

IRS Oversight Board

**STATEMENT OF
IRS OVERSIGHT BOARD
CHAIRMAN PAUL CHERECWICH, JR.
TO THE
SENATE COMMITTEE ON APPROPRIATIONS
SUBCOMMITTEE ON FINANCIAL SERVICES AND GENERAL GOVERNMENT
JUNE 9, 2009**

The Internal Revenue Service (IRS) Oversight Board thanks Chairman Durbin, Ranking Member Collins, and members of the Subcommittee for the opportunity to present the Oversight Board's views on the Administration's FY2010 IRS budget request.

This statement presents the Board's recommendations for the IRS' FY2010 budget and why the Board believes this level of funding is needed to meet the needs of the country and of taxpayers. Created as part of the IRS Restructuring and Reform Act of 1998 (RRA 98), the Oversight Board's responsibilities include overseeing the IRS in its administration, management, conduct, direction and supervision of the execution and application of the internal revenue laws. The Board is also responsible for ensuring that the IRS' organization and operations allow the agency to carry out its mission. To this end, the Board was given specific responsibilities for reviewing and approving annual budgets and strategic plans.

The Board has a responsibility to ensure that the IRS' budget and the related performance expectations contained in the performance budget support the recently published *IRS Strategic Plan 2009-2013*. In addition to this statement, the Board develops a formal report in which it explains in detail why it has recommended this budget for the IRS. Because of the late budget cycle caused by the change in Administrations, this report is still under development. The Board requests that this report be entered into the meeting record when it is sent to the Subcommittee later this month.

FY2010 IRS Budget Recommendations

The IRS Oversight Board recommends an FY2010 IRS budget of \$12.489 billion, an increase of \$966 million over the enacted FY2009 amount of \$11.523 billion. This recommendation is \$363 million above the President's request of \$12.126 billion.

Tables 1 and 2 at the end of this statement show more information on the Board's budget recommendations. Table 1 shows the program initiatives or increases the Board is recommending, and Table 2 shows the Board's recommended budget by account.

As the Board stated in its *2008 Annual Report to Congress*, our tax administration system has two serious weaknesses, the \$290 billion tax gap and the archaic nature of IRS information systems. As a result, the Board recommends that strengthening the system be a national priority.

Addressing those weaknesses is critical and urgent. The Board is fully supportive of the Administration's boost in enforcement funding. However, the Board recommends greater funding in the areas of Business Systems Modernization (BSM) and Operations Support than the President's budget requests. While the Oversight Board and the Administration's budgets agree in many ways, the Board feels that these key additional investments are needed sooner – not later – to strengthen our tax administration system.

The effort required to correct the two weaknesses identified above is not to be taken lightly. Although the tax gap can never realistically be eliminated, it is equally as foolish to suggest that nothing can be done to reduce it. As the Board has opined on numerous occasions, there is not a single solution to reducing the tax gap. Rather, a comprehensive, multi-faceted, multi-year, approach is needed that provides for excellent taxpayer service combined with vigorous enforcement, along with a long-term investment in IRS information technology and infrastructure. It is generally recognized that the IRS “cannot audit its way out of the tax gap.” Balance between immediate expansion of personnel combined with long term investments in information technology and infrastructure is needed.

The second weakness, modernizing the IRS' archaic information technology systems, is equally daunting—yet it must be done. As noted in the Board's *2008 Annual Report to Congress*, the IRS' systems modernization program has been on the Government Accountability Office's (GAO's) high risk list since 1995. The GAO placed this program on its high risk list because it believed that the IRS relied on obsolete automated systems for key operational and financial management functions. The Board believes that it is unacceptable for this program to remain on the high risk list for so long is unacceptable.

The Board believes strongly that the IRS' BSM program must be in a position to move forward in FY2010 and FY2011 so that program milestones scheduled for 2011 can be achieved. Because the President's budget provides little additional funding for the Customer Account Data Engine in FY2010, it puts the FY2011 milestones at great risk. In addition, the Board believes additional funding is needed to refresh and update the IRS' aging infrastructure. In total, of the \$363 million difference in the two budgets, about \$332 million is for investments in critical information technology and infrastructure.

The Board would also increase funding for several key initiatives to improve taxpayer service. These initiatives are all designed to help the IRS plan and implement better taxpayer service in the future.

Board Fully Supports Increased Enforcement Funding

The Board's recommendation for the enforcement account, which at \$5.5 billion is close to half of the IRS total budget, is identical to the President's budgets. Both the President's and Oversight Board's budgets add \$332 million for additional enforcement. This increase constitutes a 7.6 percent boost in enforcement funding, and includes additional funding to

strengthen criminal investigations programs, increase examinations and collections, and support a variety of regulatory matters.

This increase in enforcement resources pays for itself; in some cases many times over – a consideration that should not be ignored in the budget process. In addition, it helps to reduce the tax gap, which deprives the nation, and hence its citizens, of \$290 billion it is legally owed. The tax gap is an affront to honest taxpayers and efforts must be made to reduce it.

The President's request for enforcement funding includes a multi-year investment of \$128 million, starting in FY2010, to deal more effectively with increasing international tax activities of individual and business taxpayers. The Board is pleased with this, as the effects of globalization on tax administration are significant and must be addressed.

The Board also strongly supports additional funding to improve compliance among “high-risk” taxpayer segments. Estimates shows that much of the tax gap is due to underreporting of income by businesses, mostly run by individuals. It is imperative that the IRS not only ensure that *all* individuals understand their tax obligations, but that they report their income and pay their taxes.

Taxpayer Service Increase Recommended

For the taxpayer service account, the Oversight Board's and President's budgets are within 0.2 percent of one another. The President's budget request for taxpayer service benefits from congressional action taken during consideration of the FY2009 budget. By adding additional funding to the IRS taxpayer service budget in FY2009, Congress raised the base amount for taxpayer service in FY2010, giving the IRS additional resources to serve taxpayers in an increasingly more complex economic environment.

The need for taxpayer service is especially acute during periods of economic hardship, as taxpayers may find themselves facing challenging financial situations. In addition, taxpayers need additional help to understand new tax provisions and programs designed to help them during difficult times. Every change in the tax code causes the tax administration system to become more complex, with more taxpayers in need of help to understand and meet their obligations. It is especially important during this recession that the IRS be able to follow through on its strategic goal to “make voluntary compliance easier.”

Despite a higher funding base for taxpayer service, there are several areas where the Board recommends additional funding. In 2005, Congress asked the IRS, National Taxpayer Advocate, and the IRS Oversight Board to develop a five-year plan to improve taxpayer service. The result was the Taxpayer Assistance Blueprint (TAB), which was completed in April 2007. In the Board's opinion, the IRS needs additional resources to more fully carry out the TAB by expanding its on-line capabilities. Additional funding is also needed to optimize the use of Taxpayer Assistance Centers, also known as walk-in sites, which traditionally serve lower income taxpayers who depend more on walk-in services. Overall, the Board recommends an additional \$31.6 million be appropriated for taxpayer service, all of which will be focused on improving taxpayer service in the future.

Strategic Funding Needed for Business Systems Modernization

The IRS' archaic computer systems are a serious challenge facing the IRS. The Board is dismayed by the long-term under-funding of the BSM program, forcing the IRS to stretch out its efforts at a painfully slow pace, to the detriment of taxpayers.

The Board is pleased that the IRS has revised its BSM approach to put more focus on completing the program, and considers it a critical foundation of service and enforcement in the future.

However, the Board questions whether the President's budget will allow for substantive progress in the coming years. The Board has opined in past years that the BSM account is fundamentally under-funded, and despite the additional \$7.3 million added by Congress in FY2009 and the President's FY2010 requested increase of \$22.6 million, the FY2010 request for BSM continues to be far too low. Progress will come slowly should that trend continue. The Customer Account Data Engine project, in particular, has funding needs that go far beyond what was requested in FY2010, and those needs will only grow in FY2011.

The Board's recommended BSM budget of \$400 million is 58 percent higher than the President's BSM budget of \$253.7 million. At \$253.7 million, the President's BSM budget consumes 2.1 percent of the IRS total budget of \$12.126 billion. This compares to the Board's recommendation of a \$400 million BSM budget, which consumes 3.2 percent of its total \$12.489 billion budget. Although the difference is quite small when viewed as a portion of the total budget, the vision presented by these two BSM budgets is quite different. The Board believes that funding decisions for the IRS must look beyond consideration of short term benefits and immediate return on investment. Serious consideration must also be given to the long term benefits to taxpayers and the tax administration system that will result from a modernized information technology system. These investments will result in fundamental changes to tax administration that will benefit both taxpayers and tax administrators alike.

The Board recommends that a total of \$400 million be appropriated for the BSM program so that the pace of progress is increased, allowing the IRS to achieve key milestones in FY2011, such as the deployment of a daily Individual Master File capability and a Customer Account Data Engine relational database.

More Funding for Operations Support

Another important aspect of the IRS' performance is the state of its legacy infrastructure: the technology and tools used by IRS employees to do their work. IRS laptops, software, the telecommunications systems, and the buildings themselves are aging and must be updated and maintained. In addition, the IRS must protect its hardware and data infrastructure from threat, whether it comes from bad weather or cyber-attack.

The Administration's FY2010 budget calls for \$108.1 million in program increases to address information technology security and material weaknesses and to strengthen the Electronic Fraud Detection System. The Board supports this funding, as both can help ensure the integrity of the tax system and maintain taxpayer confidence that its returns remain private and safe from security risks.

However, more needs to be done. The Board recommends a total of \$292 million in infrastructure program initiatives, compared to the \$108 million requested by the President's IRS budget. The Board recommends an additional \$164 million in technology initiatives and a \$20 million initiative related to workforce development. This funding is needed to refresh and maintain the IRS' infrastructure, strengthen its ability to protect the personal information of taxpayers, increase the productivity of its workforce by leveraging information technology, and upgrade its financial services accounting system that uses a software application product that is so old the vendor will no longer support the program in 2013.

In addition, workforce development cannot be ignored, especially during a period when the IRS is losing experienced employees to retirement and is hiring a significant number of new employees. Frontline supervision plays a key role in employee satisfaction, quality, and productivity, and the IRS lacks funding to properly train frontline managers in a timely fashion. Approximately \$15 million of the workforce initiative is for frontline management training, with the remaining \$5 million for succession planning and executive development.

Long-Term Investment Key to IRS Strength

Although the magnitude of the Board's budget recommendations for the IRS are not vastly different from the President's budget request in amount, they do focus more on the IRS' strategic goals and call for investments that are needed today for a stronger tax administration system in the future. The Oversight Board believes that its approach represents a meaningful long-term investment to benefit our nation in the decades to come.

**Table 1. IRS Oversight Board Recommended FY2010 IRS Budget by Program Initiative
(dollars in thousands)**

FY 2009 Enacted	\$11,522,598
Changes to Base:	
Maintaining Current Levels	\$256,329
Efficiencies/Savings	(\$118,125)
Reinvestment	\$2,331
Subtotal Changes to Base	\$140,535
Total FY 2010 Base - Current Services	\$11,663,133
Program Increases	
<i>Taxpayer Service Initiatives</i>	
TAB Technology Enhancements	\$6,000
Optimize TAC Footprint	\$17,880
Research and Analysis to Improve Taxpayer Service	\$7,750
Subtotal, Taxpayer Service Initiatives	\$31,630
Program Increases:	
<i>Enforcement Initiatives</i>	
Reduce the Tax Gap Attributable to International Activities	128,064
Improve Reporting Compliance of SB/SE Taxpayers	94,215
Expand Document Matching for Business Taxpayers	26,237
Address Nonfiling/Underpayment and Collection Coverage	83,644
Subtotal, Enforcement Initiatives	\$332,160
<i>Infrastructure Initiatives</i>	
Address IT Security and Material Weakness	\$90,000
Implement Return Review Program	\$18,100
Refresh/Sustain Infrastructure	\$75,000
Training and Certifying Project Managers	\$5,000
Enhance Privacy, Information Protection and Data Security	\$9,154
Technology Investments to Enhance Operations	\$35,000
Upgrade Integrated Financial System (IFS)	\$40,700
Leadership Training and Development	\$20,000
Subtotal, Infrastructure Initiatives	\$292,954
<i>BSM Initiative</i>	
Fund BSM to Accelerate Taxpayer Benefits	\$168,933
Subtotal, BSM	\$168,933
Subtotal FY 2010 Program Initiatives	\$825,677
Total FY 2010 Request	\$12,488,810
FY2010 President's Request for IRS	\$12,126,000
Increase Over President's Request	\$362,810

**Table 2. Summary of Oversight Board Recommended IRS FY2010 Budget by Account
(dollars in thousands)**

	Taxpayer Service	Enforcement	Ops Support	BSM	HITCA	Total
FY 2009 Enacted Budget	\$2,293,000	\$5,117,267	\$3,867,011	\$229,914	\$15,406	\$11,522,598
Changes to Base:		\$0				\$0
Maintaining Current Levels Adjustment	\$60,195	\$133,815	\$61,060	\$1,153	\$106	\$256,329
Efficiencies/Savings	(\$90,918)	\$0	(\$27,207)	\$0	\$0	(\$118,125)
Reinvestment	\$2,025	\$0	\$306	\$0	\$0	\$2,331
Subtotal Changes to Base	(\$28,698)	\$133,815	\$34,159	\$1,153	\$106	\$140,535
Total FY 2010 Base - Current Services	\$2,264,302	\$5,251,082	\$3,901,170	\$231,067	\$15,512	\$11,663,133
Program Increases						
<i>Taxpayer Service Initiatives</i>						
TAB Technology Enhancements	\$592		\$5,408			\$6,000
Optimize TAC Footprint	\$4,238		\$13,642			\$17,880
Research and Analysis to Improve Service			\$7,750			\$7,750
Subtotal, Taxpayer Service Initiatives	\$4,830		\$26,800			\$31,630
<i>Enforcement Initiatives</i>						
Reduce the Tax Gap Attributable to International Activities	\$3,124	\$104,113	\$20,827			\$128,064
Improve Reporting Compliance of SB/SE Taxpayers	\$267	\$75,114	\$18,834			\$94,215
Expand Document Matching for Business Taxpayers	\$1,425	\$17,955	\$6,857			\$26,237
Address Nonfiling/Underpayment and Collection Coverage	\$712	\$55,736	\$27,196			\$83,644
Subtotal, Enforcement Initiatives	\$5,528	\$252,918	\$73,714	\$0	\$0	\$332,160
<i>Infrastructure Initiatives</i>						
Address IT Security and Material Weakness			\$90,000			\$90,000
Implement Return Review Program (RRP)			\$18,100			\$18,100
Refresh/Sustain Infrastructure			\$75,000			\$75,000
Training and Certifying Project Managers			\$5,000			\$5,000
Enhance Privacy, Information Protection and Data Security			\$9,154			\$9,154
Technology Investments to Enhance Operations			\$35,000			\$35,000
Upgrade Integrated Financial System (IFS)			\$40,700			\$40,700
Leadership Training and Development			\$20,000			\$20,000
Subtotal, Infrastructure Initiatives	\$0	\$0	\$292,954	\$0	\$0	\$292,954
<i>Business Systems Modernization Initiative</i>						
Fund BSM to Accelerate Taxpayer Benefits				\$119,133		\$119,133
Subtotal, Business Systems Modernization	\$0	\$0	\$0	\$168,933	\$0	\$168,933
Subtotal FY 2010 Program Changes	\$10,358	\$252,918	\$393,468	\$168,933	\$0	\$825,677
Total FY 2010 Board Recommendation	\$2,274,660	\$5,504,000	\$4,294,638	\$400,000	\$15,512	\$12,488,810
FY2009 Enacted	\$2,293,000	\$5,117,267	\$3,867,011	\$229,914	\$15,406	\$11,522,598
FY2010 President's Request for IRS	\$2,269,830	\$5,504,000	\$4,082,984	\$253,674	\$15,512	\$12,126,000
Increase Over President's Request	\$4,830	\$0	\$211,654	\$146,326	\$0	\$362,810
Percent Increase Over President's Request	0.2%	0.0%	5.2%	57.7%	0.0%	3.0%