



Statement of
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Prepared for the Committee on Finance, United States Senate
Regarding the Committee’s Hearing on
“House Republican Supplemental IRS Funding Cuts: Analyzing the Impact
on Federal Law Enforcement and the Federal Deficit”

May 16, 2023

Chairman Wyden, Senator Thune, and Members of the Committee:

I am honored by your invitation to present the following comments concerning the issues of Internal Revenue Service (IRS) funding, particularly as it relates to enforcement of federal tax laws and overall federal finances.

Introduction

My name is Pete Sepp and I am President of National Taxpayers Union (NTU), a non-partisan citizen group founded in 1969 to work for less burdensome taxes, more efficient, accountable government, and stronger rights for all taxpayers. More about our work as a non-profit grassroots organization is available at www.ntu.org.

Although we advocate for many structural changes to the tax system, from the comprehensive to the incremental, one common aspect on which NTU often specifically focuses is the *administrability* of such proposals. As policymakers define the rates, bases, deductions, credits, and other features of a tax system, what will the practical impact be on taxpayers’ lives and their rights? Unless this question is adequately addressed, the result will be a tax system that burdens all and serves none. Taxpayers will be more fearful or mistrustful of their government, revenue officials will encounter greater difficulty in performing their public service, tax practitioners will become increasingly frustrated with complex rules, and all sectors of the economy will pour too many productive resources into compliance tasks that only marginally affect actual compliance.

For these reasons, throughout its history NTU has led efforts in support of Congressional legislation to improve operations of the Internal Revenue Service (IRS) and provide greater balance in the tax law enforcement process. During the late 1970s and 1980s, NTU informed Congress of taxpayers who experienced IRS maladministration firsthand, as well as organized a large coalition of civil liberties organizations that successfully persuaded Congress to enact the first “Taxpayers’ Bill of Rights” as part of the Technical and Miscellaneous Revenue Act of 1988.

In 1996 and 1997, NTU’s then-Executive Vice President David Keating was named to the National Commission on Restructuring the Internal Revenue Service (“Restructuring Commission”), a federal panel whose recommendations later became the basis for the most extensive IRS overhaul in a generation.¹

More recently we worked with the IRS National Taxpayer Advocate (NTA) and Congress in promulgating and finally codifying (in 2015) a set of 10 fundamental taxpayer rights. We also led a large coalition of organizations to formulate and pass through Congress the bipartisan Taxpayer First Act of 2019 – and gratefully participated in the extensive stakeholder consultation process after enactment that led to the production of the comprehensive Taxpayer First Act Report of early 2021.

Since that time, NTU has also urged a cautious, deliberative approach – but not wholesale opposition – to proposals for increased IRS funding. As I wrote in the *New York Times* in October 2021, supporting additional IRS funding:

More resources for customer service, taxpayer rights safeguards, a functioning Oversight Board, actionable and regularly updated research on the tax gap and innovative approaches such as the recently proposed enforcement fellowship pilot program are all solutions that should unite Washington.²

Thus, we do not appear before the Committee to advocate blocking all additional funding for the IRS, and would indeed argue that locking in certain multi-year appropriations for IRS investments (e.g., Information Technology) is sensible.³ In fact, it is this history of my

¹ For background, see National Commission on Restructuring the IRS. “A Vision for a New IRS.” June 25, 1997. Available from:

<https://cybercemetery.unt.edu/archive/natcommirs/20160104232208/http://www.house.gov/natcommirs/object.htm>.

² Sepp, Pete. “I’m the President of the National Taxpayers Union. Be Careful with I.R.S. Reform.” *New York Times*. October 18, 2021. <https://www.nytimes.com/2021/10/18/opinion/tax-irs-reform.html>.

³ In 2021, former IRS Commissioner John Koskinen observed the following about the \$80 billion of additional IRS funding contained in the Biden Administration’s American Families Plan: “I’m not sure you’d be able to efficiently use that much money.” Rappoport, Alan, and Tankersley, Jim. “Biden Seeks \$80 Billion to Beef Up IRS Audits of High Earners.” *New York Times*. April 27, 2021. <https://www.nytimes.com/2021/04/27/business/economy/biden-american-families-plan.html>.

organization that informs much of the remarks to follow about the present and future circumstances of IRS funding and federal finances.

Here I wish to acknowledge the outstanding contributions to this testimony from several of my colleagues at National Taxpayers Union and National Taxpayers Union Foundation: Joe Bishop-Henchman, Executive Vice President of National Taxpayers Union Foundation, Demian Brady, Vice President of Research, National Taxpayers Union Foundation, Andrew Lautz, former Director of Federal Policy, and Andrew Wilford, Director of the Interstate Commerce Initiative, National Taxpayers Union Foundation. Their research and writing has greatly informed and improved the document you are reading today.

Political Realities: Both Parties Must Lead on Sound Tax Administration, and Both Have Shown They Can Do It Together

Before turning to the details of the topic at hand, NTU urges all Members of the Committee to recognize several important, yet inescapable political realities confronting Washington today.

First, the votes in the House of Representatives to claw back the IRS funding designated for “enforcement” in the Inflation Reduction Act (IRA) are as far in the legislative process as these proposals will go – it cannot be realistically argued that they could pass the Senate intact, much less survive a Presidential veto. Nor, given the political state of Congress, will the appropriations or reconciliation processes permit the House Republican majority to make massive IRS budget reductions for the next two fiscal years. Even if that political state changes in 2025, as a practical matter no significant alterations to the current IRS funding amount would be likely until Fiscal Year 2026.

Knowing this, opponents of the IRA must turn their immediate attention to *how* this amount should best be spent.

Second, both the House and Senate Democratic caucuses have historically insisted upon strict Congressional planning, guidance, and oversight of federal law enforcement programs and the agencies carrying out those programs. For example, when several PATRIOT Act provisions regarding surveillance were up for renewal in 2011, Rep. John Conyers (D-MI) said:

Section 215 of the Patriot Act allows a secret FISA court to authorize our government to collect business records or anything else, requiring that a person or business produce virtually any type [of] record. We didn't think that that was right then. We don't think it's right now. This provision is contrary to traditional notions of search and seizure which

require the government to show reasonable suspicion or probable cause before undertaking an investigation that infringes upon a person's privacy.⁴

In 2016, after Congress learned of civil asset forfeiture laws being wielded unfairly against taxpayers, the late Rep. John Lewis (D-GA) joined with then-Rep. Peter Roskam (R-IL) in support of taxpayer protections in the DUE PROCESS Act. Chairman Lewis said at the time, "I have never, ever seen in a very long time, this degree, this spirit of togetherness. On this issue, we are on one accord."⁵ Chairman Lewis, who I had the honor to meet in 2017, inspired our organization when he said of the Taxpayers First Act, "even in the most difficult times, we can come together as a nation, as a people and as a Congress to accomplish important things for the American people."⁶ Democrats should be proud of their tradition in supporting taxpayer rights, counting among other leaders on this issue David Pryor (D-AR), J.J. Pickle (D-TX), and Harry Reid (D-NV).

With this history, supporters of the IRA must turn their immediate attention to applying the same general philosophy behind these examples from other parts of federal law enforcement, to how the IRS should operate when it acts in a law enforcement capacity.

The third reality is more pleasant and hopeful. For decades, NTU has seen bipartisan collaboration and cooperation on a variety of tax administration initiatives to improve the way the IRS works while enhancing compliance with the law and protecting taxpayer rights. Our testimony will provide abundant opportunities for building upon this bipartisan comity in a later section.

Historical Reality: IRS Transformation Won't Succeed without Congressional Planning, Oversight

But why should bipartisan comity on tax administration matter at this particular point in time? The history of IRS funding provides an instructive, and urgent, reason why.

Although much has been made of IRS budget reductions as if they followed a straight line according to which party was in power, on an inflation-adjusted basis, the history of IRS funding from 1992-2022 is best described as peaks and valleys. After hitting a low in 1997, IRS resources increased significantly through the year 1999, recovering after a dip to reach more than \$14 billion (in 2022 dollars) in 2006. Then began an uneven path to a new height of nearly \$15

⁴ See, [ontheissues.org](https://www.ontheissues.org/MI/John_Dingell_Homeland_Security.htm). Debate over RESTORE ACT. March 14, 2008. https://www.ontheissues.org/MI/John_Dingell_Homeland_Security.htm.

⁵ See, Sibilla, Nick. "After Sending Armed Agents to Seize Bank Accounts, IRS Announces New Policy to Return Assets." *Forbes*. June 24, 2016. <https://www.forbes.com/sites/instituteforjustice/2016/06/24/irs-structuring-policy/?sh=393caba51a87>.

⁶ See, Sepp, Pete. "An Appreciation: Congressman John Lewis, 1940-2020. National Taxpayers Union. July 27, 2020. <https://www.ntu.org/publications/detail/an-appreciation-congressman-john-lewis-1940-2020>.

billion in 2011, and once more taking considerable declines until 2019. Today, after accounting for inflation, IRS funding is only moderately higher than it was five years ago.⁷

It should be noted that two of the three major IRS funding ramp-ups occurred after enactment of key IRS reform laws (the IRS Restructuring and Reform Act, or RRA '98 and the Taxpayer First Act, or TFA '2019). Both bills passed with near-unanimous margins in Congress. The third was connected to several events, including implementation of the American Recovery and Reinvestment Act of 2009 and the Affordable Care Act of 2010.

The point we wish to emphasize here is that major investments in the IRS's capacity have been preceded by extensive legislating from Congress, in close consultation with IRS leadership. RRA '98, for example, was fundamentally shaped by the 18-member National Commission on Restructuring the IRS, and appointed by Congress and the Executive Branch. According to its nearly 200-page report, over the course of a year of operation:

The Commission received extensive input from American taxpayers and experts in the IRS and tax system, holding 12 days of public hearings and spending hundreds of hours in private sessions with public and private sector experts, academics, and citizen's groups to review IRS operations and services. In addition to holding three field hearings... the Commission met privately with over 500 individuals, including senior-level and front-line IRS employees across the country... The Commission also received continuous input from stakeholder groups and congressional representatives, and conducted research and surveys to better understand IRS operations and gauge the American public's view of the IRS. Finally, the Commission reviewed thousands of reports and documents on IRS operations, management, governance, and oversight.⁸

The resulting legislation based in part on this report also involved numerous hearings and markups by multiple Committees and Subcommittees, resulting in a 184-page final bill which, in turn, helped to guide innumerable revisions to strategic plans, Internal Revenue Bulletins, and Internal Revenue Manual procedures.

By contrast, Title I, Part 3 of the Inflation Reduction Act contained all of nine paragraphs outlining \$79.6 billion in tax administration-related funding. Just three of those nine paragraphs explain how \$78.9 billion (99 percent) of the total should be spent.

⁷ See Brady, Demian. "What the IRS's New Enforcement Budget Means for Taxpayers." National Taxpayers Union Foundation. September 21, 2022. Retrieved from: <https://www.ntu.org/foundation/detail/what-the-irss-new-enforcement-budget-means-for-taxpayers>. Also, Bishop-Henchman, Joseph. "Transforming the Internal Revenue Service." Cato Institute Policy Analysis No. 942. April 11, 2023. <https://www.cato.org/policy-analysis/transforming-internal-revenue-service>.

⁸ National Commission on Restructuring the IRS. "A Vision for a New IRS." June 25, 1997. Available from: <https://cybercemetery.unt.edu/archive/natcommirs/20160104232208/http://www.house.gov/natcommirs/object.htm>.

Some would argue that the IRS funding in the Inflation Reduction Act was never intended to be as transformational as RRA '98. Perhaps this was initially the case, given the brevity of instructions Congress provided about the resource infusion. As we note below, the IRA, utilizing the reconciliation process, seemed much more focused on “hitting a number” to achieve a desirable 10-year budget score than transforming the IRS.

Whatever the intentions during legislative negotiations, it is now abundantly clear that advocates of the IRA are describing the new money in sweeping terms. In transmitting the IRA Strategic Operating Plan to Secretary Yellen, Commissioner Werfel himself wrote that “the contents of this plan provide a vision for the future of federal tax administration.” The Plan itself grandly notes that the IRA funding is “a historic opportunity to transform the administration of the tax system and the services provided to taxpayers.”

Plenty of discussions continue to take place in the policy world over the proper level of IRS funding as well as the best mix between taxpayer service, compliance initiatives, business systems, and other items.

Regardless of how those discussions land, NTU offers this reminder: *Never before has the IRS – or, to our recollection, any existing federal agency – received such a large boost of funding in percentage terms with so little planning, safeguards, or prospects of outside managerial oversight.* It is now well past time for every Member of Congress to recognize this fact and act accordingly.

Managerial Reality: Compliance Is the Goal, Not “Enforcement”

The word “enforcement” has become a common yet unfortunate shorthand in Washington for the goal of obtaining better *compliance* with the tax laws. The choice of words matters, because it predefines the direction of a conversation that ought to pursue many paths to a desirable destination. “Enforcement” should never be an end in itself, or a performance metric to justify budgets. Otherwise, policymakers will simply focus on increasing audit rates, math error notices, criminal convictions, and other tactics without being held accountable for a measurement that is actually meaningful: compliance with tax laws that is less difficult, less expensive, and more sustainable than it is today.

This definition should have currency even for those who believe that the “investment” of taxpayer dollars into “enforcement” was the primary reason for Title I, Part 3 of the IRA. The less money the IRS spends – and the more methods employed beyond traditional “enforcement” – to obtain compliance, the better the fiscal result will be.

But the language of the IRA itself points to the problem of distinguishing ends and means elucidated above. Title I, Part 3 is helpfully entitled, “Funding the Internal Revenue Service and Improving Taxpayer Compliance.” After that point, the minimal descriptions of where the

funding shall be directed fail to capture how compliance is a multifaceted issue. For example, the relatively small amount for “taxpayer services” describes “pre-filing assistance and education” along with “taxpayer advocacy services” as allowable expenses under the section. The following section, with a very large amount for “enforcement,” describes “activities...to determine and collect owed taxes” as well as “legal and litigation support.”

This categorization fails to appreciate the interrelatedness of “taxpayer services” and “enforcement” to compliance. From Earned Income Credit claimants all the way up to Form 1120 filers reporting Controlled Foreign Corporation activities, “pre-filing assistance and education” can forestall numerous situations that could result in noncompliance. Both the “legal and litigation support” and “activities to determine and collect owed taxes” could easily lead taxpayers to lean more heavily on “taxpayer advocacy services.” In other words, improved taxpayer services can go a long way to improve compliance with our tax laws, yet certain enforcement activities can further increase demands for taxpayer services.

National Taxpayer Advocate Erin Collins put it best when she observed:

The most efficient way to improve compliance is by encouraging and helping taxpayers to do the right thing on the front end. That is much cheaper and more effective than trying to audit our way out of the tax gap one taxpayer at a time on the back end.⁹

The division of funding also illustrates how the funding gap between “taxpayer services” (\$3.18 billion) and “enforcement” (\$45.6 billion) is even worse than it appears. High-profile IRS actions since passage of IRA funding in the area of services have primarily focused on “front-end” matters such as hiring more telephone operators and addressing return processing backlogs. What will be left for pre-filing education and taxpayer advocacy services after these flashier improvements have been fully funded? As the next section explains, the financial reckoning is approaching quickly.

Fiscal Reality: IRS Burn Rates on Customer Service and Modernization Should Be Concerning – Especially for “Enforcement”

While policymakers, reporters, and other stakeholders have devoted much attention to the supplemental IRS “enforcement” funding included in the IRA, NTU has also been closely tracking the agency’s use of supplemental customer service and modernization funding. There is a bipartisan interest in ensuring that the IRS both improves the taxpayer experience and upgrades severely outdated information technology infrastructure.

⁹ Waggoner, Martha. “Taxpayer services should get more of that \$80 billion, advocate says.” *Journal of Accountancy*. March 17, 2023. <https://www.journalofaccountancy.com/news/2023/mar/taxpayer-services-get-more-80-billion-advocate-says.html#:~:text=%22The%20most%20efficient%20way%20to,time%20on%20the%20back%20end.%22>.

In its IRA Strategic Operating Plan released in April, the IRS estimated that it would obligate around \$1.65 billion of its supplemental Taxpayer Services funding by September 30, 2024.¹⁰ This means that more than half (52 percent) of the agency’s allocation for enhanced Taxpayer Services activities will have been obligated in the first three fiscal years of the 10-year allocation.¹¹ Similarly, the IRS projects it will have obligated nearly 35 percent (\$1.66 billion out of \$4.75 billion) by September 30, 2024, just three years into the 10-year allocation.¹²

By comparison, the IRS will have only obligated 13.6 percent of its supplemental Operations Support funding (\$3.46 billion out of \$25.33 billion) and 3.9 percent of its supplemental Enforcement funding (\$1.78 billion out of \$45.64 billion) by the end of fiscal year (FY) 2024.¹³

The IRS has many ambitious goals and initiatives in its Strategic Operating Plan focused on customer service and modernization. Its very first objective is to “[d]ramatically improve services to help taxpayers meet their obligations and receive the tax incentives for which they are eligible,” and its second objective is to “[q]uickly resolve taxpayer issues when they arise.”¹⁴

The agency outlines 12 initiatives under its first objective, including such important efforts as “be[ing] able to file all documents securely and exchange correspondence electronically” and providing “greater upfront clarity and certainty additional guidance on tax issues.”¹⁵ The IRS outlines seven initiatives under the second objective, including “provid[ing] taxpayers with timely and tailored post-filing treatments to resolve issues and omissions on their tax returns” and “send[ing] taxpayers notices they can understand, delivered in ways they prefer, with clear explanations of issues and steps to resolution.”¹⁶

NTU agrees with many of these initiatives and would like to see the IRS succeed. Indeed, success could result in a vastly improved taxpayer experience with the IRS, the central goal of the bipartisan, recently enacted Taxpayer First Act of 2019.

But as explained in the previous section, even those who support an “enforcement”-heavy approach to IRS budgets should be concerned about the agency’s projected burn rate for supplemental Customer Service and Modernization funding. After all, the Strategic Operating Plan for the IRS acknowledges that “all our efforts as outlined in this plan – including in the

¹⁰ IRS. (April 2023). “Internal Revenue Service Inflation Reduction Act Strategic Operating Plan: FY2023 - 2031.” Retrieved from: <https://www.irs.gov/pub/irs-pdf/p3744.pdf> (Accessed May 11, 2023.)

¹¹ The first of 10 fiscal years, FY 2022, was also a noticeably short period for the IRS to obligate funding in the IRA. President Biden signed the Inflation Reduction Act into law on August 16, 2022, and FY 2022 ended just six weeks later, on September 30, 2022.

¹² Internal Revenue Service, *supra* note 10.

¹³ *Ibid.*

¹⁴ *Ibid.*

¹⁵ *Ibid.*

¹⁶ *Ibid.*

areas of customer service, issue resolution, and effective enforcement – will increase overall tax compliance.”¹⁷

The objectives and initiatives above are ambitious and transformational. Many of them are also expensive. NTU encourages the Committee to engage with Commissioner Werfel and senior IRS officials to determine whether these initiatives will require Customer Service funding beyond levels provided by Congress, and how the IRS plans to square its forward-looking initiatives with the need to hire and retain the additional customer service representatives that made this most recent tax filing season less disruptive than COVID-era filing seasons.

Now might be an opportune time for lawmakers to consider reallocating a portion of IRA funding away from the more flush Enforcement and Operations Support accounts and towards Customer Service and Business Systems Modernization. The National Taxpayer Advocate, Erin Collins, recently called for just that sort of reallocation in a March blog post on the Taxpayer Advocate Service’s website:

My office doesn’t have the financial expertise to determine the costs associated with each initiative. But at a high level, two things are clear: (1) the IRS needs substantially more funding than it was receiving in annual appropriations bills to better serve U.S. taxpayers, and (2) the additional funding provided by the IRA, while appreciated and welcomed, is disproportionately allocated for enforcement activities and should be reallocated to achieve a better balance with taxpayer service needs and IT modernization. We need to put taxpayers first.¹⁸

Tax practitioners have offered a similar recommendation of late. The American Institute of Certified Public Accountants (AICPA) recently recommended that the Treasury Department and IRS address “imbalance[s]” between the enforcement account and taxpayer services account:

...[G]iven the historic low levels of IRS taxpayer services, we are concerned that there was an insufficient allocation of funding in the IRA to improve taxpayer services to appropriate levels. We are concerned that service challenges will persist unless sufficient, targeted funding for technology improvements, human talent and training, and taxpayer services are appropriated.¹⁹

¹⁷ *Ibid.* p. 8.

¹⁸ Collins, Erin. “NTA Blog: National Taxpayer Advocate Urges Congress to Maintain IRS Appropriations But Re-Direct Some Funds Toward Taxpayer Service and Information Technology Modernization.” March 16, 2023. <https://www.taxpayeradvocate.irs.gov/news/nta-blog-nta-urges-congress-to-maintain-irs-appropriations-but-re-direct-some-funds-toward-taxpayer-service-and-it-modernization/> (Accessed May 11, 2023.)

¹⁹ AICPA. (March 28, 2023). “Re: IRS Operational Plan for Resources Included in the Inflation Reduction Act of 2022.” <https://aboutblaw.com/7i7>.

These stakeholders are not partisan, and they are certainly not invested in seeing the IRS funding provided in the IRA fail. That should underscore for Members of this Committee that there is a compelling, non-ideological case to consider diverting a portion of IRA funds away from well-funded accounts and towards critical activities that would improve taxpayer services.

Fiscal Reality: Pinpointing the Impact of IRA’s “Enforcement” Funding, or Changes to that Funding, Misses the Point of IRS Transformation

Since the stated topic of this hearing is “House Republican Supplemental IRS Funding Cuts: Analyzing the Impact on Federal Law Enforcement and the Federal Deficit,” I will turn to the latter topic.

As you know, the nonpartisan Congressional Budget Office (CBO) estimated in August 2022 that the \$80 billion in enhanced IRS resources included in the IRA would increase federal revenues by \$203.7 billion (on a non-scorable basis, due to CBO scoring conventions) from fiscal years (FYs) 2022 through 2031.²⁰ If one were to count those estimated revenues as contributing to deficit reduction, as many supporters of the IRA have, the net deficit reduction projected from the IRS provisions over the same ten-year period was \$123.7 billion.

A month later, CBO revised down the non-scorable revenue increases from FYs 2022 through 2031, from \$203.7 billion to \$180.4 billion. Making the same assumptions as above, the net deficit reduction from IRS provisions was revised down to \$100.4 billion over 10 years.²¹ Subsequent legislation from House Republicans to repeal significant portions of the IRA’s IRS funding – including all supplemental amounts for enforcement and operations support – were scored as increasing deficits by \$114.4 billion from FYs 2023 through 2032²² and \$119.7 billion from FYs 2023 through 2033.²³

NTU Foundation Vice President of Research Demian Brady previously reviewed the numerous reasons why increased revenue collections by the IRS under the IRA’s supplemental funding may fall short of CBO’s expectations:

²⁰ Congressional Budget Office (CBO). (August 5, 2022). “Estimated Budgetary Effects of H.R. 5376, the Inflation Reduction Act of 2022.” Retrieved from: https://www.cbo.gov/system/files/2022-08/hr5376_IR_Act_8-3-22.pdf (Accessed May 11, 2023.)

²¹ CBO. (September 7, 2022). “Estimated Budgetary Effects of Public Law 117-169.” Retrieved from: https://www.cbo.gov/system/files/2022-09/PL117-169_9-7-22.pdf (Accessed May 11, 2023.)

²² CBO. (January 9, 2023). “Estimated Budgetary Effects of H.R. 23, the Family and Small Business Taxpayer Protection Act, as Posted on the Website of the Clerk of the House of Representatives on January 9, 2023, as an Item That May Be Considered Pursuant to a Rule.” Retrieved from: https://www.cbo.gov/system/files/2023-01/hr23_IRS.pdf (Accessed May 11, 2023.)

²³ CBO. (April 25, 2023). “Re: CBO’s Estimate of the Budgetary Effects of H.R. 2811, the Limit, Save, Grow Act of 2023.” Retrieved from: https://www.cbo.gov/system/files/2023-04/59102-Arrington-Letter_LSG%20Act_4-25-2023.pdf (Accessed May 11, 2023.)

- “[T]he final version of the IRA dropped a provision granting the IRS expedited hiring authority. In the absence of that authority, it will take longer to onboard and train new employees, reducing the level of expected collections.
- “As inflation leads to higher cost-of-living adjustments for federal workforces, the IRS may not be able to hire as many people with the funding provided (though the number of additional FTEs would still be much larger than mainstream media estimates). This would further undermine revenue estimates.”
- “Challenging the IRS can be costly and drag on for an extended period of time, but the agency is by no means always successful in securing judgments against those it accuses of fraud. NTUF previously compiled a list of news articles where the IRS had taken an overaggressive position against taxpayers and ultimately lost in court.”²⁴

Each of those concerns remain relevant to the agency and to CBO’s estimates today.

NTU and NTU Foundation were even more skeptical of the revenue estimates offered by the Treasury Department in 2021, in the lead-up to consideration of the Build Back Better Act and the IRA. In September 2021, then-Acting Assistant Secretary for Tax Policy Mark Mazur wrote that:

Conservatively, about \$400 billion of additional revenue can be collected (incorporating both the direct and indirect effects of enforcement investment) from the President’s proposals, net of the \$80 billion investment.²⁵

The non-partisan scorekeepers at CBO clearly disagreed with this assessment – and in fact ultimately estimated revenue effects about a fourth the size of the Treasury Department’s 2021 estimates – but the IRS insisted as recently as April 2023, upon the publication of its Strategic Operating Plan, that (emphasis ours):

The Congressional Budget Office estimates that the additional \$80 billion provided to the IRS by the IRA will increase federal revenue by more than \$180 billion in the decade ahead, considering only direct enforcement revenue based on additional staffing.²⁶

²⁴ Brady, Demian. “What the IRS’s New Enforcement Budget Means for Taxpayers.” NTU Foundation, September 21, 2022. Retrieved from: <https://www.ntu.org/foundation/detail/what-the-irss-new-enforcement-budget-means-for-taxpayers> (Accessed May 11, 2023.)

²⁵ Mazur, Mark J. “The Revenue Impacts of Compliance Proposals.” Department of the Treasury Office of Tax Policy. September 14, 2021. Retrieved from: https://home.treasury.gov/system/files/136/Yellen_Neal_Congressional_Budget.pdf (Accessed May 11, 2023.)

²⁶ IRS. (April 2023). “Internal Revenue Service Inflation Reduction Act Strategic Operating Plan: FY2023 - 2031.” Retrieved from: <https://www.irs.gov/pub/irs-pdf/p3744.pdf> (Accessed May 11, 2023.)

We remain skeptical that the IRS will spend IRA resources in an efficient and effective enough manner to reach the revenue estimates established by CBO. In addition to the concerns outlined above, the IRS is already reporting to stakeholders that it is stretched thin on resources to implement the clean energy provisions included in the IRA. The Strategic Operating Plan suggests that some of the supplemental resources available to the IRS under the IRA will need to be diverted to implementation of IRA clean energy provisions.²⁷ Might this cut into the additional revenues CBO previously projected the IRS could collect through increasing enforcement activities? Time will tell, but lawmakers should monitor IRS implementation of the funding closely to see if net deficit reduction is occurring at rates projected by CBO or the Treasury Department.

None of these concerns should be taken to mean we doubt the premise that better tax compliance can enhance federal revenue. Rather, NTU simply returns to our earlier, cautionary advice in this testimony that it is a mistake to engage in transformational compliance initiatives simply to reach a particular “offset” for government spending in one piece of legislation.²⁸ The revenue collection number from IRA funding for compliance (or even the clumsy misnomer “enforcement”) is, on net, likely to be quite a bit more than zero.

There are other fundamental matters to consider at today’s hearing, in addition to whether the actual net deficit result will be \$100.4 billion, or \$50.2 billion, or something else. What types of metrics for example, besides, revenues, will be used to track enforcement activities? In the 1980s and 1990s, Congress acted to make certain that performance and promotion evaluations for individual IRS employees were not based on collection quotas.²⁹

The IRS Strategic Operating Plan outlines a number of activities that will take compliance in partially or entirely new directions, which could easily impact the CBO estimates described earlier in unpredictable ways. These include:

- “Develop a process for continually refining compliance analytics models based on feedback and new information” for audits. Robust models could prevent wasted

²⁷ *Ibid*; see the table on page 129, which indicates the agency proposed to invest \$3.9 billion on implementing “Energy security” provisions of the IRA rather than \$0.5 billion Congress specifically earmarked for such provisions.

²⁸ As an example, certain additional revenues expected from the Foreign Account Tax Compliance Act (FATCA) have not materialized as expected, for a number of reasons. “When FATCA was implemented, it was estimated to bring in \$8.7 billion in revenue over the next 10 years. Although total revenues tied to the legislation are unclear, the IRS has collected less than \$14 million over the last 12 years.” See <https://brighttax.com/blog/fatca-update-april-2022>.

²⁹ See, for example, Parker, John. “IRS Officers Pressured to Make Seizures, Ex-Chief Says.” *Daily Oklahoman*. August 19, 1998. <https://www.oklahoman.com/story/news/1998/08/19/irs-officers-pressured-to-make-seizures-ex-chief-says/62271734007/>. And, Associated Press. “IRS Suffers ‘Seizure Fever,’ Agents Tell Subcommittee.” *Los Angeles Times*. June 23, 1987. <https://www.latimes.com/archives/la-xpm-1987-06-23-fi-10105-story.html>.

resources, but flawed or biased ones could just as easily lead the Service down costly rabbit holes.

- “Develop and implement a plan to improve the IRS Whistleblower Program.” NTU is a longtime supporter of the IRS Whistleblower Program, and whistleblower protection laws throughout the federal government. In fact, the focused information and “leads” from this program could prove more effective for compliance and audits than hit-and-miss data dragnets that require costly resources and end up targeting innocent taxpayers. Depending on how and when this program upgrade is prioritized, however, key opportunities for revenue recovery could be missed.
- “Develop approaches and new treatments for large partnership enforcement by leveraging data and analytics.” A Treasury Inspector for Tax Administration (TIGTA) report from last year reported that the “no-change” in partnership audits ranged from 78 to 90 percent.³⁰ How much the IRS’s new “approaches” affect that rate could mean billions of revenue dollars either way. We would hasten to add that many of the energy provisions in the IRA would allow for the “sale” of tax credits from taxpayers who could not fully utilize them to others. These transactions would likely involve the very partnerships that many IRA supporters seem to view with suspicion. The political pressure on the IRS’s partnership audit goal could thus be acute, and diminish possible revenue collections.

The greatest uncertainty in revenue estimates, however, is the basis on which they are projected: the “tax gap” itself. Other witnesses will be providing greater detail than NTU’s testimony on this issue; our work suggests that while the tax gap is considerable, measuring its size depends not only on taxpayer behavior, but also shifts in the economy, and of course, interpretations of how laws actually apply.

The historic fluctuations in official estimates of the tax gap are an illustration of the volatile nature of the issue. Earlier this year Joe Bishop-Henchman, a colleague at our sister organization National Taxpayers Union Foundation, wrote:

The IRS released its latest estimates of the tax gap in 2022. The IRS found that the annual gross tax gap for 2014–2016 was \$496 billion. After late payments and enforcement actions, the net tax gap was \$428 billion. That figure represented 2.7 percent of GDP, the same as estimates for other recent years, and down from 3.3 percent in 2001 and 3.4 percent in 2006. The IRS estimates that the gap in 2017–2019 dipped to 2.6 percent of GDP.

³⁰ Bonner, Paul. “BBA Partnership Audits Show High No-Change Rates, TIGTA Says.” *Journal of Accountancy*, March 28, 2022. <https://www.journalofaccountancy.com/news/2022/mar/bba-partnership-audits-show-high-no-change-rate-tigta-says.html>.

International studies show that the United States has a fairly low tax gap compared to other countries. In a 2018 study, Polish economists Konrad Raczkowski and Bogdan Mróz estimated tax gaps for 35 countries, including 28 EU countries and the United States. They put the U.S. gap at 3.8 percent of GDP and the EU gap at 7.7 percent of GDP. ...In a 2019 study, political economist Richard Murphy estimated that the tax gap for 28 EU countries was equivalent to 5.6 percent of GDP. The latest IRS study puts the U.S. federal tax gap at 2.7 percent, but with an estimated state-local tax gap added, the U.S. total tax gap would be about 4.2 percent of GDP.³¹

But what of the as-yet indeterminate components of the tax gap, such as digital assets, that are not fully incorporated into conventional estimation methodologies? A National Taxpayers Union Foundation analysis from 2021 illuminated some of the obstacles to reaching a firm calculation, at a time when then-Commissioner Rettig ventured the total tax gap “could approach and possibly even exceed” \$1 trillion:

A rough IRS estimate in 2018 placed the tax gap from cryptocurrency at about \$11.5 billion, back when the digital cryptocurrency market was worth an estimated \$500 billion.

Even assuming the IRS has failed to improve at all on its previously estimated noncompliance rate of 50 percent, this extrapolates to a cryptocurrency tax gap of just under \$50 billion based on the 400 percent increase in global market capitalization that digital currencies have enjoyed since then. That is of course a significant amount, but it is also only around 12 percent of the \$381 billion tax gap estimate.

The IRS also has not made a concrete estimate of offshore holdings which are going untaxed. Research the IRS helped fund and authored in part by left-wing economist Gabriel Zucman placed the amount of American offshore holdings in low-tax jurisdictions at just over \$1 trillion. They arrive at this number by assuming that 95 percent of wealth in these holdings is concealed from the IRS, an estimate which is likely high.³²

Nevertheless, even if one assumes this data is entirely correct, the authors still estimate just \$15 billion in uncollected tax revenue per year. Combining this number with the

³¹ Bishop-Henchman, Joseph. “Transforming the Internal Revenue Service.” Cato Institute Policy Analysis No. 942. April 11, 2023, pp. 9-11. <https://www.cato.org/policy-analysis/transforming-internal-revenue-service>.

³² This is especially the case since the passage of the Infrastructure Investment and Jobs Act, after the National Taxpayers Union Foundation analysis was published. The law extends the \$10,000-plus cash transaction reporting requirement businesses to digital assets, giving the IRS a new stream of data to examine for possible tax evasion. New estimates of revenues from this area of tax compliance will need to be adjusted to reflect efforts already underway.

estimate of roughly \$50 billion in uncollected cryptocurrency tax revenue, we are still shy of \$500 billion, let alone \$1 trillion.³³

NTU does not contend that complete repeal of IRA’s “enforcement” portion of IRS funding will have zero deficit impact, relative to the current budget baseline of which IRA is now a part. Nor, however, should IRA’s supporters contend that shifting “enforcement” funding into other IRS functions has a simple linear upward impact on future deficits.

Nor should serious policy advocates on either “side” of the IRA ignore the *net* revenue impacts of IRS funding decisions. One factor in this equation is whether increased compliance burdens on all taxpayers in an income class to ferret out just the noncompliant taxpayers, diverts resources from legitimate, profitable activities that might otherwise be taxed. We leave the detailed analysis of that matter to another witness on this panel, Chris Edwards, but we acknowledge its importance.

In sum, precisely because the IRS would engage in brand-new compliance strategies, precisely because measurements of the tax gap and the hidden economy are fluid, and precisely because other options like improved customer service to enhance compliance have not been adequately explored, the deficit impact of IRA changes cannot easily be measured to the nearest \$10 billion, or likely even to the nearest \$100 billion.

It is also why tying this exercise to tax and spending legislation passed through the reconciliation process, is a far from helpful way to discuss the fiscal consequences of the transformation now occurring at the IRS. *Defining the success of this transformation, and then making that success a priority, will yield enhanced revenue in the future. Arguing now over what exactly that revenue will be over a fixed period of time will, ironically, distract policymakers’ attention from the very tasks needed to see those revenues come to fruition in the first place.*

³³ Wilford, Andrew, Moylan, Andrew, and Sepp, Pete. “The Tax Gap: No Trillion-Dollar Silver Bullet.” National Taxpayers Union Foundation. May 13, 2021. <https://www.ntu.org/foundation/detail/the-tax-gap-no-trillion-dollar-silver-bullet>. Note former National Taxpayer Advocate Nina Olson’s observation:

Equating the entire tax gap to ‘tax evasion’ is just so disingenuous. And it’s also wrong; it’s incorrect. Evasion has a technical meaning under the law, and generally it requires mens rea, a criminal intent. So much of it is error, or inadvertent...there are a bunch of different types of noncompliance. And if you say [it’s all tax evasion] - and that’s what the *Washington Post* called it, that’s what the *New York Times* called it - then that creates distrust among the taxpayers of the tax agencies. [They’re asking], “why am I paying if you’re letting all these people off the hook?”

Policy Reality: Even If the “\$400,000 Pledge” Is Kept, All Taxpayers Will Be Affected by IRA Compliance Funds

A byproduct of the policy debate over IRA has been a fixation on Secretary Yellen’s directive (reiterated by Commissioner Werfel) “not to increase audit rates relative to historical levels for small businesses and households earning \$400,000 per year or less.” No less than half a dozen Questions for the Record submitted during Commissioner Werfel’s confirmation hearing before this Committee contained variations on that theme.³⁴

As my colleagues and I have written before, the \$400,000 threshold is, in itself, subject to all manner of interpretation, besides the obvious question of how to define “historical rate”:

- Does that amount represent Adjusted Gross Income, Modified Adjusted Gross Income, Taxable Income, Total Positive Income, or some other measure? Is it what a taxpayer reports on their return for the year the IRS wishes to conduct an examination, or is it what the IRS believes the taxpayer’s taxable income ought to be after proposed adjustments? If the latter, greater numbers of Americans than advertised will be subject to scrutiny, perhaps to no avail.
- Does this directive create a “marriage penalty,” in the sense that the IRS could investigate a single taxpayer’s return reporting above \$400,000, but could also look into a joint return where each taxpayer earns \$200,000? Dual-earner households in large cities could be surprised to find themselves under the microscope.
- What year will govern the audit decision – the year of the return under examination, or the taxpayer’s present circumstances? A business owner who earned \$500,000 during the good times of 2019 might be shocked to get an audit notice next year if she finds herself struggling with half that cash flow today. In fact, high-income tax returns are also among the most volatile in reporting year over year incomes.
- What happens if the directive is disobeyed or unintentionally violated? The Secretary’s ability to impound funds is highly limited. And if “accidents” happen, how can a taxpayer possibly be made whole? A Treasury directive does not carry the force of law in court, and regardless, no outside entity will be monitoring IRS audit rates in real time.³⁵

³⁴ United States Senate Committee on Finance. “Finance Committee Questions for the Record, Hearing on the Nomination of Daniel Werfel, Responses by Daniel Werfel.” February 24, 2023. <https://www.finance.senate.gov/download/responses-to-questions-for-the-record-to-daniel-werfel>.

³⁵ For more detail, see Brady, Demian. “What the IRS’s New Enforcement Budget Means for Taxpayers.” National Taxpayers Union Foundation. September 21, 2022. Retrieved from: <https://www.ntu.org/foundation/detail/what-the-irss-new-enforcement-budget-means-for-taxpayers>.

Do these concerns amount to parsing words? Perhaps, but the operation of the entire tax system often depends upon this very exercise, as Congress proves with myriad technical corrections to various tax laws, or with numerous controversies that wind up in the courts. Only very recently have clues begun to emerge on how exactly the IRS will keep this “pledge,” but the definition has yet to be settled.

Of greater importance, the IRS’s own Strategic Operating Plan makes no secret that several compliance and enforcement efforts that have little to do with audits will apply to all taxpayers:

- “Expand capacity and resources for our non-filer and return-delinquency programs.”
- “Create processes for real-time identification of taxpayers who miss payments ...”
- “Develop and pilot new collection treatments based on data and analytics.”
- “Centralize compliance analytics and develop a process to regularly model the population of tax returns.”³⁶

These projects are couched in terms of providing better service to taxpayers; and as for regular modeling of the tax return population, this is undoubtedly preferable to plowing ahead with compliance initiatives based on a poor understanding of the filing population. Nonetheless, they demonstrate that even if a strict \$400,000 per-filing unit threshold, based on taxable income for the year audited, is faithfully adhered to, other types of “enforcement” and compliance projects from IRA funding will affect middle-class and moderate-income taxpayers.

There are also practical considerations that will soon become evident. Suppose, for instance, IRS counsel are pursuing two cases in Tax Court with virtually identical facts and circumstances, thereby utilizing the same legal strategies in both actions. In the first action, the Service prevails against a taxpayer with an income (however measured) of \$415,000. The second action, yet to be decided, involves a taxpayer with an income of \$385,000. It is foolish to assume that the Service would suddenly drop the second case and walk away because of some fluid income threshold that doesn’t even have a definition in statute.

In addition, even the most precise analytics and data collection in the area of tax compliance are likely to yield “false positives” – potential audit selections that fall at or under the \$400,000 threshold for some reason. Indeed, some situations may require innovative and advanced modeling for a particular behavior (e.g., concealing digital assets) regardless of income, and then identifying on purpose those who exceed the \$400,000 threshold for possible audit. What happens to the “accidental” or “incidental” data collected from this exercise for households who

³⁶ IRS. (April 2023). “Internal Revenue Service Inflation Reduction Act Strategic Operating Plan: FY2023 - 2031,” pp. 56, 58, 60, and 66. Retrieved from: <https://www.irs.gov/pub/irs-pdf/p3744.pdf> (Accessed May 11, 2023.)

fall under the threshold? Will a handful of taxpayers at the \$390,000 threshold be allowed to skate away from an audit? What if a million taxpayers making less than \$100,000 are suspected of concealment? Will this portion of the data simply be destroyed, or used in some other non-audit compliance manner?

Historically, it is also true that IRS tactics honed for use against one class of taxpayers are soon deployed against others. Information Document Requests (IDRs), once primarily a feature of large-business audits, are now commonplace in examinations involving firms with dozens rather than thousands of employees. In the mid-2010s, the use of designated summons power and designating cases for litigation in the examination and investigation process had become so widespread as to attract the attention of Congress and prompt limited reforms in the Taxpayer First Act.³⁷

Finally, the simple fact is that money is fungible. As Demian Brady of National Taxpayers Union Foundation explained:

Nothing the IRS receives in annual appropriations, over and above the IRA funds, would be subject to the \$400,000 taxpayer income limitation. The Service could also simply request from Congress, or to a more limited degree, redirect, more funds from what it would otherwise normally spend on high-income enforcement activities toward those lower on the scale. Furthermore, neither Secretary Yellen nor Congress demanded that any kind of public accounting be kept on how enforcement dollars will be used against certain types and classes of taxpayers. Additional monies in the IRA to the Treasury Inspector General for Tax Administration could be employed for such purposes, but here again, the legislation is silent on where TIGTA is supposed to look.³⁸

Congress could rectify this issue by following up with a demand for such a detailed accounting of high-income “enforcement” expenditures, *but another form of reconciliation is necessary too: that IRA compliance funding will touch the entire taxpaying population, even if one enforcement tool is aimed at higher-income filers. Once this reality is accepted, the need for a holistic,*

³⁷ See, for example, Sepp, Pete. “Statement Prepared for the Subcommittee on Economic Growth, Tax, and Capital Access, Committee on Small Business, United States House of Representatives, Regarding the Subcommittee’s Hearing on “Audits and Attitudes: Is the IRS Helping or Hurting Small Businesses?”” Submitted June 22, 2016. <https://www.ntu.org/publications/detail/statement-ofpete-sepp-to-house-subcommittee-regarding-irs-small-business-reforms>. Here we also note the analyses that many small businesses undergo when evaluating whether to challenge what they believe to be an erroneous IRS assessment, leading many to pay the tax owing to the costs of appeal or litigation. Today, given statistics of average disputed amounts of tax on small business returns (See IRS Data Book for FY 2022 <https://www.irs.gov/statistics/soi-tax-stats-irs-data-book>), even some in income categories of \$500,000 up to \$1 million might make a similar judgment.

³⁸ Brady, Demian. “What the IRS’s New Enforcement Budget Means for Taxpayers.” National Taxpayers Union Foundation. September 21, 2022. Retrieved from: <https://www.ntu.org/foundation/detail/what-the-irss-new-enforcement-budget-means-for-taxpayers>

systemic approach to compliance that respects all taxpayers' rights, regardless of their circumstances, will become apparent.

Recommendations: Balancing Compliance, Fiscal Responsibility, and Taxpayer Rights

If the IRS is to deliver what the Commissioner calls “the modernized tax administration system the American people deserve,” that achievement will not be solely because of the IRS’s efforts. It will take a number of major commitments throughout government and the private sector to effectuate. The following are some of NTU’s top priorities for Members of the Committee to consider. Some require direct congressional action, while others will benefit simply from your leadership and support.

1) Deploy Existing Assets for Management, Including the IRS Oversight Board

We begin our list with this item for a reason. Congress cannot, on its own, effectively oversee the IRS’s strategic plan without institutions that are dedicated to monitoring and making course corrections to the Service’s strategies and tactics on a consistent basis.

No other entity is better suited to this task than the IRS Oversight Board. Created in the IRS Restructuring and Reform Act of 1998 with the purpose of bringing in outside experts to oversee the “administration, management, conduct, direction, and supervision” of IRS operations. It was specifically tasked with reviewing and approving the annual and long-range strategic plans of the IRS, including its mission and objectives. It can do so for 2023’s Strategic Operating Plan,

The Board is supposed to have nine members, including the Treasury Secretary and the IRS Commissioner as standing members along with seven positions appointed by the President and nominated by the Senate. One of the appointees must be either a federal employee or a representative of IRS employees, but otherwise, as noted, the intention of the 1998 Act was to bring people with private sector experience into discussions regarding the agency’s operational challenges. Such experience need not be focused on managerial issues like IT or personnel. Private sector Board members could bring valuable perspectives on how to measure the tax gap, where taxpayer and customer behavior patterns overlap, and how arbitration and mediation can resolve disputes.

Even though appropriations for the IRS (as well as IRA) continue to include language providing support funding for the Board, it has unfortunately gone dormant since 2015 due to a lack of a quorum. That problem can be rectified almost immediately, by encouraging the President to send Board nominees to the Senate for quick confirmation.

Reviving the Board won’t be easy, but it is the first big test of whether policymakers are serious about making the Strategic Operating Plan work. Given that there was so little legislative

collaboration on IRA vs. RRA '98, it is more imperative now than it was 35 years ago. This Committee can create a safe space for doing so, by reaching out to and encouraging the White House to send nominees for the Board to consider as soon as possible.

At the same time, it is also apparent that little consultation with the IRS Advisory Council (IRSAC) and the Electronic Tax Administration Advisory Council (ETAAC) took place prior to production of the Strategic Operating Plan.³⁹ This needs to change. IRSAC and ETAAC could focus on rectifying specific issues raised by the IRS Oversight Board, relying on their experience as practitioners and experts on many aspects of tax administration.

Leveraging the underappreciated Taxpayer First Act Report of 2021 likewise falls under this category. The Strategic Operating Plan would appear to contain an impressive level of detail in its 150 pages, but beyond the graphics, the generous font for text, and the “Key Projects” and “Milestones” sections is a fair amount of repetition and vagueness in how the “Operating” part of the plan would actually work. The Taxpayer First Report, spanning 254 pages, gives many detailed insights into how taxpayer service, personnel training, and organizational restructuring could modernize the IRS. These include how divisions of the Service can be reorganized to improve the taxpayer experience, how outreach to underserved taxpayer communities can be improved, and how risks to managerial failure can be mitigated.

While NTU does not agree with every approach in the report, the stakeholder outreach process, detailed in the report’s appendices, is a good starting point for the kind of collaboration the IRS, in conjunction with Congress, the Oversight Board, IRSAC, ETAAC, and other stakeholders must follow going forward.

We would not wish to neglect mentioning the need to speedily evaluate another nominee that may soon be coming the Committee’s way – IRS Chief Counsel. The Committee may of course find this nominee qualified or unacceptable, but it would be a mistake to simply defer action of any kind for months on end once the nominee is designated. Former IRS officials and tax practitioners alike have told us that the Service’s legal team is especially sensitive to leadership from the top. Again, while the Biden Administration may send a poor choice for Chief Counsel to the Committee, it is important for Members to act quickly to reject such a nominee, rather than leave the post unfilled and the Chief Counsel’s office with a weak rudder that could steer IRS’s legal strategy in even less helpful directions for taxpayers.

³⁹ One member of IRSAC recently told me that the Council received little more than a private briefing just prior to the release of the plan. The Finance Committee could, and in our opinion should, ask IRS management for an explanation of the lack of consultation with IRSAC and ETAAC.

2) Create “Off-Ramps” – a Working Appeals Process, Settlement Initiatives, and ADR – to Protect Taxpayers and Save Government Resources

The Taxpayer First Act of 2019 should have been the final word in a nearly century-long line of orders from Congress to provide an independent, neutral forum for taxpayers and the government to resolve disputes without going to court. In addition to codifying the IRS Independent Office of Appeals, the 2019 law also limited the circumstances under which the Service could use tactics to deny appeal rights. Its language specifically stated that while the Treasury could provide “reasonable exceptions,” the ability to appeal was to be “generally available to all taxpayers” who were not taking “frivolous position[s],” as defined by 26 USC §6702(c).”

In November 2022, the IRS proposed a rulemaking with no fewer than 24 exceptions to appeal rights, including several that were clearly aimed at legitimate appeals challenging procedural validity of regulatory or subregulatory guidance. One reason the Service gave for its limits on appeals was resource constraints. But as NTU noted in comments filed in response to the rulemaking:

We also believe that additional funding for the Office would be an acceptable and welcome use of a portion of the \$80 billion in funding Congress has appropriated to the agency for use over the next 10 years under the Inflation Reduction Act (IRA) of 2022. In fact, additional spending to expand appeals rights and independent review of tax controversies could ultimately *save* the agency money over the long run, by obviating more expensive and protracted litigation over tax controversies. The agency could also see indirect savings from improved taxpayer compliance, should taxpayers have confidence in a more robust Independent Office of Appeals.⁴⁰

The IRS Strategic Operating Plan would seem to support this funding direction, by calling to “[increase] staff in the Independent Office of Appeals to resolve tax controversies arising from enhanced compliance efforts.” Commissioner Werfel himself affirmed that the appeals process should be a way to properly air facts and circumstances of individual cases, stating that a “one size fits all approach would not be aligned with these rights [to appeal].”⁴¹

Without additional Congressional guidance, however, the IRS’s rulemakings could stand, and appeals could still be a limited channel for taxpayers to assert their rights. One excellent way to provide that guidance would be through Committee markup and reporting to the floor of Senator

⁴⁰ Sepp, Pete, and Lautz, Andrew. “Comments re: 87 FR 55934, ‘Resolution of Federal Tax Controversies by the Independent Office of Appeals.’” November 14, 2022. <https://www.ntu.org/publications/detail/ntu-offers-comments-to-irs-on-resolution-of-federal-tax-disputes>.

⁴¹ United States Senate Committee on Finance. “Finance Committee Questions for the Record, Hearing on the Nomination of Daniel Werfel, Responses by Daniel Werfel.” February 24, 2023, pp. 22-23. <https://www.finance.senate.gov/download/responses-to-questions-for-the-record-to-daniel-werfel>.

Cornyn’s “Small Business Taxpayer Bill of Rights” (S. 1177).⁴² This legislation would clarify and strengthen appeal rights by effectively banning ex parte communications between the Appeals office and the rest of the IRS, as well as preventing the Appeals office from raising new issues or theories with taxpayers when meeting with them.

Another problem resolution method the Service should embrace more fully, where facts and circumstances of many taxpayers are indeed in closer alignment, is the settlement initiative. Pioneered over 40 years ago under then-IRS Commissioner Roscoe Egger, this concept allows the IRS to offer limited-time legal settlements to taxpayers in cases with no litigation hazard and where there are no precedents to be set or compliance problems in the absence of a trial. Depending on the issue at hand, a taxpayer might be able to keep a fraction of their deduction or credit in question, or could be limited only to their “cash outlays” in claiming a tax benefit. In the years that followed, settlement initiatives were successful in clearing numerous cases from crowded court dockets on matters such as the amortization of intangibles, a targeted jobs tax credit, and perhaps most successfully, in 2008, the lease-in/lease-out and sale-in/lease-out (LILO/SILO) controversy. Both the government and taxpayers benefited from reduced time and litigation costs, while the Treasury recovered tens of billions in revenues that might otherwise have entailed considerable effort and risk to recover.⁴³

Still another promising avenue is alternative dispute resolution (ADR), through mediation and binding arbitration. Common in tax systems around the world from the United Kingdom to Portugal to Australia, ADR allows taxpayers of limited means or time the ability to quickly obtain results that are fair to all parties. The National Commission on Restructuring the IRS gave extensive consideration to improving Alternative Dispute Resolution methods for use in federal tax controversies, including mediation as well as binding arbitration. Limited procedures were in place at that time, applying primarily to cases of over \$10 million or more. ADR at the tax agency was a relatively new concept, following passage of the government-wide Administrative Dispute Resolution Act of 1996.

Ultimately, the Commission did not make major recommendations in this area, although the subsequent 1998 RRA did remove the dollar threshold, and establish a pilot program for binding arbitration. Unfortunately, the usefulness of ADR for most taxpayers has so far been

⁴² Sepp, Pete and Lautz, Andrew. “Senate Bill Would Provide Small Business Taxpayers with New Rights.” National Taxpayers Union. May 17, 2021. <https://www.ntu.org/publications/detail/senate-bill-would-provide-small-business-taxpayers-with-new-rights>.

⁴³ For excellent background, see Gomez, Armando, and Barral, Roland. “It’s High Time to Clear Out the Tax Court’s Easement Backlog.” *Tax Notes Federal*, Volume 179, April 10, 2023. <https://www.taxnotes.com/exempt-organizations/conservation-easements/its-high-time-clear-out-tax-courts-easement-backlog/2023/04/25/7g8xx>.

questionable. The National Taxpayer Advocate's 2016 Annual Report to Congress has made the IRS's failure to "effectively use ADR" as #15 on the "Most Serious Problems" list.⁴⁴

With ADR confined largely to the periphery of taxpayer service offerings by the IRS, the IRA funding infusion could easily stand up a more robust program. A legislative framework for doing so already exists in S. 1177.

Some may object to these "off-ramps" as essentially "escape routes" for wealthy taxpayers. Aside from the fact that the U.S. Constitution does not define rights by income levels, all of these procedures actually inure most to the benefit of those whose legal resources are limited. Furthermore, they can aid in compliance by reinforcing public trust that these options for settling disputes are available *to all* and provide a "fair shake" *for all*. At the same time, expanding their availability would optimize revenue collection at the most efficient level of expenditure for the government, delivering early returns on IRA's funding.

There are also reputational risks to consider when evaluating alternatives. In recent years the government has pursued increasingly exotic positions in court, on both substantive matters such as appraised values in tax deductions and Foreign Bank Account Registration penalties, to procedural matters such as the limits of the Administrative Procedure Act and "one day late" taxpayer responses. The result has been embarrassing losses all the way up to the U.S. Supreme Court, some involving 9-0 rulings.⁴⁵ It can be argued that the government's use of "strategic ambiguity" in court can actually spawn noncompliance from taxpayers who have diminished respect for the government's position and feel they have little to lose by not settling disputes.

3) Examine and Evaluate, in Detail, the Commissioner's and Taxpayer Advocate's Recommendations about the Funding Mix Under IRA

With two of the nation's top tax administration officials clamoring for a remedy to the "funding cliffs" for taxpayer services in IRA's funding for the Internal Revenue Service, this Committee can exercise leadership now by examining in-depth whether and how Title I, Part 3 of the IRA (as well as other IRS funding) should be adjusted to reflect more immediate needs. This should also include business systems modernization, which could require more resources than anticipated. Again, NTU emphasizes that this examination should not be viewed as "zero-sum." Enhanced taxpayer services and business systems modernization can make significant contributions to compliance and resulting revenues. Of course, the Committee is not the arbiter

⁴⁴ For background see, Sepp, Pete. "Comments before the Subcommittee on Oversight, Committee on Ways and Means, 'IRS Reform: Resolving Tax Disputes,'" September 13, 2017. <https://www.ntu.org/publications/detail/irs-reform-resolving-taxpayer-disputes>.

⁴⁵ For background, see Bishop-Henchman, Joseph. "Transforming the Internal Revenue Service." Cato Institute Policy Analysis No. 942. April 11, 2023, pp. 5-6, 13-14. <https://www.cato.org/policy-analysis/transforming-internal-revenue-service>.

of appropriations, but it is uniquely equipped, along with the House Committee on Ways and Means, to comprehensively review the IRS's fiscal trajectory. This needs to take place in "real time," as appropriations season gets into full swing.

4) Focus on a Wide Range of Compliance Tools

As this testimony has made quite clear, the goal of "compliance" does not always require the means of "enforcement." As far back as 1997, Ernest Dronenburg, a member of the National Commission on Restructuring the IRS, and former California Board of Equalization Leader, remarked that:

A .5 percent increase in voluntary compliance resulting from taxpayer education and changing attitudes would increase revenue in my state by over \$400 million annually. Conversely, doubling our current audit coverage from 3% to 6% would produce less than half that amount.⁴⁶

Over the past 35 years, research into the effectiveness of non-"enforcement" compliance tools has become more sophisticated, with encouraging results. For example, at the IRS/Tax Policy Center 2022 Joint Research Conference on Tax Administration, researchers Brian Galle and Alexander Yuskavage presented a paper that examined the impact of "non-monetary sanctions" on tax compliance. Utilizing a data set of California's "Top 500" delinquent taxpayers (obviously high-income earners), they found "strong positive compliance responses" to a program that employed notices such as those "warning of the imminent publication of a taxpayer's personal information and potential license suspension."⁴⁷ At the 2021 joint conference, Paul Organ presented research indicating that "collateral sanctions" via the IRS's passport certification and revocation process have "an immediate and strong positive effect on compliance actions for many of those denied a passport request."⁴⁸ These tactics, while potentially more focused and less intrusive than a levy or lien to satisfy a tax debt, would still need to be wielded with caution.⁴⁹

But there are many other compliance methods that are less coercive. On a recent "Tax Chat!" hosted by the Center for Taxpayers Rights' President Nina Olson, several experts in the field of

⁴⁶ Cited in Sepp, Pete. "Comments before the Subcommittee on Oversight, Committee on Ways and Means, 'IRS Reform: Resolving Tax Disputes,'" September 13, 2017. <https://www.ntu.org/publications/detail/irs-reform-resolving-taxpayer-disputes>.

⁴⁷ The full joint research conference proceedings may be viewed online at <https://www.taxpolicycenter.org/event/12th-annual-irstpc-joint-research-conference-tax-administration>.

⁴⁸ The full joint research conference proceedings may be viewed online at <https://www.taxpolicycenter.org/event/11th-annual-irstpc-joint-research-conference-tax-administration>.

⁴⁹ See, for example, Wilford, Andrew. "Tax 'Shame Lists': 19 States Publish Private Info about Taxpayers." National Taxpayers Union Foundation. April 19, 2023. <https://www.ntu.org/foundation/detail/tax-shame-lists-why-19-states-publish-private-info-about-taxpayers>.

tax compliance stressed the importance of building public trust in the government’s expertise and fairness, not just fear of punishment. Erich Kirchler, a psychologist from the University of Vienna, Austria, noted that using a well-developed definition, each one percent increase in public trust of a tax authority led to more than double that percentage in compliance. Furthermore, the panelists discussed how “nudges,” such as asking for additional information on a tax return can help to resolve compliance issues before rather than after filing. One example a panelist gave was a large drop in claimed dependents when filers were required to list the Social Security numbers of those dependents. Notably, all agreed that the IRA’s funding ratio of “enforcement” to “taxpayer services” was far too lopsided.⁵⁰

If the IRS Strategic Operating Plan’s goal of being able to “help the taxpayer to become as compliant as possible” is to be achieved, then tools such as these will need to be deployed in greater abundance. An Oversight Board, combined with Congressional encouragement, could make a serious difference in making that happen.

5) Develop Better Measures for Alternative Compliance Strategies

“Data and Analytics” is an oft-repeated theme in the IRS’s Strategic Operating Plan for estimating the tax gap, finding patterns of non-compliance, and improving the taxpayer service experience. Yet, little has been discussed about the uses of data and analytics for alternate compliance tools as well as the impact of enforcement on the private sector.

At the 2023 Donald C. Lubick Symposium sponsored by the Tax Policy Center, former National Taxpayer Advocate Nina Olson observed that very little work has been done to accurately measure the fiscal benefit to tax compliance by providing improvements in IRS taxpayer services.⁵¹ Conducting research in this area should be a top priority, elevating it to the same academic and econometric level that has hitherto been afforded largely just to the revenue windfalls from conventional “enforcement” approaches. Commissioning such research now, perhaps using instructive language in IRS appropriations bills, would pay major dividends in the near future as IRS compliance strategies move from planning to execution.

In addition, as witness Chris Edwards observed, solid research on the “cost” part of “cost-benefit analysis” associated with various compliance approaches is sorely needed.

As an example, for many years, National Taxpayers Union Foundation has published an annual analysis of federal personal and business income tax system complexity, including estimates of

⁵⁰The full “Tax Chat!” to which this paragraph refers may be viewed online at <https://www.youtube.com/watch?v=DR01e0vWRmY>.

⁵¹ The full Lubick Symposium to which this paragraph refers may be viewed online at <https://www.taxpolicycenter.org/event/how-does-irs-intend-invest-80-billion-over-next-decade>.

paperwork burden hours based on Office of Information and Regulatory Affairs (OIRA) data.⁵² Two findings from recent studies are that many of OIRA’s “information collections” are based on very scant responses from taxpayers⁵³ and that online reports are less than transparent:

One simple way to improve transparency would be to separate information collections that have no actual cost from those where the cost is indeterminate. This way, users of the data would not have to wade through successive pages and attached Supporting Statements to find that out. The information on OIRA’s paperwork burden database should specify that a cost is indeterminate instead of listing it as \$0.⁵⁴

It should be noted that the Foundation’s paperwork burden estimates (6.5 billion hours and \$260 billion) for individual and business filers do not include compliance costs associated with IRS subregulatory guidance. This type of tax compliance needs to be measured and made public.

Even with measurements that have more interest from researchers, the principle of competition could be brought to bear in encouraging more innovative, fresh approaches. After all, TIGTA recently pointed out improvements that are needed at the IRS’s Office of Research, Applied Analytics, and Statistics (RAAS) for tax gap estimates:

RAAS does not have documented policies or procedures for producing the Tax Gap estimates. While the IRS has high-level quality and research guidelines, they do not discuss the Tax Gap estimates. In lieu of documented procedures, RAAS has developed technical papers for each component of the Tax Gap estimates, which provide varying levels of specificity on the data sources and methodologies used. In addition, RAAS does not have written policies, procedures, or guidance to 1) specify the frequency of issuing Tax Gap estimates or 2) help RAAS analysts meet internal milestones for developing the Tax Gap estimates. Instead, RAAS relies on its staff’s experience with developing previous Tax Gap estimates to meet internal milestones. This raises concerns about the potential for a lapse in quality, timeliness, and continuity of operations following an unexpected departure of subject matter expert(s).⁵⁵

⁵² See, for example, Brady, Demian. “6.5 Billion Hours, \$260 Billion: What Tax Complexity Costs Americans.” National Taxpayers Union Foundation. April 17, 2023. <https://www.ntu.org/foundation/detail/65-billion-hours-260-billion-what-tax-complexity-costs-for-americans>.

⁵³ Brady, Demian. “Increasing Complexity Brings Back Bigger Compliance Burdens.” National Taxpayers Union Foundation, April 18, 2022. <https://www.ntu.org/foundation/detail/increasing-complexity-brings-back-bigger-compliance-burdens>.

⁵⁴ Brady, Demian. “6.5 Billion Hours, \$260 Billion: What Tax Complexity Costs Americans.” National Taxpayers Union Foundation. April 17, 2023. <https://www.ntu.org/foundation/detail/65-billion-hours-260-billion-what-tax-complexity-costs-for-americans>.

⁵⁵ Rascon, Jose. “IRS Lacks a Clear Estimate of Uncollected Taxes, Watchdog Says. Meritalk, March 31, 2023. <https://www.meritalk.com/articles/irs-lacks-a-clear-estimate-of-uncollected-taxes-watchdog-says/>.

Other federal agencies, such as CBO, the Joint Committee on Taxation, the Small Business Administration, and others can and should be invited more regularly to share their experience and expertise on tax compliance matters. So should private sector associations and econometric firms. A well-functioning IRS Oversight Board, in conjunction with IRSAC, could easily provide the ongoing direction to coordinate this activity.

6) “Tax Certainty” Begins with Following Notice and Comment Procedures

NTU applauds the Strategic Operating Plan’s emphasis on providing guidance and certainty to taxpayers, including revision of notices “by simplifying the language,” “increasing the current rate from five to seven notices per year to as many as 500 per year,” “develop[ing] additional, tailored tax certainty programs,” and growing “capacity for addressing taxpayer issues through guidance interpreting the tax law.”⁵⁶

These efforts would have much more credibility if Congress or the courts were to affirm that the IRS must follow the Administrative Procedure Act requiring that “agency decisions be made only after affording interested persons notice and opportunity to comment.”

My colleague at NTU Foundation, Joe Bishop-Henchman, recently explained:

The IRS and the Treasury Department do not follow APA procedures for most of the hundreds of official changes they make annually to how they enforce the tax code, “having claimed for several decades that their rules and regulations are exempt from those requirements.” They characterize APA directives as merely interpretive, not legally binding, and therefore they are not subject to the APA. But even when the Treasury Department has initiated a formal notice-and-comment rulemaking process, it often skips steps. In more than 36 percent of cases, it made the proposed rule legally binding before accepting any comments, and in nearly 5 percent of cases, it skipped accepting comments and simply adopted the final rule.

It is no accident that the IRS set up a situation where it claimed its one-sided and burdensome regulation was both exempt from the APA process and unable to be challenged because of the Anti-Injunction Act, or that the IRS can take months to respond to taxpayers, but taxpayers automatically lose if they take even one extra day to respond. The *CIC Services* and *Boechler* decisions chip away at defenses that the IRS has often used to insulate its subregulatory “guidance” from legal challenge. But there still has not been a congressional or judicial declaration that the IRS must follow the APA.

⁵⁶ IRS. (April 2023). “Internal Revenue Service Inflation Reduction Act Strategic Operating Plan: FY2023 - 2031” pp. 52-54. Retrieved from: <https://www.irs.gov/pub/irs-pdf/p3744.pdf> (Accessed May 11, 2023.)

Until that happens, the IRS enjoys, as six federal judges observed in 2011, “a world in which no challenge to its actions is ever outside the closed loop of its taxing authority.”⁵⁷

The Service can also do more to clarify for taxpayers the degree to which they may rely on subregulatory guidance such as the Internal Revenue Bulletin, Revenue Procedures, and Technical Advice Memorandums. Furthermore, the “Job Aid” process, which involves practitioners more thoroughly in the mechanics of compliance with complex issues should be amplified.⁵⁸

7) Tax Simplification: The “Broken Record” that Keeps Playing

No other single item in NTU’s testimonies on tax administration over past decades has made the “top 10” list of recommendations than the need to simplify the tax laws. While we are well aware that this task is often extolled but rarely practiced, we once again offer some practical first steps.

Section 4022 (a) of RRA ‘98 required the IRS to produce an annual report to Congress on “sources of complexity in the administration of the federal tax laws.” The provision was successful, even though IRS compliance with it was limited. According to the National Taxpayer Advocate, the tax agency has issued just two annual reports compliant with the 1998 statute, but in both instances, “Congress adopted legislation to address each area of complexity referenced in the reports, and the IRS addressed the administrative problems they uncovered. Thus, the IRS’s decision to discontinue the reports has likely contributed to tax complexity.” The last report was published in 2002; Congress should order resumption of the annual reports now.

NTU also concurs with the Taxpayer Advocate’s recommendation that “the IRS establish a process to automatically provide the tax writing committee staff with a list of specific front-line technical experts who can discuss the administrability of pending (or existing) legislation directly with the tax-writing committees,” as provided in Section 4021 of RRA ‘98. The most important results would be in budgetary savings to the IRS and reduced private-sector compliance costs – a win-win situation for taxpayers.

Furthermore, the need for a regular review of the tax laws with an eye toward clearing away unnecessary, conflicting, or cumbersome provisions will always be extant. NTU’s staff recalls vividly from field hearings and other submissions to the Commission that many members of the private-sector tax community were willing to volunteer substantial time and energy to make

⁵⁷ Bishop-Henchman, Joseph. “Transforming the Internal Revenue Service.” Cato Institute Policy Analysis No. 942. April 11, 2023, p. 7. <https://www.cato.org/policy-analysis/transforming-internal-revenue-service>.

⁵⁸ See, as an example, Sepp, Pete. “IRS Considering Backdoor Death Tax Hike.” Comments to Internal Revenue Service re: Docket ID: IRS-REG-163113-02, RIN 1545-BB71. November 2, 2016. <https://www.ntu.org/publications/detail/irs-considering-backdoor-death-tax-hike>.

suggestions for simplification. A panel, meeting once every four years, would harness this volunteer activity.

There are several models for a process such as this, among them the creation of an executive branch body (e.g., via the Federal Advisory Committee Act). Its mission: to evaluate Title 26 of the U.S. Code and Title 26 of the Code of Federal Regulations in order to methodically identify specific opportunities for simplification, clarification, and repeal of provisions that are complex, contradictory, difficult to administer, or outdated, and provide actionable recommendations that the Executive and Legislative Branches can implement in expedited fashion.

Members would include individual taxpayers, business taxpayers, tax practitioners, tax attorneys, academics, and former public officials with an expertise in tax administration (subject to federal employment rules). The Commission's management could be drawn from the National Taxpayer Advocate's Office, the IRS Oversight Board, IRSAC, ETAAC, or the Treasury Inspector General for Tax Administration. Participation and consultation of Congressional staff would be invited and encouraged. The Commission's report could be partitioned according to those requiring legislative action and those necessitating executive action. In order to precipitate such action, the legislative portion could be required by law to be received by the tax-writing committees and brought to the floor under privileged consideration. The executive portion could be automatically referred to the rulemaking process under APA.

The preceding outline would require additional details. As we have been for 25 years, NTU is ready and willing to assist in developing the charter for this Commission.

8) Secure the Service's IT Capacity Before Launching Ambitious Cyber-Compliance Plans

At the Donald C. Lubick Symposium mentioned earlier, former Commissioner Charles Rossotti mentioned the need to "go slow" when ramping up new compliance strategies.⁵⁹ One area where NTU believes the IRS must indeed learn to walk before it runs is on the Information Technology track.

By now, every Member of this Committee is well aware of the Service's IT problems with customer service, and all of us hope that Commissioner Werfel's ambitious goal of completely revising the interoperability of the Individual Master File by 2028.⁶⁰ Although the Service's IT operations have certainly benefited from the leadership of Chief Information Officer (CIO) Sieger and hopefully from Acting CIO King, as the Government Accountability Office recently pointed out in February of this year, "[a]s of August 2022, the IRS had 21 modernization

⁵⁹ The full Lubick Symposium to which this paragraph refers may be viewed online at <https://www.taxpolicycenter.org/event/how-does-irs-intend-invest-80-billion-over-next-decade>.

⁶⁰ Rascon, Jose. "IRS Chief Aiming for Individual Master File Update by 2028." Meritalk, April 20, 2023. <https://www.meritalk.com/articles/irs-chief-aiming-for-individual-master-file-update-by-2028/>.

initiatives, including 9 to replace its outdated IT systems. However, 6 of those 9 initiatives did not specify how they would dispose of outdated systems—a key element in IT modernization.”⁶¹ This is but one of many challenges on the road ahead.

Still, there are many areas of IT at the Service outside of taxpayer-facing platforms that will need to be updated ... and none will require greater operational security than those platforms that will be designed for compliance research and data-gathering purposes. The Department of Justice has recently announced the formation of a Digital Asset Coordination Network to “combat the growing threat posed by the illicit use of digital assets to the American public.”⁶² Digital assets are a key focus of the IRS as well as IRA supporters who see opportunities for revenue enhancement through increased compliance funding.

Aside from the fact that international criminals are notoriously difficult targets for tax compliance efforts, the fact that the IRS will be “fishing in the pond” of digital assets more often means that cybersecurity will take on special importance. Even if the Service is interested primarily in compliance from those who aren’t running criminal schemes but are simply failing to properly pay taxes on legitimate digital asset transactions, the Service will be casting a wide net. Caught in that net will likely be some of the most skilled online malefactors in the world. The IRS must be prepared for *anything* to happen from these interactions. A breach of the Service’s IT systems could become a portal through which criminals or even bad-actor states could compromise our entire national security.

Furthermore, while technology is an important driver in enhancing taxpayer service and compliance, it is not without risks to both objectives. During a recent Tax Policy Center webinar entitled “Can Machine Learning Improve Tax Enforcement?” Alex Engler of the Brookings Institution expressed support for the IRS’s direction of its five-year-old machine learning techniques for detecting noncompliance but cautioned that the technology should be carefully monitored. As he explained, AI could improperly identify certain taxpayers for examination or enforcement, thus depriving them of certain deductions or credits. Some of the challenges to AI functioning properly in this area are that algorithms may be based on prior taxpayer case records, delays in court cases make “fresh” data problematic, and the shifting tax laws present a challenge

⁶¹ U.S. Government Accountability Office. “Information Technology: IRS Needs to Complete Modernization Plans and Fully Address Cloud Computing Requirements.” GAO-23-104719, January 12, 2023. <https://www.gao.gov/products/gao-23-104719>.

⁶² U.S. Department of Justice. “Justice Department Announces Report on Digital Assets and Launches Nationwide Network.” September 16, 2022. <https://www.justice.gov/opa/pr/justice-department-announces-report-digital-assets-and-launches-nationwide-network>.

to modeling. Also, parts of the tax code are very complicated, open to different interpretations and ambiguity.⁶³

The Strategic Operating Plan’s commitment to “[continue to implement best practices in cybersecurity]” is laudable, but given recent evaluations, much remains to be done. Last year, TIGTA found that the IRS failed to meet 17 of 20 “Core Inspector General Metrics” established for cybersecurity government-wide.⁶⁴ In addition to taxpayer services, cybersecurity must be a foundational priority for the Service before other initiatives can move forward. Congress must provide firm guidance to the IRS during the appropriations process to ensure both these ends are adequately funded out of existing resources.

9) Plan for Hearings on Other Approaches to Improving Compliance, Including Access to Courts and True “Community Engagement”

NTU continues to believe that as with any other area of compliance with laws, tax compliance benefits from the existence of safeguards to Americans’ fundamental rights. When citizens feel that everyone will get a “fair shake” from examinations, collections, appeals, jurisprudence, and other aspects of tax administration, they will more readily respect and follow the laws of the system. With so many compliance resources flowing to the IRS, the Committee could plan ahead.

Although the 1988 and 1998 taxpayer rights laws provided for certain exceptions, taxpayers still generally cannot enforce their rights in court until after they have been violated. Under Section 7421 of the Internal Revenue Code, no lawsuit can be brought by any person in any court for the purpose of restraining the assessment or collection of a tax, except under limited circumstances.

The case law around the Anti-Injunction Act further impedes the ability to restrain the collection of the tax. In theory, injunctions can be granted where the failure to grant relief would result in irreparable damage to the taxpayer, but in practice, this provision is virtually unusable. With the more recent *CIC Services* decision, the IRS can no longer hide behind the Act for every reason, such as penalty determinations. Nonetheless, the Declaratory Relief Act, which allows citizens to file a suit that can persuade a court to declare their rights, indicates that the law applies “except with respect to federal taxes.” The Federal Tort Claims Act presents additional barriers to tax-related controversies.

⁶³ See Tax Policy Center, Urban Institute Webinar. “Can Machine Learning Improve Tax Enforcement?” 2022. The entire webinar to which this paragraph refers may be viewed online at <https://www.youtube.com/watch?v=fIZYd3o7wJQ>.

⁶⁴ Gaetano, Chris. “TIGTA: IRS Cybersecurity Falls Short on 17 of 20 Metrics.” *Accounting Today*, July 21, 2022. <https://www.accountingtoday.com/news/tigta-irs-cybersecurity-programs-not-effective-falls-short-on-17-of-20-metrics>.

Congress should give serious consideration to providing citizens with the limited ability to stop the IRS from violating their rights through litigation. Doing so will involve some level of controversy, and will no doubt prompt lengthy deliberation. As a starting point, my colleague Joe Bishop-Henchman has suggested “narrowing the Anti-Injunction Act to limit only preliminary or temporary injunctions.” Another approach might be for Congress to re-codify the 10 taxpayer rights in the Protecting Americans from Tax Hikes Act of 2015 so that the rights may be invoked in actual disputes, instead of “mere suggestion[s] for IRS employees that they can safely ignore.”⁶⁵

Besides weightier issues such as these, during markup of a version of the Taxpayer First Act in 2018, NTU offered suggestions to improve the taxpayer experience in Tax Court. Several Tax Court officials, including Chief Special Trial Judge Peter Panuthos, have been contemplating a shift in the Court’s role to provide a fairer venue for taxpayers. At a 2017 International Conference on Taxpayer Rights, Judge Panuthos of the Court provided a truly compassionate (and in his case customary) view of his role, in discussing how he thought the Court might be able to engage in “affirmative judging”.

Andy Roberson of McDermott Will and Emery wrote:

Drawing on a report by a law school professor, Judge Panuthos discussed whether judges should follow the “passive norm” – just call “balls and strikes,” – or engage in affirmative judging (i.e., assisting taxpayers by asking questions and being more involved in the process). The discussion was very interesting, particularly with the point being made that in complex cases such as transfer pricing, judges routinely have conference calls with the parties and are actively engaged in trying to narrow the issues and get the parties to agree on what is really at issue.⁶⁶

Five years ago, the Tax Court’s Judicial Conference discussed several changes to procedures that Congress ought to encourage:

- Codification of how amicus briefs can be filed in Tax Court cases. Currently individual Tax Court judges have discretion over how and where they are accepted.
- Availability of more Tax Court documents (such as filings, not just decisions) online to the public, not just to litigants or those who are able to visit the Tax Court’s facility in Washington, DC. Appropriate privacy guidelines, especially for pro se taxpayers, would be necessary.

⁶⁵ Bishop-Henchman, Joseph. “Transforming the Internal Revenue Service.” Cato Institute Policy Analysis No. 942. April 11, 2023, p. 12. <https://www.cato.org/policy-analysis/transforming-internal-revenue-service>.

⁶⁶ Cited in Sepp, Pete. “Comments on the Taxpayer First Act to the Honorable Lynn Jenkins and the Honorable John Lewis.” April 4, 2018.

- Clearer and more consistent notices for non-party subpoenas.⁶⁷

The Committee could be very helpful by formulating legislative language either directing the Tax Court to develop these procedures or expressing the Sense of Congress that the Tax Court should do so.

NTU wishes to remind Committee Members in recognition of this hearing's title, that for many years traditional "law enforcement" oversight mechanisms have been discussed for the IRS as well. One was brought to the attention of the Restructuring Commission during its Omaha, Nebraska field hearing on April 4, 1997. During those proceedings, Samuel Walker, a Professor of Criminal Justice at the University of Nebraska-Omaha, offered a proposal for an IRS citizen review board. This office, modeled after citizen review and complaint entities established in many cities for police departments, would not be charged with resolving tax administration problems (the mission of the National Taxpayer Advocate) or allegations of criminal behavior (investigated through the Inspector General or the Department of Justice). Rather, it would hear taxpayer concerns over specific instances of mistreatment by IRS personnel and make recommendations for disciplinary action.

Walker outlined a structure whereby an External Independent Complaint Auditor, appointed in consultation with Congress, would oversee an Internal Office of Citizen Complaints to receive specific reports from citizens and, summarize annually any changes to personnel procedures that might help to minimize incidents and complaints in the future. The Restructuring Commission's final report proposed, instead, that the IRS should "centralize the cataloging and review of taxpayer complaints of IRS misconduct on an individual employee basis." This advice, subsequently embedded in RRA '98, has failed to provide a more formalized grievance procedure which, along with regular reporting on personnel remedies that a citizen review board can provide, could result in more productive resolution of disciplinary problems among tax agency employees.

Congress could request a study from the IRS Oversight Board or National Taxpayer Advocate to evaluate the experiences of city police department complaint entities since 1997, and explore the suitability of updating Walker's proposal to current circumstances with the Strategic Operating Plan.⁶⁸

There are many other aspirational proposals we would gladly raise with Committee Members. The ones outlined here would plainly require bipartisan alignment that would need to take place over a potentially lengthy period of time. Nonetheless, it will pay – literally – to think ahead

⁶⁷ *Ibid.*

⁶⁸ For background see, Sepp, Pete. "Comments before the Subcommittee on Oversight, Committee on Ways and Means, 'IRS Reform: Resolving Tax Disputes,'" September 13, 2017. <https://www.ntu.org/publications/detail/irs-reform-resolving-taxpayer-disputes>.

about proposals such as these, while the Committee concentrates on near-term goals such as those articulated in legislative form below.

10) Work on Bipartisan Legislation for Much-Needed Reforms to Tax Administration

Despite recent, and at times heated, political rhetoric over the IRS and the \$80 billion funding infusion provided to the agency by the IRA, lawmakers in both parties continue to work together on legislation that would improve tax administration. Doing so would foster a spirit of cooperation that could make all of the 9 recommendations above less difficult to confront.

Last month, NTU was proud to support the Taxpayer Advocate Enhancement Act, introduced by Sens. Ben Cardin (D-MD) and Bill Cassidy (R-LA) in the Senate (S. 1283)⁶⁹ and Rep. Randy Feenstra (R-IA) and four bipartisan cosponsors in the House (H.R. 2755).⁷⁰ This legislation would allow the National Taxpayer Advocate (NTA) to appoint her own counsel, enhancing the independence of the Office of the Taxpayer Advocate and improving the NTA’s ability to provide sound, sensible, and non-partisan recommendations on tax administration policy. NTU has supported allowing the NTA to hire her own counsel for years, since former NTA Nina Olson first included the recommendation in the annual “Purple Book.”⁷¹

Last month we also supported the Cutting Paperwork for Taxpayers Act (H.R. 2978),⁷² introduced by Reps. Abigail Spanberger (D-VA) and Young Kim (R-CA). This commonsense legislation would prevent taxpayers receiving a late refund from the IRS from then also having to pay taxes on the interest they justly receive for the agency’s delays.

Bipartisan legislation introduced earlier in the 118th Congress by Sens. Chuck Grassley (R-IA) and Chair Wyden (D-OR) in the Senate, and Rep. Mike Kelly (R-PA) in the House, would significantly enhance whistleblower protections at the IRS. This important bill, the IRS Whistleblower Program Improvement Act (S. 625, H.R. 1300),⁷³ dovetails with two critical and long-running initiatives advanced by NTU: improving federal tax administration and enhancing

⁶⁹ Congress.gov. “S.1283 - Taxpayer Advocate Enhancement Act.” Introduced April 25, 2023. Retrieved from: <https://www.congress.gov/bill/118th-congress/senate-bill/1283> (Accessed May 11, 2023.)

⁷⁰ Congress.gov. “H.R.2755 - National Taxpayer Advocate Enhancement Act of 2023.” Introduced April 20, 2023. Retrieved from: <https://www.congress.gov/bill/118th-congress/house-bill/2755> (Accessed May 11, 2023.)

⁷¹ For the latest Purple Book, released in January 2023, see: Taxpayer Advocate Service. “National Taxpayer Advocate 2023 Purple Book.” January 2023. Retrieved from: <https://www.taxpayeradvocate.irs.gov/reports/2022-annual-report-to-congress/national-taxpayer-advocate-2023-purple-book/> (Accessed May 11, 2023.)

⁷² Congress.gov. “H.R.2978 - Cutting Paperwork for Taxpayers Act.” Introduced April 27, 2023. Retrieved from: <https://www.congress.gov/bill/118th-congress/house-bill/2978> (Accessed May 11, 2023.)

⁷³ Congress.gov. “S.625 - IRS Whistleblower Program Improvement Act of 2023.” Introduced March 2, 2023. Retrieved from: <https://www.congress.gov/bill/118th-congress/senate-bill/625> (Accessed May 11, 2023.); Congress.gov. “H.R.1300 - IRS Whistleblower Program Improvement Act of 2023.” Introduced March 1, 2023. Retrieved from: <https://www.congress.gov/bill/118th-congress/house-bill/1300> (Accessed May 11, 2023.)

federal protections for courageous individuals blowing the whistle on wasteful spending or abuse of power within the government.

Another bipartisan bill introduced in the current session of Congress, the Electronic Communication Uniformity Act (S. 1338)⁷⁴ from Sens. Marsha Blackburn (R-TN) and Catherine Cortez Masto (D-NV), would “[provide] that such documents and payments [submitted electronically to the IRS by taxpayers] shall be deemed filed or made on the date on which they are sent electronically, regardless of the date on which the IRS actually receives or reviews them.” This legislation would establish parity between electronic and paper filings, a recommendation NTU called for in an April 2022 written submission to this Committee.⁷⁵

In summary, there is no shortage of productive, constructive, and bipartisan bills for this Committee to consider in the months ahead that could reform IRS procedures and processes and improve tax administration as the agency embarks on spending up to \$80 billion in supplemental funding over the next 10 years. There may be little to no agreement among the two parties over whether to keep or rescind the supplemental funding provided to the IRS by the IRA, and there may be even less agreement over how much supplemental funding may yield additional revenues for the Treasury, but there are plenty of areas of agreement that would improve the IRS and the taxpayer experience with the agency.

At Your Service: The Taxpayers FIRST Project

Asking policymakers from many perspectives to work together, as this testimony does, is easier said than done. Nonetheless, perhaps the Committee can draw some encouragement from a recent undertaking by the National Taxpayers Union Foundation.

Taxpayers for IRS Transformation (Taxpayers FIRST) is designed to convene an expert group of non-governmental stakeholders with a diverse set of backgrounds and perspectives to offer guidance to the IRS as it plans to spend the most significant infusion of funding it has ever received. The Project aims to assist IRS officials and policymakers so that the new funding is spent effectively, improves taxpayer services, upgrades outdated technology, and helps efficiently reduce the tax gap while respecting and strengthening taxpayer rights and due process.⁷⁶ These experts include:

- Nina Olson, former National Taxpayer Advocate

⁷⁴ Congress.gov. “S.1338 - Electronic Communication Uniformity Act.” Introduced April 27, 2023. Retrieved from: <https://www.congress.gov/bill/118th-congress/senate-bill/1338> (Accessed May 11, 2023.)

⁷⁵ Sepp, Pete; and Lautz, Andrew. “NTU Submits IRS Reform Recommendations Ahead of Agency’s Budget Hearing.” NTU, April 7, 2022. Retrieved from: <https://www.ntu.org/publications/detail/ntu-submits-irs-reform-recommendations-ahead-of-agencys-budget-hearing> (Accessed May 11, 2023.)

⁷⁶ For further information and updates in the Taxpayer FIRST project’s activities, please visit www.taxpayers-first.org.

- Fred Goldberg, former Commissioner of the IRS
- Caroline Bruckner, Managing Director of the Kogod Tax Policy Center
- Jason Fichtner, Vice President and Chief Economist at Bipartisan Policy Center
- Jeff Trinca, former tax counsel for Senator David Pryor (D-AR) and currently founding Vice President with Van Scoyoc Associates
- Janet Holtzblatt, Senior Fellow at the Urban-Brookings Tax Policy Center
- Erica York, Senior Economist at Tax Foundation
- Renell Dubay, Kay Perrone & Associates
- Gordon Gray, Director of Fiscal Policy at American Action Forum
- Fred Forman, former IRS Associate Commissioner of Business Systems Modernization
- Jason DeCuir, Partner at Advantous Consulting
- Adam Michel, former Deputy Staff Director of the Joint Economic Committee and current Director of Tax Policy at Cato Institute
- Barbara Robles, former principal economist at the Federal Reserve Board of Governors as well as the Joint Committee on Taxation and former tax examiner for the IRS
- Alex Brill, Senior Fellow at American Enterprise Institute
- Peter Mills, Senior Manager of Tax Policy at AICPA
- Rebecca Thompson, Vice President of Strategic Partnerships & Network Building at ProsperityNow

These individuals, joined by leaders from the National Association of Enrolled Agents and more to follow, will be conducting many consultative sessions this year on matters such as measuring the tax gap, improvements to customer service, modernization, and protection of taxpayer rights and privacy. Taxpayers FIRST will be presenting its recommendations in reports to be released at public events into 2024.

The National Taxpayers Union Foundation has been able to initiate Taxpayers FIRST in part to serve as a resource to policymakers who are earnestly seeking solutions to many of the challenges facing the IRS's future success. This panel of experts, which will add members over time, will be available on tax administration matters at any point in time. Please consider Taxpayers FIRST to be an advisor in the Committee's work.

Conclusion

How do organizations execute successful transformations? This is the central question subsequent to the enactment of \$80 billion of additional funding for the IRS. In my opinion, such transformations, whether in the private or public sectors, come from several sources.

- **From employees.** Private companies, on occasion, are prompted to change through their workforces. IRS workers proved to be key in advising the National Commission on Restructuring the IRS, as well as this Committee during the deliberations over RRA '98. They were able to identify leadership, personnel policy, and structural issues that were

standing in the way of success for the Service's next chapter. So far, Congress has heard little from Service employees about the Strategic Operating Plan.

- **From customers.** Private sector actors are under constant pressure to innovate and deliver, at the risk of losing customers. To be frank, taxpayers can't choose which IRS to use, and therefore are not "customers" in the conventional sense. They can only exert a modest degree of influence over the way the Service operates by volunteering for IRSAC, ETAAC, the Taxpayer Advisory Panels, and occasionally, through litigation.
- **From competitors.** Loss of market share from firms that provide a product faster, cheaper, and better often incentivizes private sector companies to keep innovating or fade away. Here again, except for a few Americans who take the drastic step of renouncing citizenship, the IRS has no "competitor" at the federal level. "Patriotic" or not, companies and individuals abroad seeking to invest in the United States, as well as those already here who are contemplating expansion, can evaluate whether tax administration climates elsewhere in the world are more hospitable.
- **From shareholders.** This group is a fulcrum of leverage that can often change the entire direction of a private company. Alas, there is not a direct equivalent in government, save the voters, who get to speak more on the general path of government than specific issues like IRS management.
- **From boards of directors and others.** Many private sector companies are re-oriented in a more productive direction by positive action from boards of directors and other entities that are outside the day-to-day management structure. So it must be with the IRS – a functioning Oversight Board, along with IRSAC, ETAAC, TAPs, Congress, and institutions outside government such as Taxpayers FIRST, and many, many more institutions yet to weigh in, can have a role in a transformation for which all Americans have a stake.

This testimony has been broken into sections using the theme of "realities," no doubt leading some to wonder whether the recommendations above are realistic themselves. The answer is, they have to be. No, activities such as rebalancing the role of the courts, or imposing a tax simplification process, can happen overnight. But other steps, such as reconstituting the IRS Oversight Board and evaluating the IRA funding mix, can and should happen now.

Each item in these recommendations may have its own timetable, *but several are well within the grasp of this Congress, this year.* For the sake of all taxpayers, let us move forward.

I am most grateful to all of you for engaging in this hearing and for devoting so much attention to these lengthy remarks.