IRS Oversight Board Public Meeting
March 2, 2011

A SUMMARY OF DISCUSSION AND COMMENTS

OVERVIEW OF THE IRS OVERSIGHT BOARD PUBLIC MEETING

Welcome and Introduction

On March 2, 2011, Board Chair Paul Cherecwich, Jr. welcomed attendees to the special tenth anniversary public meeting conducted by the IRS Oversight Board. He said the two former co-chairs of the National Commission on Restructuring the IRS, former Senator Bob Kerrey and current Senator Rob Portman, would both address the meeting. He noted that without their great work ten years ago, there would not have been an IRS Oversight Board. He further said that the passage of the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98) resulted in a wide range of changes that made for more effective tax administration over the past ten years.

The Chair said the meeting would consist of two panels that address important issues in tax administration, and that the Board had invited recognized experts, Nancy Killefer and Pamela Olson, to serve as moderators and guide the panel discussions. He said both had served in senior positions in the Treasury Department and in the private sector.

Chairman Cherecwich introduced the Board's guests for the forum, James R. White, Director Strategic Issues, Government Accountability Office (GAO); and J. Russell George, Treasury Inspector General for Tax Administration (TIGTA). He said IRS Commissioner Doug Shulman was in budget discussions, but would attend later in the session.

Chairman Cherecwich introduced Senator Robert J. Kerrey, noting his impressive career as a congressional medal of honor recipient, the 35th governor of Nebraska, U.S. Senator from Nebraska, co-chair of the National Commission on Restructuring the Internal Revenue Service, and most recently, as president of the New School University in New York City.

Summary of Senator Kerrey's Remarks

Senator Kerrey opened his remarks by saying that he wanted to emphasize that the IRS, in his view, is one of the least known and most under-appreciated administrative and technological successes in our country. He thanked all of the men and women who work for the IRS and have worked hard to implement the '98 Act and carry out their difficult missions every day. He also thanked the congressional authorizing and appropriating committees as well as Presidents Bush and Obama for their support for the changes to the IRS and support for the budgets that enabled the IRS to succeed.

Kerrey encouraged the audience to consider the three most important things for a represented democracy to do; raise taxes in a fair and equitable way, service the people who are paying those taxes; and attempt to collect from those who voluntarily decide that they will not obey the law. He noted that the IRS is the only federal agency that touches every household, and it is very important that taxpayers feel the agency is treating them fairly while operating at the highest levels of efficiency. Just as important, he said, is that taxpayers must feel that there is a reasonable, accessible, affordable and speedy process to resolve disagreements.

Senator Kerrey emphasized that the intent of the IRS Restructuring Act of 1998 was to reorganize the IRS according to successful structures in the private sector. A Taxpayer Bill of Rights was created, along with the IRS Oversight Board. The IRS became the most efficient tax collection agency on earth, while providing improved taxpayer service and successfully deploying new information technology. He recounted the effort put forth by the restructuring commission to develop a vision for IRS success, and he said a guiding principle to the commission was that taxpayer satisfaction had to be an important a part of the IRS mission.

Kerrey praised the IRS for success with e-filing, updating its technology, smooth filing seasons despite late law changes, recruiting and training a quality workforce, and continuing to grow more efficient. He thanked everyone who has been a part of the efforts to improve the IRS.

Following Senator Kerrey's comments, Chairman Cherecwich introduced the Moderator of Panel 1, Nancy Killefer. Ms. Killefer served as assistant secretary for management and Chief Financial Officer in the Department of the Treasury; she was a charter member of the IRS Oversight Board and served as the second chair of the Board. She presently is the senior director and head of the Washington, DC office of McKinsey & Company, where she focuses on how to improve performance within the financial and human resource limits that all organizations face. She worked closely with the IRS on strategic planning and on the Workforce of Tomorrow Task Force.

Panel 1: People and Partnership Assets in Future Tax Administration

Moderator: Nancy Killefer, McKinsey & Company
Panelists:

- *Claudia Hill, EA, MBA*, President of TaxMam, Inc.
- *Joel Slemrod*, Professor of Economics, University of Michigan
- *Elizabeth Tucker*, IRS Deputy Commissioner, Operations Support
- *Thomas Dohrmann*, partner, McKinsey & Company

Ms. Killefer said she was honored to participate in the Board's public meeting; she described the Board as a unique institution composed of private citizens that endeavors to help support and improve the performance of the IRS, and that it has served the IRS very well. She briefly described the vast improvements in customer service enacted by the IRS over the past ten years, and noted that her view of the original problem was that the IRS did not fundamentally understand their constituent taxpayers. She said the IRS today is organized along the lines of and has a deep knowledge of its taxpayer segments. She said the agency is on the verge of using information to better understand taxpayer needs as well as compliance issues, and she congratulated the agency on its progress.

Ms. Killefer then asked each of the panelists to introduce themselves and make a brief statement.

Claudia Hill, a noted practitioner, has worked closely with the IRS and spoke to the partnership relationship the practitioner community has with the IRS. She said there would not be the same level of voluntary compliance without return preparers who provide quality services to their clients. She believes they have been and will continue to be part of the solution for tax administration. She said the IRS will emphasize the positive in its efforts to leverage preparer regulation to the mutual benefit of taxpayer, tax preparers, and tax administration. She said while the return preparer initiative will give the IRS more information about preparers and enable better monitoring and oversight, she believes that education and the message of dual responsibility to the client and to the system, and to the quality of the returns entering the system, presents the greatest potential for the program.

Joel Slemrod, professor of business economics and public policy at the University of Michigan, spoke of behavioral economics and how that affects compliance with the tax code. As to what motivates compliance, he said it is clear that it is deterrence and enforcement. As an example, he cited the non-compliance rates for different kinds of income. Where there is information reporting and withholding, the non-compliance rate is 1.2 percent. For income where there is little or no information reporting and no withholding, the IRS estimates the non-compliance rate is 53.9 percent. He suggested extending where possible information reporting of income.

Slemrod also said people have speculated that compliance behavior will depend upon the fairness of the tax system, among other factors, and that heavy-handed enforcement might bring about a result other than a dutiful one. In a constrained budget environment, he said the principle mission of the IRS is still to raise revenue, fairly and efficiently, so enforcement is still of primary importance. However, he did note that reducing frustration and improving service has an important value of its own.

Elizabeth Tucker, IRS Deputy Commissioner for Operations Support, said that the reason our tax administration system continues to work is because of the dedication of the men and women of the IRS. She said the IRS leadership continues to look to the future and prepare to ensure the right people, the right technology and the right systems are in place to meet the challenges ahead. She discussed the goals of the IRS Workforce of Tomorrow task force and the tremendous amount of energy it created towards recruiting for the next generation of workers at the IRS. She stressed the importance of developing an engaged workforce and the challenges of meeting the needs of a those new IRS workers.

Ms. Tucker praised the IRS for its results in last year's Annual Best Places to Work in the Federal Government Survey; the IRS is now ranked 79th out of 224 government agencies, compared to 127th the year before. She also praised the IRS workforce for the results of the overall employee engagement index; the IRS jumped from eighth out of fourteen large government agencies to number three. She said the remarkable results were due to the agency investing more in training and technology and making employees feel valued.

Tom Dohrmann, partner at McKinsey & Company, talked about his work over the past few years leading a research effort with the OECD to look at tax administration practices in 15 countries. Based on his experience, he said there are certain aspects that allow the IRS to perform well and are also a roadmap for the future. He said that having insight about taxpayers based on the data available, which allows for segmenting them into appropriate groups for tailored service, education, outreach and targeted enforcement, is at the heart of increasing voluntary compliance. He noted an interesting metric collected from tax administration systems around the world, the audit no change rate. The IRS has the lowest no change rate in the world, which generally means it is efficiently using its resources compared to other tax systems. He said that the IRS' tailored processes are high quality and allows the agency to touch at least twice as many taxpayers as any other tax authority in the world. Coupling insight with data to segment taxpayers and tailor enforcement approaches to them allows the IRS to achieve the success it has. Looking at the right issues on the enforcement side has a positive reinforcing effect on deterrence. He said there are opportunities to improve and strengthen the system using the same approach.

Ms. Killefer asked the panelist to choose one top priority for investment, considering the budget realities of the next few years. Ms. Tucker would invest in technology, which would return multiple benefits to the IRS, including advances in training and employee engagement. Mr. Slemrod would invest in continual learning about what works best, both for service and enforcement. Ms. Hill would invest in customer service, especially telephone assistance for taxpayers. She also complimented the IRS communication efforts with the practitioner community and the IRS web site for providing useful information quickly. Mr. Dohrmann would invest in the combination of research and technology, to develop databases to mine for targeted enforcement efforts.

Board Chair Paul Cherecwich asked Ms. Hill what she thought practitioners could do to help the IRS reach out to those individuals who should be filing tax returns but who do not. She responded that the tax practitioner industry, given the chance to acquire new clients, would jump on the opportunity. She suggested the IRS might have an opportunity to work with preparers coming into the new preparer registration system to encourage a positive attitude toward voluntary compliance.

Mr. Tobias asked the panelists how they would advise the IRS about resetting expectations in times of a budget crunch. Mr. Dohrmann suggested a lean budget environment would provide opportunities for innovation and a rethinking and reworking of standard operating procedures. Ms. Tucker said the IRS had asked for employee suggestions regarding ways to deal with budget reductions and was pleased that so many employees became engaged in the process and responded positively.

The panel discussion concluded, and Mr. Cherecwich introduced the Commissioner of Internal Revenue, Douglas Shulman.

Summary of Commissioner Shulman's Remarks

Commissioner Shulman complimented the Board for being an incredibly valuable resource to the IRS leadership and thanked the members for their service. He began his introduction of the second keynote speaker, Senator Portman, the co-chair of the commission that resulted in the IRS restructuring act in 1998. He noted that Senator Portman has had a distinguished career both in the public and private sector, and that he was dedicated to find the best solutions to make the IRS work better.

Summary of Senator Portman's Remarks

Senator Portman said he was proud to say he was part of the effort, now over twelve years ago, to lay the groundwork for a culture change at the IRS to balance enforcement and service. He recognized a number of individuals in the audience and on the Board who had participated on the commission that he co-chaired with Senator Kerrey.

Senator Portman then looked back to the reasons that the commission was established, to address problems with customer service and systems modernization at the IRS. He said there was new focus on service, strategic planning and electronic filing. He said the Board was created to bring outside expertise to the IRS, to establish continuity as the IRS modernized, and to establish accountability for IRS leadership. He praised the IRS for improving customer service, increasing e-filing to nearly 70 percent, implementing performance measures, and achieving a high accuracy rate on its telephone service.

However, the Senator also listed several primary challenges facing the IRS over the next few years. The tax gap needs to be addressed at a time of huge budget shortfalls. He also said that although the IRS is making progress in modernizing its information technology, the deliverable in January 2012 needs to be accomplished. Addressing budget issues over the next few years will also be a challenge for the IRS; the agency must do more with less to make the tax system as productive and efficient as possible. He suggested that true tax reform that simplifies the way in which taxpayers interact with their government would help the IRS meet these challenges.

Senator Portman said the Oversight Board can do more to help Congress understand where the IRS has succeeded and where it has fallen short. He issued a challenge to the Board to develop less than a dozen measures of customer service and compliance, establish those as benchmarks, then monitor how well the IRS is doing its job. He said the challenge for Congress is to simplify the tax law and simplify the burdens that taxpayers face in trying to comply.

Following Senator Portman's comments, Chairman Cherecwich introduced the Moderator of Panel 2, Pamela Olson. Ms. Olson is a partner with Skadden Arps Tax Group where she represents clients in a broad range of tax matters. She served as Assistant Secretary for Tax Policy at the Department of the Treasury where she provided the Secretary with policy analysis and recommendations for domestic and international issues of federal taxation.

Panel 2: Business Processes and Technology Assets in Future Tax Administration

Moderator: Pamela Olson, Esq., Skadden Arps Tax Group
Panelists:

- *Mark Matthews, Esq*., Morgan Lewis, Tax & Litigation Practice Group
- *Terry Milholland*, IRS Chief Technology Officer
- *Eric Toder*, Fellow, Urban Institute
- *Dan Maurer*, Senior Vice President, Consumer Group, Intuit

Ms. Olson said she was pleased to participate in the Board's public meeting, and introduced the four panelists on Panel 2. She asked Mr. Milholland to begin with an assessment of IRS efforts to modernize its technology systems.

Milholland said that an effective and efficient future tax administration system is created by building an effective and efficient information technology organization. He said the IRS information technology organization is moving toward being a world-class organization, with a focus not only on technology, but also on people and processes. He said the IRS is close to having a modern, state-of-the-art relational database that would allow future applications to be constructed around data rather than functionality. He compared the modernized system to a database that could be found in any Wall Street financial institution.

Milholland said the IRS launched an effort to align its IT processes with industry standards, and said the agency had achieved Level 2 Capability Maturity Model Integration (CMMI) status. He indicated the IRS has a goal to be world-class and get to Level 3 status in the next 24 months. With respect to the people component, he said the IRS is working to establish formal program management disciplines within the IT division. Milholland said an ultimate goal is for the IRS to become an internet company and to build technology, processes, investments and personnel to deliver services over the internet. In this context, the IRS could deliver future tax services through very modern, state-of-the-art technology web portal. Integrated with this would be electronic authentication and encrypted e-mail to allow for protected external communication between the IRS and taxpayers.

Dan Maurer, Senior Vice-President and General Manager for Intuit's Consumer Group, said that over 90 percent of people either do their taxes using software or practitioners, who also use software. He described the software industry as an engine investing billions of dollars in innovation and invention over the past 30 years to better assist taxpayers.

Maurer described five interrelated trends on the tax administration horizon. One is the impact of cloud computing; consumers are increasingly conducting their lives online. The implication is that consumers expect to be able to conduct business at all hours every day. The second trend is an increasing volume of information in the cloud. Addressing the amount of data and data inter-connectivity will be a challenge going forward. A third trend is the increasing demand for highly customized personalized services. The customer expectation will be for targeted service delivered quickly and efficiently. A fourth trend is continuous development and rapid adoption of new platforms, such as tablet computers and smartphones. Services will have to be adapted to the devices of tomorrow. A fifth trend is the increasing reliance on social networks rather than traditional institutions. Consumers use forums, communities, and other relationships to make social, economic and political decisions.

Maurer says that in light of these five trends, it is wrong to focus on technology only, without thinking also about the processes and people that are all part of adapting to an interconnected world. He cited the IRS' implementation of CADE and MeF as examples of beginning to adapt to this changing world. He also commended the IRS' new refund tool for cell phones as a step in the right direction. To achieve success in this new, evolving world, Mauer recommends several actions. First, have good standards for security, privacy, quality, and availability to build trust with taxpayers. Second, inject problem-solving innovation back into tax administration by partnering with external stakeholders. He also mentioned developing and implementing a joint IRS industry-connected services strategy to reduce taxpayer burden, and finally, to work towards providing service quickly and efficiently to taxpayers.

Dr. Toder addressed two issues, measuring non-compliance and measuring taxpayer burden. The IRS estimated the size of the tax gap based on 2001 data, and is working toward a more updated, revised estimate. Dr. Toder said one of the hardest parts of the tax gap to estimate is how much should be paid by those who should be filing returns but do not. He said there are some creative new methods being developed to deal with non-filing that will be good applications of better data matching technologies. He also said there are some problems with estimating the true tax gap, and that more conceptual work needs to be done. He compared estimates of non-filers to estimates of how much oil there is in the world; a more accurate estimate would be how much is extractable at what economic cost. So the tax gap estimate may not be telling the IRS where to invest its marginal resources to get the most return. Dr. Toder continued by saying that more information reporting will present a challenge to the IRS as to whether it will be able to effectively utilize that information to make an impact on the tax gap.

Dr. Toder turned to a discussion of burden. He said that based on recent surveys, the overall burdens may have gone down a bit, and he suggested two reasons for that: the shift to using automated methods, particularly software, in completing returns, and the fact that software keeps getting better and more user-friendly. He emphasized that burden should be going down, and would be if the tax system were simpler.

Mark Matthews continued the discussion about burden by talking about the data collected by government and the ways it is used. He said that the private sector perspective regarding data collection is that there needs to be a rational basis for its collection and use. It is costly to private industry to gather and report information to the IRS; the IRS in turn must be responsible for using that data effectively. He cited the FATCA regulations for increasing compliance burden and estimated that the compliance burden to some countries will exceed the tax savings to the United States; deductions by U.S. companies for the cost of complying may exceed the value of additional taxes paid. He suggested that requests for additional information reporting be subject to cost benefit analysis before it is implemented.

The panelists concluded their remarks, and Ms. Olson asked for questions from the Board or the audience. Chairman Cherecwich asked how some of the innovation that occurs in the private sector can be injected into government, specifically productivity gains in working more efficiently with less manpower. Mr. Milholland said it is important to have technology foundations in place to take advantage of other innovation; he said the IRS is experimenting with technology processes and personnel flexibilities in addition to modernizing its information technology systems. Mr. Maurer added that it also is important to have the right attitude and set expectations higher.

Ms. Wince-Smith said that treating the IRS and the tax system as one of the critical infrastructures of the country can make the national case for providing the resources and capability to have the most advanced systems possible. She also asked about cyber-security and how that impacts the amount of innovation that can be accomplished with the tax system. Mr. Milholland replied that information security and disaster recovery processes prompt the IRS to be cautious at it moves into new and untested technology areas.

In closing, Mr. Matthews suggested that the Board serve as a marshalling entity for bringing together a constituency of stakeholders that would support the resources needed to achieve good tax administration. Mr. Wagner agreed, saying that even with improved technology, processes, and workforce, the IRS has continued to be stretched with implementing new programs, such as the First Time Homebuyer Credit.

At the conclusion of the meeting, Chairman Cherecwich thanked the panelists for their participation and the meeting was adjourned.