

## Internal Revenue Service

### Mission:

To provide America's taxpayers top-quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.

### Program Summary by Appropriations Account

(Dollars in Thousands)

Appropriations	FY 2005	FY 2006*	FY 2007**		
	Enacted	Enacted	President's Budget	Change	% Change
Processing, Assistance and Management	4,056,857	4,095,212	4,045,122	(50,090)	-1.2%
Pre-filing Taxpayer Assistance & Education	539,374	517,707	329,557	(188,150)	-36.3%
Filing & Account Services	1,710,368	1,679,688	1,618,784	(60,904)	-3.6%
Shared Services Support	1,210,874	1,285,181	1,504,247	219,066	17.1%
General Management & Administration	596,241	612,636	592,534	(20,102)	-3.3%
Tax Law Enforcement	4,363,539	4,678,498	4,762,327	83,829	1.8%
Compliance Services	4,104,471	4,415,064	4,496,735	81,672	1.8%
Research & Statistics of Income	94,474	95,954	97,542	1,588	1.7%
Earned Income Tax Credit	164,594	167,481	168,050	568	0.3%
Information Systems	1,577,768	1,582,977	1,602,232	19,255	1.2%
Information Systems Improvement Programs	49,002	48,960	49,302	342	0.7%
Information Services	1,528,766	1,534,017	1,552,930	18,913	1.2%
Business Systems Modernization	203,360	197,010	167,310	(29,700)	-15.1%
Health Insurance Tax Credit Administration	34,562	20,008	14,846	(5,162)	-25.8%
<b>Subtotal, Internal Revenue Service</b>	<b>\$10,236,087</b>	<b>\$10,573,706</b>	<b>\$10,591,837</b>	<b>\$18,131</b>	<b>0.2%</b>
Mandatory Appropriation - New User Fees	0	0	135,000	135,000	
<b>Total Program Operating Level</b>	<b>\$10,236,087</b>	<b>\$10,573,706</b>	<b>\$10,726,837</b>	<b>\$153,131</b>	<b>1.4%</b>
Offsetting Collections - Reimbursables	156,892	158,820	182,643	23,823	15.0%
Mandatory Appropriation - Existing User Fees	119,000	100,000	99,627	(373)	-0.4%
<b>Total Program Operating Level (All New Resources)</b>	<b>\$10,511,979</b>	<b>\$10,832,526</b>	<b>\$11,009,107</b>	<b>\$176,581</b>	<b>1.6%</b>

Numbers may not add due to rounding.

\*The FY 2006 enacted level includes a 1% across the board rescission and excludes rescission of unobligated balances (\$20 million from PAM and \$9 million from HITCA).

\*\* In FY 2007, the IRS request is supplemented by \$135 million in new user fees for a total operating level of \$10,726,837 thousand.

### Overview

The Internal Revenue Service (IRS) administers America's tax laws and collects the revenue that funds most government operations and public services. The IRS and its employees represent the face of government to more U.S. citizens than any other agency. The IRS' taxpayer service programs provide assistance to millions of taxpayers to help

them understand and meet their tax obligations. The IRS' enforcement programs are aimed at deterring taxpayers inclined to evade their responsibilities while vigorously pursuing those who violate tax laws.

The IRS budget request for FY 2007 supports the IRS' five-year strategic plan. This plan underscores the IRS' commitment to provide quality service to

taxpayers while enforcing America's tax laws in a balanced manner. The IRS strategic plan goals guiding the future direction of the Service are:

- *Improve Taxpayer Service* – Improve service to taxpayers to help them understand their tax obligations,
- *Enhance Enforcement of the Tax Laws* – Ensure taxpayers meet their tax obligations so when Americans pay their taxes, they can be confident their neighbors and competitors are doing the same, and
- *Modernize the IRS Through Its People, Processes, and Technology* – Strategically manage resources, associated business processes, and technology systems to meet service and enforcement goals.

The IRS supports the Administration's goal to reduce the federal deficit by increasing tax receipts collected through taxpayer service and enforcement compliance. The FY 2007 Budget provides funding to continue the IRS' commitment to service, and sustains its efforts to enhance enforcement of the tax laws. The great majority of Americans pay their fair share of taxes, but there is still a significant tax gap – the difference between what taxpayers are supposed to pay and what they actually pay – due to non-filing, underreporting and nonpayment. Reducing the net tax gap, currently estimated at \$257 to \$298 billion for 2001, is a top priority. The IRS' approach to reducing the tax gap and increasing tax receipts relies on implementation of selected tax-related legislative changes, improved administrative procedures, and implementing a sound technological infrastructure designed to support taxpayer service and enforcement. The IRS also supports the Administration's deficit reduction goal by continuing to identify productivity improvements and efficiencies that will reduce the cost of collecting revenues.

The Internal Revenue Service FY 2007 budget request is \$10,591,837,000 in direct appropriations, supplemented by \$135,000,000 in new user fee revenue, \$99,627,000 in existing user fee revenue,

and \$182,643,000 in reimbursable resources for a total program operating level of \$11,009,107,000.

## Performance Highlights

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The following is a summary, outlined by the IRS' strategic goals, of significant program performance improvements:

### Improve Taxpayer Service

Assisting the public to understand their tax reporting and payment obligations is the cornerstone of taxpayer compliance and is vital for maintaining public confidence in the tax system. The IRS continues to meet this challenge by improving the quality and accuracy of responses from its call centers and expanding taxpayer service through increased electronic self-service transactions. The following information highlights the IRS' taxpayer service achievements in FY 2005:

- Survey results from the American Customer Satisfaction Index and the IRS Oversight Board Taxpayer Attitude Survey reveal that most taxpayers are satisfied with the levels of service they receive over the telephone. In FY 2005, the IRS' customer assistance call centers answered 59.1 million calls. The IRS exceeded its FY 2005 target of 82 percent toll-free telephone level-of-service and improved its toll-free tax law accuracy rate to 89 percent, an increase from 80 percent in FY 2004.
- The newly redesigned IRS website, [www.irs.gov](http://www.irs.gov), provides 24-hour assistance, seven days a week, with improved site navigation and an enhanced search engine, increasing search result accuracy and usability. New and improved features for [www.irs.gov](http://www.irs.gov) in 2006 include 1040 Central, Free File, Alternative Minimum Tax Assistant, Earned Income Tax Credit (EITC) Assistant, "Where's My Refund?", and electronic application and receipt of Employer Identification Number.
- The IRS provided and staffed toll-free phone assistance lines for hurricane victims. The IRS also implemented numerous tax law changes to help the victims of hurricanes Katrina and Rita, businesses located in the disaster areas, and

## IRS Performance by Appropriation

Appropriation	Performance Measure	FY 2003	FY 2004	FY 2005	Target Met?	FY 2006	FY 2007
		Actual	Actual	Actual	Target	Target	Target
PAM	Customer Service Representative Level of Service (%) (Oe)	80.0	87.3	82.6	✓	82.0	82.0
	Customer Accuracy - Tax Law Phones (%) (Ot)	82.0	80.8	89.0	✓	90.0	90.5
	Percent of Business Returns Processed Electronically (%) Oe **	n/a	17.4	17.8	✓	18.6	20.6
	Percent of Individual Returns Processed Electronically (%) (Oe) **	40.3	46.5	51.1	✓	55.0	58.8
	Customer Contacts Resolved per Staff Year (E)	n/a	8,015	7,585	✓	7,477	7,555
	Taxpayer Self-Assistance Rate (%) (E)	51.0*	46.4*	42.4*	Baseline	45.7	47.5
TLE	Collection Coverage - units (%) (Ot) (L)^	n/a	n/a	53.0	✓	52.0	52.0
	Examination Coverage - Business (Corps >\$10M) (%) (Oe) (L)	6.1	7.5	7.8	✓	7.5	8.4
	Examination Coverage-Individual (%) (Oe) ***	n/a	0.8	0.9	✓	0.9	1.0
	Automated Underreporter (AUR) Program Efficiency (E) (L)^^^	n/a	1,664	1,701	n/a	1,759	1,834

(E) = Efficiency Measure (Oe) = Outcome Measure (Ot) = Output Measure

\* FY 2003-2005 data based on a methodology for calculating performance developed in FY 2005

N/A: Not Applicable (measure not in place) for this fiscal year

\*\* Variance from PART and 80% statute goal

\*\*\* Variance from PART section (does not include AUR cases)

^ Variance from PART - Methodology change - prior performance reported as 39% under old methodology

^^ Measure shown in PART as Document Matching Cases per FTE - calculation no longer includes screen outs

individuals donating to charities to support the victims. The IRS will continue to implement recent tax law changes designed to encourage investment in areas affected by hurricane Katrina, including the Administration's Gulf Opportunity (GO) Zone proposals for bonus depreciation and additional small business expensing.

- The number of taxpayers filing electronically continues to increase. In 2005, for the first time, more than half of all individual taxpayer returns (68 million) were filed electronically with more than five million of these taxpayers filing for free through the Free File Alliance. This is a 43 percent increase in Free File Alliance filings over the previous year. Increased electronic filing benefits the taxpayer and the IRS. The American Customer Satisfaction Index shows that e-file taxpayers are significantly more satisfied with their interaction with the IRS than are paper filers. In addition,

electronic filing processes refunds more quickly and eliminates most common filing errors (math errors, number transposition, etc.).

The Service continues to leverage community partnerships to provide free tax return preparation assistance through successful programs such as Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE). In 2005, over 62,000 trained volunteers at 14,000 locations across the country prepared more than 2.1 million tax returns, an 80 percent increase since 2001 (the year prior to the implementation of the community partnership model). In addition, the VITA and TCE volunteers e-filed more than 77 percent of these returns, an increase in volume of 130 percent over 2001.

### Enhance Enforcement

The IRS made significant progress towards

achieving its enforcement-related goals in FY 2005. These improvements were achieved through efforts such as streamlining and centralizing work processes, improving workload selection techniques, increasing managerial involvement in casework, and implementing initiatives to reduce cycle time by refining case selection criteria. The IRS also expanded its compliance coverage through increased efficiency in its examination program. The Service's examination coverage technique encourages examiners to pursue significant tax issues and to use their professional judgment when asking taxpayers for supplemental documentation. As a result the IRS:

- Collected more than two trillion dollars in revenue with \$47.3 billion collected through enforcement activities, a 10 percent increase from FY 2004,
- Increased high-income audits (taxpayers earning \$100,000 or more) by 33 percent from FY 2004,
- Increased individual audits completed by 20 percent from FY 2004,
- Increased small business audits (< \$10 million) by 81 percent, and increased corporate audits (> \$10 million) by 15 percent from FY 2004,
- Generated more than \$4.7 billion in revenue in FY 2005 through two prominent settlement initiatives aimed at reducing examination and litigation expenses while deterring the use of abusive tax shelters,
- Increased collection case closures by 12 percent and dollars collected by 14 percent from FY 2004, and
- Increased convictions to 2,151 in 2005 (from 1,926 in 2002) through increased productivity.

In addition, the IRS leveraged its Counterterrorism Program both to support the war on terrorism and tax compliance. Almost half of Criminal Investigation Division's (CID) inventory of terrorism-related cases have a tax-related violation under investigation. In FY 2005, the Department of Justice obtained 78 indictments on CID counterterrorism cases and CID recommended 86 cases for prosecution.

## **Modernize the IRS through its People, Processes and Technology**

The IRS must ensure its employees have the tools and skills necessary to increase organizational effectiveness and support its mission. In addition, employees need challenging work and appropriate compensation. To achieve these objectives, the IRS recently developed a new Human Capital Strategic Plan. Once finalized, the plan will communicate the direction the IRS will take to hire, train, and retain employees while ensuring retention of organizational knowledge, leadership competency and continuity.

Within the past two years, the IRS Business Systems Modernization (BSM) program has begun to improve its performance on delivering projects and releases on time, on budget, and meeting or exceeding scope expectations. After several years of not achieving project cost, scheduling, and performance goals, the IRS is realizing benefits to taxpayers and enhanced BSM program management capabilities.

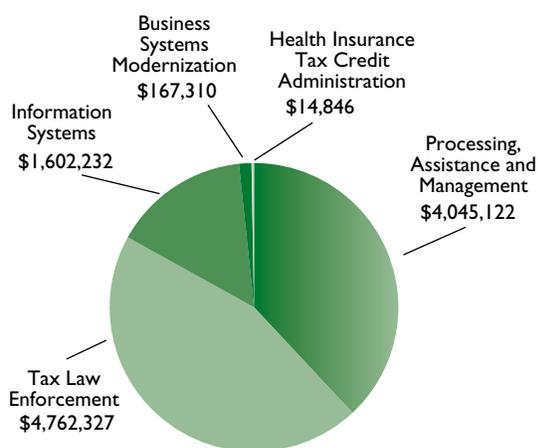
In FY 2006 and continuing in FY 2007, BSM is revising its modernization strategy to emphasize the incremental release of projects to deliver business value sooner and at a lower risk. The FY 2005 IRS modernization efforts focused on three key tax administration systems that provide additional benefits to taxpayers and IRS employees: the Customer Account Data Engine (CADE) project; Modernized e-File (MeF); and Filing and Payment Compliance (F&PC).

- CADE will ultimately replace the IRS' antiquated Master File system, which is the repository of taxpayer information. CADE allows faster refunds (processing refunds on a daily basis), improved taxpayer service, faster issue detection, more timely account settlement, and a robust foundation for integrated and flexible modernized systems. CADE posted more than 1.4 million returns and generated more than \$427 million in refunds. In FY 2006, CADE will process 4 million returns (with an anticipated 33 million by the following year) and will be the single authoritative repository for account and return data for those returns.

- MeF deployed Form 7004 (filing extension for corporations) as well as Form 990PF (information returns for private foundations). This enabled the IRS to establish regulations requiring large corporations and tax-exempt organizations to file their income tax or annual information returns electronically. MeF processed Forms 1120 and 990 at higher-than-expected volumes while still achieving performance goals – a significant reduction in burden and time for corporate and tax-exempt taxpayers.
- F&PC, Release 1.1 completed the architecture engineering analysis and development needed to separate complex cases requiring direct IRS involvement from those that private collection agencies can handle. This release will provide initial capabilities for routing collection cases to private collection agencies in FY 2006.

In 2005, for the sixth consecutive year, the IRS achieved an unqualified audit opinion from the Government Accountability Office on all financial statements. This was accomplished despite the challenge of implementing the new Integrated Financial System.

### IRS Funding by Appropriation



### Source of Funds

The Internal Revenue Service (IRS) budget request for FY 2007 is \$10,591,837,000 in direct appropriations, supplemented by \$135,000,000 in new user fee revenue, for a total operating level of \$10,726,837,000.

This represents an increase of 1.4 percent from the FY 2006 enacted level. This Budget supports the following FY 2007 priorities:

- Maintain balance between service and enforcement,
- Maintain the tax enforcement funding increase provided in FY 2006 to improve tax compliance,
- Focus on areas in need of closer scrutiny by IRS, including tax strategies involving international elements for both corporations and high-income individuals,
- Continue the examination of tax-exempt charities used to violate federal income tax laws, and
- Focus on technology issues to ensure the IRS is utilizing technological advances to optimize both taxpayer service and enforcement programs.

The IRS' funding is appropriated among five accounts. Three are operating accounts associated with the salaries and expenses of tax administration: *Processing, Assistance and Management (PAM)*, *Tax Law Enforcement (TLE)*, and *Information Systems (IS)*. The fourth account, *Business Systems Modernization (BSM)*, funds contract costs for the development, delivery, and implementation of the IRS' modernized, major systems. The fifth account, *Health Insurance Tax Credit Administration (HITCA)*, funds the costs of administering the Health Coverage Tax Credit. The IRS programs and supporting functions appropriated in the three operating accounts – PAM, TLE and IS – strategically align with either taxpayer services or tax law enforcement program. The budgets for these two strategic program areas are funded by allocating direct and overhead resources from the three operating accounts. Many of the enhancements to service and enforcement are dependent on information technology. The information technology resources funded in the IS account provide the infrastructure that is a critical component ensuring delivery of IRS programs. The following information summarizes the strategic alignment of the IRS' FY 2007 resources requested in the PAM, TLE, and IS operating accounts.

## Strategic Alignment of Taxpayer Service and Enforcement Programs

(Dollars in Thousands)

Programs	FY 2005 Enacted	FY 2006 Enacted	FY 2007 President's Budget	% Change
<b>Taxpayer Service</b>	<b>\$3,605,978</b>	<b>\$3,532,618</b>	<b>\$3,583,336</b>	<b>1.4%</b>
Direct Appropriation	\$3,605,978	\$3,532,618	\$3,448,336	-2.4%
New User Fee Revenue			\$135,000	N/A
<b>Enforcement</b>	<b>\$6,392,187</b>	<b>\$6,824,070</b>	<b>\$6,961,345</b>	<b>2.0%</b>
<b>Total Taxpayer Service &amp; Enforcement</b>	<b>\$9,998,165</b>	<b>\$10,356,688</b>	<b>\$10,544,681</b>	<b>1.8%</b>

As the table above illustrates, the Administration proposes to fund taxpayer service and enforcement programs as follows:

- *Taxpayer Service* at \$3,448 million in direct appropriations and \$135 million from new user fee revenues, for a combined operating level of \$3,583 million, a 1.4 percent increase from the FY 2006 enacted level. The IRS will maintain its commitment to provide high-quality taxpayer services through improvements to information technology and other targeted efficiencies. The growth in electronic filings also improves efficiency and accuracy, ultimately reducing tax administration costs. The IRS will continue to identify other opportunities to provide quality taxpayer service at a lower cost, such as providing and marketing expanded services to increase use of the Internet.
- *Enforcement* at \$6,961 million, a 2 percent increase from the FY 2006 enacted level. The IRS continues to emphasize compliance with tax laws and the importance of enhanced enforcement to increase collections through productivity improvements, such as the implementation of legislative changes, streamlining operating procedures, and deploying improved technology. The FY 2006 Budget provided increased budget authority as part of a government-wide program integrity “cap adjustment” for IRS enforcement programs in FY 2006. This was proposed as part of the *Budget Enforcement Act (BEA)* reauthorization (not yet enacted) but provided in the 2006 Budget Resolution. The IRS FY 2007 Budget request reflects a two percent increase in enforcement funding. The Administration is again proposing

to fund this increase (+\$137.275 million) as a BEA program integrity cap adjustment (see Chapter 15, Budget Reform Proposals of the Analytical Perspectives volume of the FY 2007 President’s Budget).

### FY 2007 Budget Adjustments

#### FY 2006 Enacted

The FY 2006 enacted level for IRS is \$10,573,706,000 in direct appropriations, supporting 95,386 FTE.

#### Current Services

*Adjustments Necessary to Maintain Current Levels +\$272,231,000/0 FTE* Funds are requested for the proposed January 2007 pay raise (\$149,819,000), the FY 2007 cost of the January 2006 pay increase (\$61,994,000), and non-pay inflation for items such as contracts, travel, supplies, equipment, and rent adjustments (\$60,418,000).

#### Program Reductions

*Business Systems Modernization (BSM) Program Reduction -\$29,700,000/0 FTE* This reduced level of funding continues support for the development and deployment of the Customer Account Data Engine, the Filing and Payment Compliance project, and the Modernized e-Filing project.

#### Base Reinvestments

*Increase Returns Processing Efficiencies +12,237,000/+11 FTE* This initiative requests funding to continue consolidating the processing of Individual Master File returns into fewer submission processing sites. These resources fund the ramp down of the Philadelphia submission processing site in

## IRS FY 2007 Budget Highlights

(Dollars in Thousands)

	Processing, Assistance and Management	Tax Law Enforcement	Information Systems	Business Systems Modernization	Health Insurance Tax Credit Administration	Total
<b>FY 2005 Enacted</b>	<b>\$4,056,857</b>	<b>\$4,363,539</b>	<b>\$1,577,768</b>	<b>\$203,360</b>	<b>\$34,562</b>	<b>\$10,236,087</b>
FY 2006 Appropriation (P.L. 109-115)	4,136,578	4,725,756	1,598,967	199,000	20,210	10,680,511
Rescission (P.L. 109-148)	(41,366)	(47,258)	(15,990)	(1,990)	(202)	(106,805)
<b>FY 2006 Enacted</b>	<b>\$4,095,212</b>	<b>\$4,678,498</b>	<b>\$1,582,977</b>	<b>\$197,010</b>	<b>\$20,008</b>	<b>\$10,573,706</b>
<b>Current Services</b>						
<b>Adjustments to Maintain Current Levels</b>	\$104,406	\$127,346	\$40,141	\$0	\$338	\$272,231
Pay Annualization	21,148	34,879	5,954		13	61,994
Proposed Pay Raise	51,090	84,284	14,388		57	149,819
Non-Pay Inflation Adjustment	32,168	8,183	19,799		268	60,418
<b>Program Reduction</b>	\$0	\$0	\$0	(\$29,700)	\$0	(\$29,700)
Business Systems Modernization Program Reduction				(29,700)		(29,700)
<b>Base Reinvestment</b>	\$7,696	\$4	\$4,537	\$0	\$0	\$12,237
Increase Returns Processing Efficiencies	7,696	4	4,537			12,237
<b>Program Cost Savings</b>	(\$47,792)	(\$40,690)	(\$27,613)	\$0	(\$5,500)	(\$121,596)
E-File Savings	(6,640)	(56)	(63)			(6,760)
Improvement Project Savings	(7,000)	(674)	(541)			(8,215)
Competitive Sourcing Savings	(10,206)	(4,246)	(2,548)			(17,000)
Program Efficiencies	(23,946)	(35,714)	(24,461)			(84,121)
HITCA Program Efficiency					(5,500)	(5,500)
<b>Transfers Out</b>	(\$272)	(\$204)	(\$465)	\$0	\$0	(\$941)
Transfer to TIGTA	(272)	(204)	(465)	0	0	(941)
<b>Current Services Level</b>	<b>\$4,159,250</b>	<b>\$4,764,954</b>	<b>\$1,599,577</b>	<b>\$167,310</b>	<b>\$14,846</b>	<b>\$10,705,937</b>
<b>Program Adjustments</b>						
<b>Program Increases</b>	\$643	\$0	\$20,257	\$0	\$0	\$20,900
Consolidate Philadelphia Campus	643		20,257			20,900
<b>FY 2007 Operating Level</b>	<b>\$4,159,893</b>	<b>\$4,764,954</b>	<b>\$1,619,834</b>	<b>\$167,310</b>	<b>\$14,846</b>	<b>\$10,726,837</b>
<b>Offsetting Collections</b>						
New User Fees	(\$114,771)	(\$2,627)	(\$17,602)	\$0	\$0	(\$135,000)
<b>FY 2007 President's Budget Request</b>	<b>\$4,045,122</b>	<b>\$4,762,327</b>	<b>\$1,602,232</b>	<b>\$167,310</b>	<b>\$14,846</b>	<b>\$10,591,837</b>

FY 2007 and prepare for the ramp down of the Andover submission processing site in FY 2009. The initial ramp down of the Andover site requires funding to secure swing space, ship equipment, and begin preliminary infrastructure support. The estimated costs to ramp down the Philadelphia submission processing site include severance costs and information technology support.

### Program Cost Savings

**E-File Savings -\$6,760,000/-174 FTE** This savings results from increased electronic filing (e-file) and a reduction in Individual Master File paper returns. Estimated e-file savings are based on the projected reduction in the number of paper returns processed each year, offset by the cost of processing e-filed returns. In FY 2007, the IRS expects to process 3.6

million fewer paper filed returns than in FY 2006. The savings from reduced paper returns is 230 FTE and the corresponding cost for supporting increased e-filed returns is 56 FTE, resulting in a net savings of 174 FTE and \$6.8 million.

***Improvement Project Savings -\$8,215,000 / -135 FTE***

This savings result from operational improvements generated by the Contact Recording, Queuing Management (Q-Matic), Correspondence Imaging Systems, and End-to-End Publishing improvement projects already in progress. Contact Recording will enable managers at toll-free sites and Taxpayer Assistance Centers (TACs) to improve the quality of taxpayer assistance on incoming and outgoing telephone calls/interviews. Q-Matic is an on-line system available at TACs to facilitate workload and resource distribution for improved workflow and timeliness of service. The Correspondence Imaging System will allow customer service representatives to work from a stored image to streamline case resolution. End-to-End Publishing will provide technology solutions to streamline business processes associated with publishing and distribution.

***Competitive Sourcing Savings -\$17,000,000/ 0 FTE***

The IRS expects to achieve efficiencies and savings through competitive sourcing resulting from six different projects in various phases of implementation. These projects reduce operational costs through the establishment of a most efficient organization or through private vendor efficiencies. The National Distribution Center (centralization of nationwide tax forms distribution operation) and Integrated Document Solutions Enterprise (formerly Campus Operations, which provides information systems computer operations at the 10 IRS Campus Facilities) reach full implementation in FY 2007 and achieve the last increment of savings.

***Program Efficiencies -\$84,121,000/-2,096 FTE*** The IRS continues to improve the efficiency of taxpayer service and enforcement programs. This initiative eliminates duplicative overhead in the operations support organizations, without having an adverse

impact on taxpayer service and enforcement operations. Taxpayer service operations will be improved through a variety of efforts, including the judicious distribution of workload and the automation of certain taxpayer assistance functions, such as the centralized monitoring of case inventories. The IRS will enhance productivity and efficiency of its enforcement programs by consolidating, reducing and redirecting some of the resources allocated to overhead and internal support functions to front-line compliance activities. In addition, the IRS will identify processes that can be reengineered and centralized, as well as improve workload selection techniques in examination and collection.

***Reduction to Health Insurance Tax Credit Administration (HITCA) Program -\$5,500,000/0 FTE***

This funding adjustment reflects the program's effort to align fiscal year costs with contract year expenditures. In addition, HITCA is using a comprehensive plan outlining cost reduction initiatives to improve customer service and reduce information technology support to achieve these savings.

**Transfers Out**

***Transfer to Treasury Inspector General for Tax Administration (TIGTA) -\$941,000/0 FTE***

This base transfer is comprised of (1) TIGTA's portion of the Working Capital Fund, which is currently paid directly by the IRS (-\$926,000) and (2) printing funds currently paid directly by the IRS to the Government Printing Office for TIGTA activities (-\$15,000).

**Program Increases**

***Consolidation of Philadelphia Campus +\$20,900,000 /0 FTE***

This initiative requests funding for the information technology related costs to relocate multiple IRS activities from the remaining nine satellite sites located throughout Philadelphia into a single facility in the United States Postal Service (USPS) main building located in Philadelphia, PA. These activities include compliance and customer account services, operations support, taxpayer advocate services, and appeals. Relocation to the USPS site presents several benefits, including

rent stability, improved employee access to public transportation, and a quality work environment.

## IRS Funding History

(Dollars in Thousands)



## Appropriations and Budget Activities

### Processing, Assistance and Management (PAM)

The FY 2007 request level is \$4,045,122,000 in direct appropriation, supplemented by \$114,771,000 in new user fee revenue, for a total operating level of \$4,159,893,000. This is an increase of 1.6 percent from the FY 2006 enacted level. This appropriation funds the following budget activities:

**Pre-Filing Taxpayer Assistance and Education** (\$329,557,000 from direct appropriation and \$4,120,000 from new user fees) provides services to assist with tax return filing and includes interpretation of the tax laws, media, and publications. The IRS continues to emphasize taxpayer education, outreach, increased volunteer support time and locations, expanding pre-filing agreements and rulings, and enhancing pre-filing taxpayer support through electronic media.

**Filing and Account Services** (\$1,618,784,000 from direct appropriation and \$110,651,000 from new user fees) funds taxpayer services, issuing refunds, and maintaining taxpayer accounts in addition to the processing of all paper and electronically submitted tax returns. The IRS continues to make progress in

decreasing paper returns and increasing the use of electronic filing and payment methods. The IRS is increasing both the capacity and effectiveness of its telephone and in-person taxpayer support.

**Shared Services Support** (\$1,504,247,000 from direct appropriation) provides administrative services to all IRS employees. Included in this activity are facilities services, rent payments, printing, postage, and security.

**General Management and Administration** (\$592,534,000 from direct appropriation) includes resources for top-level management and IRS-wide support for strategic planning, communications and liaison, finance, human resources, legal services, and specific benefits programs.

### Tax Law Enforcement (TLE)

The FY 2007 request level is \$4,762,327,000 in direct appropriation, supplemented by \$2,627,000 in new user fee revenue, for a total operating level of \$4,764,954,000. This is an increase of 1.8 percent from the enacted level. This appropriation funds the following budget activities:

**Compliance Services** (\$4,496,735,000 from direct appropriation and \$2,627,000 from new user fees) provides services to the taxpayer after a return is filed and identifies and corrects possible errors or underpayment. These programs enforce the tax laws and compliance through examination and collection activities, criminal investigations, and appeals. Funding also provides for the Taxpayer Advocate Service.

**Research and Statistics of Income** (\$97,542,000 from direct appropriation) provides resources for researching annual income, financial, and tax data from tax returns filed by individuals, corporations, and tax-exempt organizations. It also provides resources for market-based research to identify compliance issues, for conducting tests of treatments to address non-compliance, and for the implementation of successful treatments of taxpayer non-compliant behavior.

*Earned Income Tax Credit (\$168,050,000 from direct appropriation)* funds customer service and public outreach programs, strengthened enforcement activities, and enhanced research efforts aimed at reducing erroneous claims and filings associated with the Earned Income Tax Credit (EITC).

### **Information Systems (IS)**

The FY 2007 request level is \$1,602,232,000 in direct appropriation, and by \$17,602,000 in new user fee revenue, for a total operating level of \$1,619,834,000. This is a 2.3 percent increase from the FY 2006 enacted level. This appropriation funds the following budget activities:

*Information Systems Improvement Programs (\$49,302,000 from direct appropriation)* funds improvements or enhancements to business applications or internal management systems that conform to the modernized IRS architecture on which IRS operations depend.

*Information Services (\$1,552,930,000 from direct appropriation, and \$17,602,000 from new user fees)* provides funding for salaries, benefits, and related costs to manage, maintain, and operate the information systems critical to the support of tax administration programs. The IRS' business programs rely on these systems to process tax and information returns, account for tax revenues collected, send bills for taxes owed, issue refunds, assist in the selection of tax returns for audit, and provide telecommunications services for all business activities including the public's toll-free access to tax information.

### **Business Systems Modernization (BSM)**

The FY 2007 request level is \$167,310,000, 15.1 percent less than the FY 2006 enacted level.

*Business Systems Modernization (\$167,310,000 from direct appropriation)* provides resources for the planning and capital asset acquisition of information technology to modernize the IRS' business systems. The program combines best practices and expertise in business solutions and internal management from IRS, business, and technology to develop a

world-class tax administration system that fulfills the revenue collection requirements of the United States as well as taxpayers' needs and expectations.

### **Health Insurance Tax Credit Administration (HITCA)**

The FY 2007 request level is \$14,846,000, a decrease of 25.8 percent from the FY 2006 enacted level.

*Health Insurance Tax Credit Administration (HITCA) (\$14,846,000 from direct appropriation)* provides resources to administer a refundable tax credit for health insurance to qualified individuals, which was enacted as part of the Trade Adjustment Assistance Reform Act of 2002.

## **Legislative Proposals**

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The Administration proposes five new legislative changes to reduce the tax gap and re-proposes four legislative changes to improve tax administration efficiency. In addition, the Administration will study the standards used to distinguish between employees and independent contractors for purposes of withholding and paying federal employment taxes. The nine legislative changes are:

### **Closing the Tax Gap**

- *Clarify the circumstances in which employee leasing companies and their clients can be held jointly liable for federal employment taxes.* This proposal would facilitate the effective use of third party employee leasing companies by small businesses to pay employment taxes. In addition to clarifying joint liability, it would also provide standards for holding employee leasing companies solely liable for such taxes, if they meet specified requirements.
- *Increase information reporting on payment card transactions.* In order to improve compliance, payment card issuers would be required to report to the IRS annually the aggregate reimbursement payments made to certain businesses in a calendar year.
- *Expand information reporting to certain payments made by federal, state and local governments to procure property and services.* This proposal would

improve tax compliance of those taxpayers who do business with government agencies.

- *Amend Collection Due Process procedures for employment tax liabilities.* For Collection Due Process purposes, this proposal would align the treatment of levies to collect employment taxes with the treatment of levies to collect federal taxes from state tax refunds. The proposal would curtail delinquent employers' ability to pyramid multiple periods of unpaid employment tax liabilities. Taxpayers would retain the ability to seek managerial appeal and to participate in the formal Collection Appeals Process.
- *Expand to non-income tax returns the requirement that paid return preparers identify themselves on such returns and expand the related penalty provision.* This proposal would address the growing problem of return preparers who assist in the preparation and submission of improper excise, employment tax, and other non-income tax returns and related documents.

### Improving Tax Administration

- *Implement administrative reforms to improve the efficiency of IRS operations such as:* (a) adopt measures to reduce frivolous submissions made solely to delay or impede tax administration; (b) allow the IRS to terminate installment agreements if the taxpayer is not paying as agreed; and (c) streamline jurisdiction over collection due process cases in the Tax Court.
- *Initiate cost savings measures such as:* (a) Reduce transaction costs by changing the way the Treasury Department's Financial Management Service is reimbursed for offsetting collections, and (b) expand IRS' authority to require electronic filing.
- *Authorize the IRS to access employment data in the HHS' National Directory of New Hires* for tax administration purposes, including data matching, verification of taxpayer claims during return processing, preparation of substitute returns for non-compliant taxpayers, and identification of levy sources.

- *Extend IRS' authority to fund undercover operations,* which expires on December 31, 2006, to permit the IRS to fund certain necessary and reasonable expenses of undercover operations, including international and domestic money laundering and narcotics operations.

The legislative changes strategically target areas where (1) research reveals the existence of significant compliance problems, (2) improvements will burden taxpayers as little as possible, and (3) the changes support the Administration's broader focus on identifying legislative and administrative changes to reduce the tax gap. The implementation of these legislative changes positions the IRS for improved service and enforcement productivity. Additional information about these proposals is included in the FY 2007 Treasury Blue Book, which contains all of the Administration's legislative proposals.

