HEARING ON THE NATIONAL TAXPAYER ADVOCATE'S 2015 ANNUAL REPORT TO CONGRESS

BEFORE THE HOUSE COMMITTEE ON OVERSIGHT AND GOVERNMENT REFORM,

SUBCOMMITTEE ON GOVERNMENT OPERATIONS

Written Statement, Jim Buttonow, Chairperson, IRS Electronic Tax Administration Advisory Committee

April 15, 2016

Chairman Meadows, Ranking Member Connolly, and distinguished Members of the Subcommittee:

Thank you for holding today's hearing on the National Taxpayer Advocate's 2015 Annual Report to Congress. The National Taxpayer Advocate (NTA) and her office are valuable voices for the rights for all taxpayers and the improvement of overall tax administration. The IRS Electronic Tax Administration Advisory Committee (ETAAC) has always and will continue to collaborate with the NTA on important tax administration issues.

ETAAC objectively advocates for electronic tax administration improvements

ETAAC was formed in 1998 to provide Congress with strategies on how to improve tax administration through electronic means. During the past 17 years, ETAAC members have been tax and technology experts from private industry and government. The committee reports directly to Congress each year in an annual report published before June 30. ETAAC members take seriously their objective responsibilities to improve overall tax administration using electronic strategies. This committee has provided short-term tactics and long-term strategies for the IRS and Congress to address the most serious problems and goals in tax administration.

In 1998, ETAAC's main purpose was to help the IRS reach its goal of having 80% of tax returns filed electronically. At the time, that seemed like a tremendous endeavor. However, the IRS pursued various strategies and partnered with the tax industry to meet and surpass the important 80% e-file goal. As Congress intended, ETAAC has turned to other issues in tax administration.

Namely, ETAAC has been and continues to be focused on two big challenges in tax administration today:

1. The erosion of the tax system's integrity from the proliferation of tax identity theft, and
2. Inadequate levels of taxpayer service at the IRS.

ETAAC believes that the IRS can make great strides toward solving these problems through innovation.

The first big problem: Tax identity theft

Today, tax identity thieves have ample opportunity to steal taxpayers' personal identifiable information and file a tax return for them. To urgently address this issue, IRS Commissioner John Koskinen formed the Security Summit, a partnership made up of the IRS, state tax administrators, and industry, to find solutions to the challenges the IRS faces in authenticating tax filers and detecting stolen identity refund fraud.

Last year, the Security Summit developed new techniques to combat these problems, including:

- New ways to validate the authenticity of taxpayers and information included on tax return submissions
- Information-sharing to improve detection and expand prevention of refund fraud, and
- Threat assessment and strategy development to prevent risks and threats.

The Security Summit continues to work to find new solutions that will ultimately bring this problem under control. ETAAC advocates that these ultimate solutions will improve the IRS' ability to verify taxpayer identities before or at the time they file their returns.

In ETAAC's 2016 report to Congress, we explore opportunities for the IRS to validate taxpayer identities before the IRS issues a refund. We will be recommending, as many groups have in the past, that the IRS receive third-party taxpayer information earlier in the tax-filing season to allow the IRS to match the information against tax-return data to validate taxpayers and their information. ETAAC recommends that the IRS and Congress work to replace the current "look-back" compliance system that operates with verification and compliance checks after a return is accepted. Instead, the IRS should move toward a front-loaded process that allows the IRS to check the accuracy of a return and validate a taxpayer *before* accepting his or her return.

ETAAC will also be recommending that the IRS explore a taxpayer-registration process to confirm taxpayers' identities before accepting a return – much like businesses verify their customers before conducting business with them. These common-sense approaches used to be far-fetched, but with modern technology and collaboration between the IRS and Congress, these can be a near-term reality.

The second big problem: Inadequate levels of taxpayer service

For most taxpayers, interacting with the IRS is not quick, it's not easy, and it's mostly done by paper and phone. Most taxpayers have no idea about their tax information or their status at the IRS. And when they do have to interact with the IRS, they can face long wait times and extended answer periods.

The current state of service and lack of digital tools at the IRS could leave us feeling pessimistic about the near-term possibility of solving the taxpayer-service issue. However, the IRS has a long-term vision and a plan to enable digital taxpayer service. The comprehensive strategy started as the IRS Concept of Operations, or ConOps. This plan provided an iterative approach to building electronic taxpayer service features that will create a 21st-century experience when taxpayers interact with the IRS. The ConOps strategy is the backbone of the current IRS Future State Initiative.

ETAAC has looked closely at the ConOps strategy and its digital-service components. We have endorsed implementation of the digital service components of the plan. To take it a step further, we have advocated to Congress that the IRS accelerate its digital taxpayer service plans.

ETAAC's vision for digital innovation at the IRS

During the past three years, ETAAC has been focused on the future state of the IRS. But what does the future state look like?

ETAAC envisions a taxpayer experience that allows taxpayers to:
- *Fully understand their tax obligations*
- *Have transparent access to their tax information and status with the IRS, and*
- *Effectively and securely interact with their tax administrator in the way that they want to be served.*

Here is a breakdown of each component in ETAAC's vision to explain exactly what ETAAC has been advocating for:

A primary focus on the taxpayer experience reduces burden. Focusing first on the taxpayer experience means that the IRS provides personalized service, rather than a one-size-fits-all model. The future IRS understands who you are as a taxpayer, what you need, and how you want to be served.

Helping taxpayers understand their obligations helps them comply. Taxpayers need transparency. They need to understand their tax obligations and have access to their tax information and status with the IRS. If taxpayers have better information about what is expected of them before, during, and after filing, the entire process will be less mysterious. Taxpayers will feel more empowered and more confident about the fairness of tax laws – all of which encourages voluntary compliance.

Digital tools can replace outdated processes with real-time service. With electronic access to their IRS accounts, taxpayers can evaluate their circumstances, understand their options, and effectively and securely interact with the IRS.

The IRS must serve taxpayers in the way they want to be served. Some taxpayers want to get information and complete transactions online and stay off the phone. Others want to chat or call, or visit a Taxpayer Assistance Center or VITA site. And many want their tax professional to handle it all for them. The IRS should provide all of these options to meet the variety of taxpayer preferences.

The result will be a significant shift – meaning taxpayers will no longer have to bend to fit the IRS' customer-service mold, and instead, the IRS will be flexible enough to serve taxpayers in the way they want to be served.

The data has something to say about what taxpayers need and want. According to the IRS Oversight Board's last study on taxpayer attitudes, 43% of taxpayers had to interact with the IRS outside of filing a tax return – that is, they needed taxpayer service. In today's environment, digitally enabled, real-time information and service is the standard. Consumers – and taxpayers – expect these capabilities.

What about taxpayers who can't go online, prefer not to, or need to talk to a person?

In the digitally enabled IRS future state, taxpayers who want or need to deal with the IRS in person or by phone are not left behind. By creating digital capabilities for taxpayers to more efficiently and effectively interact with the IRS, the IRS can solve two big problems at once:

- It can meet the growing digital service expectations of taxpayers, and
- It can free up phone lines and people for issues that require human interaction and for taxpayers who really need and prefer a person.

How the IRS and Congress can overcome obstacles to building the future state

Implementing the future state of taxpayer service won't be easy. The IRS faces several obstacles to accelerating these plans that it will need to overcome. Here's how the IRS should start.

1. The IRS needs to make security of taxpayer information the first priority.

Recent attacks on IRS systems have been the result of a slow-moving roadmap. The IRS hasn't been able keep up with the real-time pace that is required to maintain online security in today's world. As the IRS enters the modern online customer-service environment, it will need to create an organizational structure around security and commit to taking on that responsibility. Online security is not about building a feature; it is a fundamental effort that requires continual maintenance and enhancement to protect taxpayer information.

2. The IRS needs to be more deliberate in executing its digital taxpayer service plans.

While ETAAC believes that the IRS has taken an important first step with its digital service plans, we also encourage the IRS to quickly commit to release dates. The lack of planned release dates creates a perception that the IRS may not be fully committed to digital enablement and that the plans could be more aspirational than strategic.

3. The IRS needs to be more transparent and collaborative with Congress on its digital plans.

This is simple. Congress doesn't know the IRS' plans to solve taxpayer service issues. The IRS needs to communicate its strategies and work with Congress to make those plans a reality. The IRS should provide Congress with its plans and the associated costs and benefits of developing digital service. With this information, Congress can make informed decisions on what taxpayers will get for their investment. The IRS plans to include Future State digital-service goals, plans, and return-on-investment data in its next strategic business plan and future budgets.

4. The IRS needs to partner with stakeholders to provide taxpayer service.

The IRS needs to recognize that most taxpayers will go to a trusted source for tax help. That's either a tax professional or tax software. More than half of taxpayers use a tax professional for their tax compliance needs, and more than 90% of tax returns are filed using tax software.

Since most taxpayers use these third parties, the IRS can leverage them to help with taxpayer service. How? The IRS should provide taxpayers with easier access to their information through tax software. And the IRS should build tax professional online accounts, and allow taxpayers to authorize their tax professionals to get access to their information.

5.   The IRS needs to embrace change by cultivating an environment of innovation.

Change is difficult within any large organization. Embracing innovation is even harder. But innovation allows organizations to find ways to do more with limited resources, and to do it better. ETAAC believes that the IRS is headed in the right direction with its recent formation of a Digital Subcommittee, made up of IRS executive leaders. This subcommittee is focused on strategies for creating and prioritizing digital solutions. It's an important first step in cultivating an environment of innovation. The next step, and perhaps the hardest for the IRS, is to execute its digital service plans. ETAAC is closely monitoring IRS progress in moving beyond conceptual and planning phases and into execution to make these plans a reality.

6.   Taxpayer service needs to be the priority at the IRS.

Specifically, the mindset at the IRS needs to be "service first, compliance second." As the Taxpayer Advocate pointed out last year, the IRS budget is still predominantly funded toward compliance enforcement. The IRS needs to always remember that more than 98% of all taxes paid into the U.S. Treasury are paid voluntarily. Strategically, prioritizing service efforts for taxpayers who file and pay is much more fruitful than focusing on the noncompliant, especially in lean budget times. With a taxpayer service-first mindset, tough priority decisions would clearly lean toward enabling better service to taxpayers. That includes funding decisions to accelerate building a secure online account for taxpayers to do business with the IRS.

ETAAC's specific recommendations

ETAAC has made recommendations to Congress for the IRS to implement electronic service components and to change the way it does business. In fact, many of our recommendations from the past three years are incorporated in the IRS Future State Initiative. Here is a summary of some of those recommendations:

2014 Report

In ETAAC's 2014 Annual Report to Congress, we recommended that the IRS build secure, personalized online accounts for individual and business taxpayers and their tax professionals. In our recommendations, we provided IRS data illustrating consumer behavior, preferences, and adoption of online tools. We emphasized the importance of creating capabilities that would allow taxpayers to securely authorize third parties to help them with their tax obligations. We painted the big picture for the IRS by providing recommendations for features that would help taxpayers understand their tax information and obligations, and interact with the IRS more efficiently and effectively.

The 2014 report and its 11 recommendations: https://www.irs.gov/pub/irs-prior/p3415--2014.pdf

2015 Report

In ETAAC's 2015 Annual Report to Congress, we built on the previous year's observations and recommendations. We pointed out that the IRS was stalling in its commitment and strategy to provide digital taxpayer service. The IRS needed to enable a culture of innovation to find scalable digital solutions to its taxpayer service problem.

To that end, we recommended specific ways in which the IRS could change its organization and operations to be more agile. This would allow the agency to accelerate the development of electronic tools that would be the foundation of many future taxpayer service capabilities.

We provided recommendations on how the IRS can gain adoption of online accounts, especially considering taxpayer apprehension about dealing with the IRS. We encouraged the IRS to work with the tax industry and other partners to gain adoption of online accounts, much like the IRS leveraged tax professionals and the tax software industry over the past 20 years to streamline tax-return processing through e-filing, and to reduce return-filing error rates and costs. In researching electronic capabilities of state taxing authorities, such as New York State, we found success stories and learnings that the IRS could leverage in developing, deploying, and supporting digital taxpayer service.

The 2015 report and its 15 recommendations: https://www.irs.gov/pub/irs-pdf/p3415.pdf

2016 Report

This year's report, due June 30, 2016, will also provide recommendations about the future state of the IRS. To combat stolen identity refund fraud, increase the accuracy of filed returns, and fix a fundamentally reactive tax system, ETAAC is recommending that the IRS receive more accurate information earlier in the tax season to verify the accuracy of returns before sending refunds to taxpayers.

These recommendations are not new concepts, but they build on many discussions around a front-loaded tax system that have been introduced in the past few years. The time gap is narrowing between when the IRS receives information and when a return is filed, but more fundamental changes would allow the IRS to verify tax return information *before* issuing refunds.

In this year's report, ETAAC is also recommending that the IRS explore a taxpayer-registration system that would allow the IRS to verify a taxpayer's identity and establish an IRS account, much like businesses validate customers' identities and communicate the terms of business upfront. These recommendations are more relevant than ever before, given the continuing proliferation of tax identity theft and the need for the IRS to transform the way it serves taxpayers.

The 2016 report will also recommend additional improvements the IRS should make to provide comprehensive service to taxpayers and their tax professionals before, during and after filing.

The report can be found at IRS.gov on June 30, 2016.

The time to build the future state is now

In closing, the future state of the IRS enables technology as a part of a holistic taxpayer service strategy. The future state embraces digital solutions to allow the IRS to maximize its limited resources. It creates targeted capacity to serve all taxpayers the way they want to be served.

And, importantly, the future state is reflected in taxpayers who understand their tax obligations, have transparency to their tax information, and can file, pay, and comply with tax laws effectively and efficiently.

The IRS should not delay. The IRS needs to prioritize and accelerate its digital service strategy now to invest in voluntary compliance, taxpayer service, and the integrity of the tax system.

Jim Buttonow, CPA, CITP

Jim Buttonow, CPA, CITP, of Greensboro, NC, is a subject matter expert in tax controversy and tax administration. For the past two years, Jim has served as chairperson of the IRS Electronic Tax Administration Advisory Committee (ETAAC), which issues an annual report to Congress on how to advance electronic tax administration. ETAAC promotes the IRS digital-first strategy to develop transformative technology solutions to systemic challenges in tax administration. As part of Jim's ETAAC role, he has presented committee priorities to Congressional committees, staff, and the IRS Oversight Board.

Jim directs tax practice and procedure services and software for H&R Block, where he designs tax problem-solving products and services. Since 2006, Jim has also been in private practice. For 19 years, Jim worked at the IRS, serving as a large case team audit coordinator for 15 years.

Jim writes regularly on tax controversy and tax administration issues, develops and presents CPE series on IRS practice and procedure, and regularly speaks on compliance trends and post-filing practice efficiency strategies for CPA societies and private firms. He earned a B.S. in Accounting from the University of South Florida.