. NBU and BU employees: QSIs.
- 3) **Excluded Recognition.** These procedures do not cover suggestion awards, travel gain-sharing awards, referral bonuses, foreign language awards,<sup>6</sup> or any other award or bonus not listed under paragraph 2, Covered Recognition.

<sup>6</sup>Foreign language awards are distinguished from IRS bilingual awards. Foreign language awards may be granted only to law enforcement officers as defined in statute (for example, GS-1811 Criminal Investigators (Special Agents) assigned to the Criminal Investigation Division). However, bilingual awards are covered recognition under these procedures.

a. NBU and BU employees: Manager’s Awards and Special Act Awards are not covered by this policy because they are not being paid during the applicable period.

**4) Disqualifying Misconduct** will result in ineligibility for covered recognition.

a. 1203(b) Violations. A Covered Employee shall not be eligible for recognition described in paragraphs 2a and 2b to be paid or made effective in FY 2015 if there has been a final Agency decision in FY 2014 that a Section 1203(b) violation has occurred.

NOTE 1: Section 1203(b) violations are described in *Section 1203(b)(1)–(10) of the Internal Revenue Service Restructuring and Reform Act of 1998 (“RRA ’98”)* which provides that IRS employees must be terminated from Federal employment if they violate any of the ten specific acts or omissions described. Acts or omissions of IRS employees will be subject to the discipline prescribed by section 1203(b) only if those acts are taken, or those omissions are made, with some degree of intent. The statute also allows the IRS Commissioner to mitigate the sanction of termination.

NOTE 2: With respect to Section 1203(b) violations, “Final Agency decision” refers to when the IRS deciding official makes the decision that an employee violated Section 1203(b) of RRA ’98 after the employee’s oral and/or written reply occurs (if applicable).

b. 1203(b) Violations. A Covered Employee shall not be eligible for recognition for a QSI as described in paragraphs 2c to be paid or made effective in FY 2015 if there has been a final Agency decision in FY 2015 that a Section 1203(b) violation has occurred. See Notes 1 and 2 above.

c. Non-1203(b) Violations. A Covered Employee shall not be eligible for recognition for a QSI as described in paragraph 2c if there has been a final Agency decision in FY 2015 to impose any discipline with a penalty of suspension of 15 days or longer, or removal.

NOTE: With respect to discipline, “Final Agency decision” refers to when the IRS deciding official makes the decision that an employee will be disciplined as described in paragraph 4c, after the employee’s oral and/or written reply occurs (if applicable).

NOTE: See summary chart below:

Award/Recognition	Ineligibility Standard
Cash/TOA for FY 2014 performance paid in March 2015 QSI for FY 2015 performance paid in FY 2015	Final Agency decision in FY 2014 that a Section 1203(b) violation has occurred  <ul style="list-style-type: none"> <li>• Final Agency decision in FY 2015 that a Section 1203(b) violation has occurred</li> <li>• Final Agency decision in FY 2015 to impose any discipline with a penalty of suspension of 15 days or longer</li> </ul>
PBI based on FY 2014 performance rating paid in FY 2015	Final Agency decision in FY 2014 that a Section 1203(b) violation has occurred

**5) Screening for Disqualifying Misconduct.** The Human Capital Office will use the HCO Automated Labor Employee Relations Tracking System (ALERTS) to perform centralized screening for disqualifying misconduct and will ensure that employees, who have been the subject of final Agency decisions in FY 2014 or FY 2015 as applicable, shall not be granted Covered Recognition in FY 2015.

**6) Employee Notification.** Ineligible employees will receive a letter mailed to their home address of record prior to the effective date of the covered recognition. Upon receipt of the letter, a BU employee may file a grievance under Article 41 of the National Agreement to contest his/her ineligibility. For NBU employees, a determination of ineligibility under these procedures is not grievable under the Agency Grievance Procedure, IRM 6.771.1.

**7) Documentation.** The Workforce Relations Division shall maintain ALERTS screening documentation in accordance with records retention standards.

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

DEPUTY COMMISSIONER

March 14, 2014

MEMORANDUM FOR SENIOR EXECUTIVE TEAM

FROM: John M. Dalrymple, Chairman, Executive Resources Board

SUBJECT: Misconduct Policy and Procedures for High-Level Employees

[Supersedes Deputy Commissioner for Services and Enforcement Memorandum of January 06, 2014]

This memorandum and its attachments promulgate Internal Revenue Service policy and procedures pertaining to the adjudication of misconduct allegations involving high-level employees (i.e., Executives [ES; SL; AD]; Executive Officers [IR-01]; Senior Managers [IR-01]; Front Line Managers [IR-03]; and non-bargaining unit employees at grade GS-15, with the exception of those serving at grade via temporary promotion), and is issued under my authority and responsibilities as Chairman, Executive Resources Board.

One of our responsibilities as stewards of our nation's tax system is to establish and maintain the highest standard of professionalism and personal integrity throughout the IRS. All high-level employees must set an example through impeccable conduct. An allegation that a high-level employee has failed to meet this obligation must be promptly addressed and accurately and effectively resolved. The IRS has determined that high-level employees must be held to a higher standard of professionalism, integrity, and accountability than employees of lower grade and organizational rank. Accordingly, high-level employees who engage in misconduct generally will be subject to corrective action exceeding that which is suggested for comparable offenses committed by employees of lower grade and rank.

Attached are the Policies and Procedures for Adjudicating Conduct-Related Matters Involving High-Level Employees; Standards for Conduct-Based Inquiries; and Report of Inquiry template. The policies, procedures, and guidelines contained in the attachments will help to ensure consistency, objectivity, and accountability in resolving allegations of misconduct. Each allegation of misconduct will be evaluated thoroughly and accurately by either internal administrative review/inquiry, or by formal investigation conducted by the Treasury Inspector General for Tax Administration (TIGTA).

Every allegation of misconduct, involving a high-level employee, must be presented to the Executive Misconduct Unit (EMU), of the Workforce Relations Division, Human Capital Office, for guidance and processing. Additionally, all formal and informal agreements to resolve complaints of misconduct (including Equal Employment Opportunity-related misconduct), and all formal and informal appeals of a disciplinary or adverse action, must be coordinated with the EMU before settlement terms or commitments may be communicated to complainants, grievants, or appellants.

If you have any questions regarding the policies and procedures related hereto, please contact Lia Colbert, Acting Director, Workforce Relations Division, Human Capital Office, at (202) 317-4390, or Max Goodman, Manager, EMU, at (202) 302-7571.

Attachments (3)

cc: All Executives  
All Executive Officers  
All Senior Managers  
All Front-Line Managers  
All Human Resources Managers  
All EEO Managers  
Associate Chief Counsel (General Legal Services)  
TIGTA Deputy Inspector General for Investigations



### **Policies and Procedures for Adjudicating Conduct-Related Matters Involving High-Level Employees**

1. *Applicability.* These policies and procedures apply only to *conduct-based* issues. [The respective Operations Branches within the Labor/Employee Relations Field Operations Office, Workforce Relations Division, Human Capital Office, provide services and support for all performance-based actions involving high-level employees at grades GS-15, IR-03, and IR-01, and conduct-based actions involving employees serving at grades GS-15, IR-03, and IR-01 via temporary promotion. The Office of Executive Services, Human Capital Office, provides services and support for all performance-based actions involving Executives and Executive Officers.]

2. *Referring Allegations of Misconduct.* All allegations of misconduct involving high level employees must be promptly referred to the Executive Misconduct Unit (EMU) or to the Treasury Inspector General for Tax Administration (TIGTA). The EMU can be reached at (202) 302-7571. Complaints may be filed with TIGTA at [http://www.treas.gov/tigta/contact\\_report.shtml#theform](http://www.treas.gov/tigta/contact_report.shtml#theform), or by phone at 1-800-366-4484. [Note: TIGTA Complaint Referral Memoranda (TIGTA Forms 2070 and 2070A) and Reports of Investigation (TIGTA Form 2076) involving a high-level employee, and received by the Business Unit from a source *other* than the EMU, must be forwarded immediately to the EMU.]

3. *Role of the EMU.* The EMU is the exclusive servicing Employee Relations (ER) office for all conduct-based issues involving high-level employees. On occasion, the EMU will request assistance and support from other ER components within the Human Capital Office or the Business Units. When a complaint referred to the EMU includes a co-subject who is not a high-level employee, the case associated with that employee will be adjudicated by that individual's servicing ER office, after adjudication of the primary case.

4. *Processing Misconduct Cases.* The EMU will receive and evaluate all complaints of misconduct against high-level employees, regardless of the source of the complaint (e.g., TIGTA, Employee Tax Compliance Branch, Credit Card Services Branch, IRS management official, Member of Congress, taxpayer, etc.).

The EMU may close conduct referrals at its own discretion; typically this occurs when an allegation of misconduct lacks sufficient information to justify administrative inquiry or formal investigation.

The EMU will analyze all referrals of potential or confirmed misconduct, before forwarding the cases to the responsible Business Unit Commissioner or Chief. When it is determined by the EMU that a misconduct matter requires the attention of the impacted Business Unit, the EMU will refer the matter with instructions, guidance, and/or recommendation. A due date for the Business Unit's recommendation for disposition will also be identified.

When appropriate, the EMU will consult with TIGTA; the Office of the Associate Chief Counsel, General Legal Services (GLS); and/or the AWSS Office of Equity, Diversity, and Inclusion Field Services for the purpose of assisting the responsible Business Unit with its case analysis and subsequent deliberations.

When an allegation of misconduct has been subjected to formal investigation by TIGTA, the resulting Report of Investigation (ROI) will be referred by the EMU to the responsible Business Unit for review and recommendation. The Business Unit may conduct additional administrative inquiry if deemed necessary or request that the EMU seek supplemental investigation by TIGTA and/or legal opinion from GLS. If an allegation of misconduct was not subjected to formal investigation by TIGTA, the EMU will determine whether to request a formal investigation or forward the matter to the responsible Business Unit for administrative inquiry (see attachments 2 and 3). In all cases, the Business Unit Commissioner/Deputy Commissioner or Chief/Deputy Chief must submit a written recommendation for disposition to the EMU by the identified response date. The EMU will advise as to whether the recommended disposition is consistent with previously adjudicated cases, involving comparable facts, circumstances, infractions, and grade level.

**Note: Before the matter is returned to the EMU, the recommendation for disposition must be discussed with the management official (typically the first or second-level supervisor) who will be responsible for issuing any recommended corrective action upon final approval. No discussion with**

**the affected employee may occur until the Business Unit is notified by the EMU that the recommended disposition is approved.**

When the adjudication process results in confirmation of misconduct by a high-level employee, and the Business Unit recommends either disciplinary action (i.e., Letter of Admonishment, Letter of Reprimand, or Suspension of 1 to 14 days) or adverse action (i.e., Suspension of 15 days or more, involuntary Change-To-Lower-Grade, or Removal from the Federal service), the EMU will refer the case and recommendation for disposition to the Chairperson, Executive Resources Board (currently, the Deputy Commissioner for Services and Enforcement) for approval to proceed with the initiation of the recommended administrative action. Cases involving Operations Support employees will be routed through the Deputy Commissioner for Operations Support.

**Note: Under no circumstances may corrective action be administered or may the matter be otherwise resolved without contacting the EMU in advance.**

5. *Penalty Selection.* General penalty guidelines are set forth in the IRS Guide to Penalty Determinations, IRS Document 11500 (Rev. 08-2012).

6. *Proposing and Deciding Officials.* Notices of proposed disciplinary or adverse action will be prepared by the EMU and issued by the employee's immediate supervisor (or second-level supervisor, when deemed appropriate). Disciplinary or adverse action decision letters will be prepared by the EMU and issued by the employee's first-level supervisor, second-level supervisor, or third-level supervisor, as deemed appropriate by the affected Business Unit Commissioner or Chief. However, the deciding official for actions involving Executives or Executive Officers cannot be delegated below the Business Unit Deputy Commissioner or Deputy Chief.

7. *Adjudication Actions.* The following dispositions are available:

Non-disciplinary Actions (not appealable):

Clearance Notification

Closed-Without-Action Notification

Oral Counseling (confined to first offenses of minor consequence)

Letter of Caution

Disciplinary Actions (may be appealed internally only, via the Agency Grievance System):

Letter of Admonishment (this is the lowest level of formal disciplinary action)

Letter of Reprimand

Suspension (less than 15 calendar days)\*

Adverse Actions (may be appealed externally only, pursuant to U.S. Merit Systems Protection Board regulations and procedures):

Suspension (greater than 14 calendar days)

Reduction in Grade and Pay\*

Removal from the Federal service

\* Note: by Federal regulation, these dispositions are not available to members of the Senior Executive Service.

8. *Disposition Letters.*

a. Clearance Notification:

The subject of a misconduct complaint may receive a Clearance Notification if: (a) he or she was interviewed during the investigation or administrative inquiry; (b) the allegation was unequivocally disproved; and (c) the subject or Business Unit requests such notification. If all conditions are met, the responsible Business Unit will issue such notification, orally or in writing, following consultation with the EMU. Confirmation that such notification was issued must be provided to the EMU.

b. Closed-Without-Action Notification:

The subject of a misconduct complaint may receive a Closed-Without-Action Notification if: (a) he or she was interviewed during the investigation or administrative inquiry; (b) the allegation was unresolved; and (c) the subject or Business Unit requests such notification. If all conditions are met, the responsible Business Unit will issue such notification, orally or in writing, following consultation with the EMU. Confirmation that such notification was issued must be provided to the EMU.

c. Letter of Caution:

A Letter of Caution may be issued to the subject of a misconduct complaint when the facts of the case suggest only a need for the subject to exercise maximum diligence in the future with respect to the identified issue (i.e., the offense is not attributed to carelessness, negligence or intentional disregard). The letter will be prepared by the EMU and issued by the employee's immediate supervisor (or second-level supervisor, when deemed appropriate).

d. Letter of Admonishment:

A Letter of Admonishment will be retained in the Employee Drop File (EDF) for 2 calendar years from the date it was received by the employee. The letter will be prepared by the EMU and issued by the employee's immediate supervisor (or second-level supervisor, when deemed appropriate).

e. Letter of Reprimand:

A Letter of Reprimand will be retained in the employee's Official Personnel Folder (OPF) for 2 calendar years from the date it was received by the employee (for tax-related offenses, Letters of Reprimand will be retained in the OPF for 5 calendar years). The letter will be prepared by the EMU and issued by the employee's immediate supervisor (or second-level supervisor, when deemed appropriate).

9. *Other Actions.*

a. High-level employees are ineligible for "Alternative Discipline."

b. An Executive who is reprimanded, suspended, or reduced in grade as result of misconduct, is ineligible for the following:

- a monetary performance-based award for the rating period in which the disciplinary action or adverse action was administered (e.g., performance bonus, Special Act Award, Presidential Rank Award, etc.);
- a performance-based salary adjustment, otherwise authorized under 5 CFR 534.404.

An Executive Officer who is reprimanded, suspended, or reduced in grade as result of misconduct, is ineligible for the following:

- a monetary performance-based award for the rating period in which the disciplinary action or adverse action was administered (e.g., performance bonus, Special Act Award, Quality Step Increase, etc.);

\*Note: Senior Managers (IR-01), Front Line Managers (IR-03), and GS-15 (NBU) employees are unaffected by Section 9.b.

10. *Settlement Agreements.* All formal and informal agreements to resolve a complaint of misconduct (including EEO-related misconduct), and all formal and informal appeals of a disciplinary or adverse action, must be coordinated with the EMU before a settlement commitment or terms of settlement can be communicated to the complainant, grievant, or appellant.

11. *Agency Grievance System.* High-level employees may grieve a disciplinary action via the Agency Grievance System (IRM 6.771.1). Such grievances will be referred directly to an external grievance examiner (i.e., private contractor). The grievance examiner's findings and recommendation will be submitted directly to the management official one level above the management official who issued the disciplinary action decision.

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ATTACHMENT 2

**STANDARDS FOR CONDUCT-BASED INQUIRIES**

**Independence:**

When appropriate and feasible, it is preferred that the fact-finding responsibility be assigned to an Executive outside the subject's chain-of-command. The inquiry should be conducted with thoroughness and impartiality.

**Scope of Work:**

Inquiries should provide an objective and thorough review of the issue(s). Facts should be sufficiently developed to ensure that an informed decision could subsequently be rendered. Guidance is available from the EMU, Workforce Relations Division, Human Capital Office, if desired.

Affirmative response to the following questions generally will ensure that the fact-finding was thorough:

Were all the issues in the referral addressed?

Were all key individuals (e.g., complainant, subject, witnesses) contacted? [With regard to interviews of IRS employees, the fact-finder has a right to full cooperation from the interviewee. Refusal to cooperate may result in disciplinary or adverse action. The fact-finder also has the right to expect truthful answers from the interviewee. The lack of candor, false statement, or misrepresentation may also result in disciplinary or adverse action.]

Were all relevant questions asked?

Were all relevant policies, regulations, and procedures researched?

Were legal opinions and technical advice solicited, when appropriate? [Requests for legal opinions unrelated to tax administration should be referred to the EMU.]

**Documentation Acquired in the Course of the Inquiry:**

A copy of all documentation acquired in the course of the inquiry must accompany the report of inquiry upon its release to the head of the Business Unit.

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ATTACHMENT 3

**REPORT OF INQUIRY**

**NAME, TITLE, GRADE OF SUBJECT:**

**TIGTA Case No. or ALERTS No.:**

**Inquiry conducted by:**

**Name of Management Official:**

**Position and Grade:**

**Organization:**

**Telephone Number:**

*Date of Report:*

**Scope of Inquiry:**

State the issue(s); name of complainant, if identified; name all individuals from whom information was obtained; identify the date on which each individual was interviewed; attach a copy of all documents acquired during the course of the administrative inquiry.

**Summary:**

State the facts as they relate to each issue. For each issue, provide an analysis of the facts and conclusions drawn from the analysis. Conclusions should state, with regard to each issue, whether the allegation was substantiated, disproved, or unresolved.

*A recommendation for disposition should NOT to be inserted in the Report of Inquiry. Rather, it should be delivered orally to the Business Unit Commissioner or Chief, if desired or requested, but only if the fact-finder is in the subject's chain-of-command.*

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PREPARED STATEMENT OF HON. RON WYDEN,  
A U.S. SENATOR FROM OREGON

Whenever I talk with Oregonians in meetings or town halls, the conversation nearly always comes down to the same core issue—the struggling middle class. Years after economists first said the recession officially ended, too many middle-class Americans feel like they're standing on quicksand because the recovery has yet to reach them. So the challenge facing policymakers is putting America's middle class on solid economic ground—growing their paychecks and ensuring that our recovery reaches everybody across the country.

That challenge will be top of mind at each of the three hearings the Finance Committee is holding this week. Tomorrow and Thursday, the committee will talk with HHS Secretary Burwell and Treasury Secretary Lew about the administration's plans to save Americans' money on health care, create jobs, increase wages, and invest in the middle class. Today, the committee has an opportunity to discuss the status of America's accounting department—the Internal Revenue Service—with IRS Commissioner John Koskinen.

With W-2 forms in the mail and tax season beginning, the nation's annual headache is setting in. Taxpayers today live in two separate worlds. In one world, a middle class office employee pays taxes directly out of her wages and is subjected every spring to the painstaking process of filing returns. There are no complicated tax avoidance strategies at her disposal—no shelters or vehicles for her to hide income. Meanwhile, in the other world, teams of accountants pry open loopholes hidden in the tax code, and the line between right and wrong is murky at best.

The inherent unfairness of our tax system is a blow that falls hardest on the middle class. And it takes a number of forms. The most obvious is that every year, families spend more time and money filing their taxes. People are concerned about compiling all their records, completing all the forms and filing correctly. Unfortunately, the tax code itself hasn't gotten any simpler, and the lack of resources at the IRS slows service to a crawl. Nina Olson, the independent IRS Taxpayer Advocate, calls this the "most serious problem" facing taxpayers.

When people call into IRS help lines, they sit in long queues listening to hold music. Protections against identity theft are delayed, and taxpayers who worry they might be victims of scams can't get the timely assistance they need. Families depending on their refund to help cover the mortgage or tuition are left waiting.

There's a second issue to consider today. According to the IRS, nearly \$400 billion in taxes go unpaid every year. It's called the tax gap. One of its biggest causes is the dishonesty of tax cheats and scammers who avoid paying what they owe.

Who's getting short shrift as a result? The middle-class wage earners whose taxes come straight out of their paychecks. Honest taxpayers have to make up the difference when scofflaws dodge their responsibilities, and that's not right. But until Congress simplifies and restores fairness to our broken tax code, multinationals and people with high-priced accountants will continue to find loopholes.

There's no question that the IRS could make better use of the resources it has. That's true for every federal agency, every private business, and even Congress itself. It has also been acknowledged by Commissioner Koskinen and his predecessor.

Meanwhile, policymakers cannot lose sight of the biggest challenge facing Congress today, which is putting the middle class on solid economic ground. There will be many more opportunities ahead for this committee to work on a bipartisan basis with Commissioner Koskinen and the IRS to make the system work better for middle class families—including through comprehensive tax reform.

The goal should be fairness. Taxpayers should no longer be divided into separate worlds, one of which carries a much heavier burden than the other. I look forward to working with Commissioner Koskinen and the committee to making that our reality.

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## COMMUNICATION

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### STATEMENT FOR THE RECORD OF THE NATIONAL ASSOCIATION OF COLLEGE AND UNIVERSITY BUSINESS OFFICERS

This statement is submitted for the record on behalf of the more than 2,100 public and nonprofit colleges and universities belonging to the National Association of College and University Business Officers. NACUBO represents chief financial officers and their staff at member institutions and our mission is to advance sound financial management and business practices of higher education institutions in fulfillment of their academic missions. Our members take their responsibilities for filing IRS information returns seriously and strive to the best of their abilities to comply with agency rules and regulations.

Today provides an opportunity, as the Senate Finance Committee addresses the current state of operations and the budget of the Internal Revenue Service, to address an issue that gets to the heart of the current allocation of IRS resources. We write this statement in order to draw attention to an example of government wheel-spinning that for the past few years has burdened already squeezed college compliance offices. IRS has unnecessarily created an endless annual cycle of proposed fines, waiver requests, notices of delayed response, and eventually confirmation of waivers. This is bureaucracy at its worst.

On behalf of colleges and universities across the country, NACUBO requests that the Internal Revenue Service stop issuing penalty notices to colleges and universities related to missing or inaccurate taxpayer identification numbers (TINs) on 2012 Forms 1098-T and take steps to rescind the notices that have been issued. Under existing rules, institutions must solicit a TIN at least once a year from certain enrolled students, but are not responsible if students fail to respond or respond with incorrect information.

In August 2013 the IRS began asserting penalties against a large number of colleges and universities for filing Forms 1098-T with incorrect or missing TINs. These proposed penalties for the 2011 tax year generated unnecessary confusion for both the IRS and the regulated community.

Following an outcry, IRS decided to waive such penalties for the 2011 tax year. However, many schools still have yet to receive official notice that their fines for 2011 have been waived, despite the fact that the IRS announced the blanket waiver for 2011 one year ago.

Hundreds of campuses again received penalty notices addressing the 2012 tax year. Given that Forms 1098-T for 2012 were all filed long before the proposed fine notices were issued for the 2011 tax year, and also given that nothing has changed that should cause the IRS to come to a different outcome for 2012, it is unclear why the IRS is committed to repeating the cycle. We strongly believe that penalties should be waived until a long-term solution has been identified.

#### BACKGROUND

Section 6050S of the Internal Revenue Code requires colleges and universities to report to the IRS, and to students, certain information on enrollment, tuition and related expenses, and scholarships related to claims for education deductions or credits. Form 1098-T is used for this purpose. It requires the college or university to identify the student by name, address, and TIN. The regulations at 26 CFR 1.6050S-1(e) allow for a waiver of penalties for filing Form 1098-T with a missing or incorrect TIN if the failure is due to reasonable cause (such as the student's failure to provide a correct TIN) and the institution acted in a responsible manner.

Under the IRS regulations, an institution acts in a responsible manner if it solicits a TIN at least once a year from anyone with a missing or incorrect TIN.

In the course of complying with the tuition reporting requirements, it is inevitable that colleges and universities will submit Forms 1098-T with incorrect TINs because they must rely on student input to obtain TINs and have no way to verify TINs prior to filing. *By statute, colleges and universities are not permitted to use IRS-approved TIN matching services to verify TINs reported on Form 1098-T.* This is because the IRS generally may not disclose a taxpayer's name, TIN, or other return information under Section 6103. Although there is a limited exception under Section 3406 that enables payers of reportable payments subject to backup withholding to verify TINs with the IRS prior to filing, tuition reporting does not qualify for this exception. As a result, it would be a violation of taxpayer confidentiality under Section 6103 for the IRS to permit colleges and universities to use TIN matching for tuition reporting.

Further, some students do not have, or choose not to provide, a TIN. With the popularity of dual enrollment programs increasing, particularly at community colleges, high school students may comprise a significant population of those with missing TINs. However, the rules require institutions to file Forms 1098-T for these students regardless of missing or inaccurate numbers. Foreign students may or may not have a TIN. In this context, it is inappropriate to assert penalties on colleges and universities for filing Forms 1098-T with incorrect TINs.

Notably, we appreciate the step IRS made to include guidance under section 6050S of the Internal Revenue Code regarding information reporting on tuition and related expenses on the 2014–2015 Priority Guidance Plan.

#### RECOMMENDATIONS

It is manifestly unfair to penalize colleges and universities for erroneous information that is beyond their control and which they cannot independently verify. The IRS should promptly issue another blanket waiver for proposed fines associated with 2012 Forms 1098-T and not repeat this mistake in future years. There are no material differences between the 2011 and 2012 tax years that could justify disparate treatment. Other possible solutions going forward include:

1. The IRS should issue new guidance to reinstate its past practice of forbearance until a long-term solution has been identified. Until 2013, the IRS's long-standing policy had been not to assert penalties against colleges and universities for incorrect TINs on Form 1098-T.
2. The IRS should revise the process used to file Forms 1098-T with the IRS to allow the filing organization to affirmatively certify that it has "acted in a responsible manner" and met the standards for soliciting TINs from its students.
3. The IRS should revise its regulations at § 1.6050S-1 to allow higher education institutions to *not* file a 1098-T for students who fail to provide a TIN. Institutions could be required to notify such students that they will not receive a form unless they provide a TIN by a certain date.

We are very willing to work with Congress and with the Service to find a solution, eliminate the morass of red tape and identify both short- and long-term alternatives to the current information-reporting enforcement program.

