WRITTEN TESTIMONY OF
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SENATE APPROPRIATIONS COMMITTEE
SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT
ON THE IRS BUDGET
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INTRODUCTION

Chairwoman Capito, Ranking Member Coons, and Members of the Subcommittee, thank you for the opportunity to appear before you today to discuss the IRS's budget and current operations.

Let me start by saying we look forward to working with Congress as you continue to assess the IRS's appropriate funding level. It is important to note that, since my term as IRS Commissioner ends in November, all but a few weeks of the agency's Fiscal Year (FY) 2018 budget will cover the term of the next IRS Commissioner. I want to do everything I can to help ensure that the budget situation for the agency will be as strong as possible for the new Commissioner.

The IRS remains very appreciative of Treasury Secretary Mnuchin's support for the IRS to have appropriate resources, and in particular for upgrading our information technology (IT) systems. We also strongly support the Administration's efforts to reduce the federal budget deficit. We recognize that the IRS must always appropriately analyze and control our expenditures, and continue to be as efficient as possible with the funding granted by Congress.

At the same time, I would note that the IRS remains one of the most cost-effective investments in the federal government; resources invested in the IRS increase revenue collections. This unique and critical role is vital to the function of the government and to keeping the nation and economy strong. In FY 2016, the IRS collected more than $3.3 trillion in tax revenue, processed more than 244 million tax returns and other forms, and issued more than $426 billion in tax refunds. The IRS's enforcement programs collected more than $54.3 billion in FY 2016, a return on investment (ROI) of about $5 for every dollar invested in the agency.

While we will continue to look for efficiencies in our operation, it is important to recognize that the IRS remains one of the most efficient tax administrators in the world. For every $100 collected in taxes, the IRS spends about 35 cents, which is far less than most other developed countries, according to statistics compiled by the Organization for Economic Cooperation and Development (OECD).

As the IRS budget has declined over recent years, we have consistently found ways to increase our efficiency to meet expanding workloads and new challenges. From 2010 to 2015, the number of returns filed grew by more than 10 million (or nearly 7 percent).

Further increasing our workload, the IRS during this period has had to implement a number of significant legislative mandates, nearly all of which came with no additional funding. This list includes: the Affordable Care Act (ACA); the Foreign Account Tax Compliance Act (FATCA); the Achieving a Better Life Experience (ABLE) Act; a new certification program for professional employer organizations; reauthorization of the Health Coverage Tax Credit (HCTC); the registration requirement for newly created 501(c)(4) organizations; and the Private Debt Collection program. Legislative mandates carry significant costs, in particular the technological changes required to successfully integrate them into the tax system.

Because more than 70 percent of the IRS's budget is personnel, the agency has dealt with the funding cuts through an exception-only hiring freeze that has been in effect since FY 2011. This has left us unable to replace most employees who retire or leave for other jobs in government or the private sector. As a result, the agency has lost about 18,000 full-time employees since 2010.

I am concerned that continued erosion of the IRS workforce will threaten the agency's effectiveness and its ability to provide appropriate taxpayer service, enforcement of the tax laws, and ultimately, our ability to collect the revenues the government depends upon for operations.

Against this backdrop, we are appreciative of the funding flexibility provided by Congress in 2016, which continued in 2017 to improve taxpayer service, increase cybersecurity and improve our efforts against identity theft.

In the cybersecurity area, we implemented the use of monitoring and other capabilities that are more sophisticated than what we had used previously. This has helped us detect suspicious activity in our various online tools and applications more quickly.

In regard to identity theft, we put many new taxpayer protections in place for the 2016 tax filing season that produced significant results. We had fewer false returns entering our systems, fewer fraudulent refunds issued, and fewer tax-related identity theft victims. Most important, the number of people who reported to the IRS that they were victims of identity theft declined from 698,700 in Calendar Year 2015 to 376,500 in 2016 – a drop of 46 percent. Preliminary indications are that this number is again declining in 2017.

THE PRESIDENT'S FY 2018 BUDGET

The President's FY 2018 Budget request for the IRS is $10.975 billion, which is $260 million, or 2.3 percent, below the FY 2017 enacted budget. The IRS will continue to seek less costly ways of delivering taxpayer service and maintaining enforcement using technology, training and internal efficiencies. Major areas outlined in the President's Budget request include the following:

Operations Support. A priority in the President's Budget is helping the IRS improve information services by addressing its antiquated IT systems. Approximately 63 percent of IRS IT hardware systems are aged and out of warranty, and 32 percent of software products are two or more releases behind the industry standard, with 15 percent more than four releases behind. The importance of keeping systems updated was demonstrated recently with the spread of the "WannaCry" virus to IT systems around the world.

The President's Budget request includes $3.9 billion for operations support. Within that total, $2.07 billion is allocated for information services, $216.1 million, or 11.6 percent, above the FY 2017 enacted budget. This funding will allow the IRS to take the initial steps needed to bring our IT infrastructure up-to-date.

With the growing reliance on IT as an integral part of the solution to provide improved taxpayer service and enforcement, the IRS will continue to modernize to harness new information delivery models and manage data. Infrastructure modernization is necessary to increase agility, efficiency and service quality, ultimately reducing operational cost.

Taxpayer Services. The President's Budget includes $2.21 billion for taxpayer services, which is $153.4 million, or 6.5 percent, below the FY 2017 enacted budget. While the IRS will continue to provide service to taxpayers across all channels, we will emphasize improving and expanding the use of online tools and offerings such as virtual tax assistance sites, which will help the agency operate in a cost-effective manner.

The IRS has, in fact, been working to increase our online offerings for several years, in response to increasing taxpayer demand. We provide a wealth of tax information on IRS.gov, which was visited more than 500 million times during FY 2016, and more than 354 million times so far in FY 2017. Taxpayers use IRS.gov to get forms and publications, find answers to their tax questions, and perform transactions such as paying their tax bill. The most heavily used part of our website is the "Where's My Refund?" electronic tracking tool, which was used about 300 million times in FY 2016, and more than 264 million times already this year.

The IRS will continue working toward a more proactive and interactive relationship with taxpayers by enhancing and expanding our communications with them. This includes offering taxpayers and tax professionals more services, tools and support that are both innovative and secure, and specific to their needs, especially in relation to online and virtual interactions.

Enforcement. The President's Budget includes $4.71 billion for enforcement programs, which is $153.5 million, or 3.2 percent, below the FY 2017 enacted budget.

The IRS remains committed to increasing compliance and reducing the tax gap, while minimizing burden on the vast majority of taxpayers who pay their taxes accurately and on time. The tax gap represents the difference between taxes owed and taxes paid on time. In FY 2016, the IRS released updated tax gap estimates for tax years 2008 through 2010, and found that the annual average gross was an estimated $458 billion, and the estimated voluntary compliance rate was 81.7 percent.

Business Systems Modernization. The President's Budget includes $110 million for business systems modernization, which is $180 million, or 62.1 percent, below the FY 2017 enacted budget. As noted above, this decline is a result of reallocating funding to IT infrastructure systems to decrease the backlog of deferred software and hardware updates, which is a critical priority, and must be accomplished before development and modernization of new systems.

With the FY 2018 request, the IRS will continue operating the Return Review Program (RRP) which has significantly enhanced fraud detection capabilities. In FY 2018, RRP will make a wider array of data available to other systems for expanded fraud detection.

The IRS will also continue developing web applications to simplify the taxpayer's online experience, provide secure digital communications and add more interactive capabilities to existing web self-service products. This includes continuing the development of online account capabilities for taxpayers. The initial features of the online account, launched during FY 2017, include allowing taxpayers to check if they have a balance due, make payments and see prior payment and other tax records.

LEGISLATIVE PROPOSALS IN THE PRESIDENT'S BUDGET

Along with the funding request, we are also asking for Congress's help legislatively. In that regard, let me highlight several important legislative proposals in the President's FY 2018 Budget that would improve tax administration and support the IRS in fulfilling its mission:

Streamlined critical pay authority. The IRS Restructuring and Reform Act of 1998 increased the IRS' ability to recruit and retain a small number of key executive-level staff by providing the agency with streamlined critical pay authority. This allowed the IRS, with approval from Treasury, to move quickly 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. Executives hired under this authority included our former Chief Information Officer, a senior cybersecurity expert, our system architect, the director of our online systems development team and other senior IT executives. After having been renewed several times by congressional appropriators, this authority expired at the end of FY 2013 without being renewed. The President's FY 2018 Budget proposes reinstating this authority through FY 2021. It is my hope that this critical program, which ran effectively for 14 years before it expired, will be renewed.

Correction procedures for specific errors. Under current law the IRS has authority in limited circumstances to identify certain computation mistakes or other irregularities on returns and automatically adjust the return for a taxpayer. 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 a proposal in the President's Budget to replace the existing specific grants of this authority with authority to correct specific errors instead. This would allow the IRS to fix errors where we have reliable information that a taxpayer has an error on their return in areas such as the Earned Income Tax Credit (EITC) program, educational tax credit programs or child tax credit programs.

Authority to require minimum qualifications for return preparers. The President's Budget proposes providing the Secretary with authority to require all paid tax return preparers to have a minimum knowledge of the tax code. Requiring all paid preparers to keep up with changes in the Code would help promote high quality service from return preparers, improve voluntary compliance, and foster taxpayer confidence in the fairness of the tax system.

Chairwoman Capito, Ranking Member Coons and Members of the Subcommittee, that concludes my statement. I would be happy to take your questions.