

**INTERNAL REVENUE SERVICE
ADVISORY COUNCIL**

GENERAL REPORT

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OF THE
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INTRODUCTION

The purpose of the Internal Revenue Service Advisory Council (hereinafter “IRSAC” or the “Council”) is to provide an organized public forum for discussion of relevant tax administration issues between Internal Revenue Service (hereinafter “IRS” or the “Service”) officials and representatives of the public. Its membership consists of up to twenty-three individuals who bring a wide variety of experience, expertise, and background to the Council’s activities.

The IRSAC has organized itself into three subgroups, comprised of three of the four IRS Operating Divisions: the Large & Mid-Size Business Subgroup (hereinafter the “LMSB Subgroup”); the Small Business/Self-Employed Subgroup (hereinafter the “SB/SE Subgroup”); and the Wage & Investment Subgroup (hereinafter the “W&I Subgroup”). The reports of the subgroups that follow this general report are a result of four working sessions and numerous conference calls between IRSAC members and key IRS personnel.

The members of the IRSAC wish to extend their thanks and appreciation to those operating division representatives who participated in this year’s Council meetings. These devoted staff members, along with the support staff of the Office of National Public Liaison (NPL), were instrumental in making this year’s Council activities run smoothly. (“flawlessly” seemed a bit of a stretch in light of the June flood)

This past year, IRSAC discussed many issues in an effort to assist the IRS in meeting its mission of providing 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.

We began the year with a collaborative, brainstorming session to identify issues each member believed to be important to the IRS and to taxpayers. Our goal was to highlight issues that were significant and complementary to issues the IRS operating divisions had identified for IRSAC consideration. Throughout the year, many presentations were made to the full IRSAC on topics including Earned Income Tax Credit, the Cash Economy, and e-Filing, as well as controversial topics such as the outsourcing of some collection functions. The IRS solicited input from IRSAC on the outsourced collection of low dollar cases and of those with little collection potential. IRS provided the full range of issues and concerns regarding the program, while explaining the process and procedures established to minimize negative impact on taxpayers and employees. The IRSAC commends the IRS for formulating the program and fully supports its implementation as an effort to reduce its accounts receivable and the tax gap.

The balance of the year was filled with many opportunities for IRSAC to contribute to IRS goals and programs. In particular, the IRS requested input from IRSAC on the five tax gap legislative initiatives the IRS was contemplating and has subsequently proposed to Congress. Those initiatives include:

- Expanding third-party information reporting to include certain Government payments for property and services;
- Expanding third-party information reporting on debt and credit card reimbursements paid to certain merchants;

- Clarifying liability for employment taxes for employee leasing companies and their clients;
- Expanding beyond income taxes the requirement that paid return preparers sign returns, and imposing a penalty when they fail to do so; and
- Authorizing the IRS to issue levies to collect employment tax debts prior to collection due process proceedings.

Input from IRSAC to SB/SE Commissioner Kevin Brown included honest and open dialogue prior to any announcement to the media, taxpayer groups, or taxpayers on these potentially sensitive initiatives.

Like the IRS, IRSAC was impacted by the flooding of IRS Headquarters in June 2006, resulting in the cancellation of the Council's July meeting in Washington D.C. Given IRSAC's strong desire to provide input to the IRS, we met as a full IRSAC via conference call. The subgroups also met by conference call or at alternative sites in lieu of their regular July meetings. Members were committed to continuing the work of IRSAC despite the logistical barriers.

To ensure that the IRS maintains a pool of diverse and qualified candidates for future Councils, we committed to work with NPL on the recruitment of 2007's new members. Members of the IRSAC were present at three of the IRS Nationwide Tax Forums and held town hall meetings with interested attendees. The town hall meetings were intended to disseminate an understanding of IRSAC's purpose and to provide information to potential candidates on the operations of IRSAC, the time commitment required, and the expectation that issues be approached in a team-like atmosphere. We

believe this interaction contributed to the number and quality of the applications that the NPL received for IRSAC this past nomination season.

Although each subgroup worked on issues of importance to its affiliated operating division, the full IRSAC believed that we should also provide feedback as a group on common issues that affect all operating divisions. During the January brainstorming session noted above, IRSAC identified two important IRS issues, Hiring Initiatives and Taxpayer Burden, and has included reports on those issues in the pages that follow. As all the issues and recommendations contained in this report are reviewed, it is hoped that the reader will conclude that the matters were fully addressed, relevant and frank input was obtained from an assortment of stakeholders, and, most importantly, quality feedback has been provided to the IRS.

Commissioner Mark Everson told the Council at the beginning of this year: “You are the eyes and ears of the practitioners and taxpaying public,” and he expressed appreciation for our eagerness to serve and our honest feedback. We believe this partnership has proven beneficial for both the IRS and taxpayers by giving the IRS input from outside the beltway. Each of us has enjoyed this partnership, and, collectively, we hope that this report provides valuable input to the IRS.

ISSUE ONE: HIRING INITIATIVES

Executive Summary

The hiring of IRS employees is critical to the mission of the IRS. The IRSAC finds that those individuals charged with developing and carrying out the Service's hiring initiatives are doing an exemplary job in a very difficult budgetary environment.

However, a number of suggested actions may increase the effectiveness of future hiring initiatives. Many of the recommended actions are already in process. Some of the recommendations may require legislative and/or executive branch action outside the IRS.

Background

Hiring initiatives was made a subject for IRSAC consideration at the request of the IRSAC after its January meeting in Washington, D.C. IRSAC's initial concerns were (1) the possible effect of baby boomer retirements on IRS staffing needs and (2) whether current IRS hiring practices and procedures were up to the task of meeting this challenge. IRSAC received written materials and heard reports concerning the IRS's current hiring initiatives at its May 2006 meeting in Washington, D.C. and in a conference call on August 25, 2006. Additional data was provided by e-mail on August 30, 2006. The information provided gave the members of IRSAC a better understanding of the recruiting and hiring processes of the IRS. IRSAC was also informed of some upcoming changes and programs that look promising.

Recommendations

1. Develop an online exit survey for all employees retiring or otherwise voluntarily leaving the employment of the IRS. The data from this survey could be used to determine whether there are any systemic factors that cause early retirement or

- voluntary separation from IRS employment by qualified employees. Eliminating these factors might improve retention, which would directly impact the number of new hires needed to fulfill IRS staffing requirements. It might also lead to an increase in referrals of new recruits by retiring and/or former IRS employees.
2. Expand the use of an online survey for all new hires of all operating divisions. The LMSB operating division uses an online survey for new hires. The SBSE operating division is in the process of developing one. The type of data gathered in such a survey is useful in determining what works and what does not work in recruiting and hiring.
 3. Include questions in the online new hire survey regarding what TV shows, web sites, magazines, and newspapers the new hire most frequently viewed and/or read for all purposes in the twelve-month period before he or she applied for employment with the IRS. While recruits may have learned about the IRS positions for which they applied from a job-related web site and/or publication, data regarding their general web and media usage may allow more effective, targeted advertising for new recruits. The portion of the online survey that contains these questions should indicate the purpose of the questions, and the survey should be anonymous.
 4. Increase the use of referral fees and sign-on bonuses. Sign-on bonuses and referral fees have both proven to be very useful recruiting tools. While each technique is subject to budgetary constraints, the statistics presented to the IRSAC appear to indicate that funds expended in this fashion produce better hiring results.

5. Continue and expand recruiting efforts for individuals recently or soon to be separated from the military. After World War II, the Korean War and the Vietnam War, a significant number of veterans chose to be employed by the IRS. Former military personnel constitute a well-trained, well-disciplined talent pool from which to obtain new employees who are already accustomed to working in a large organization with a known chain of command.
6. Allow telephone workers to operate from home by expanding the pilot telecommuting program and the hours of its operation and, if possible, making it permanent. The IRS finds it particularly difficult to recruit workers for its telephone "customer support" and other similar telephone functions. Part of the difficulty is due to the hours of service and the physical location and surroundings of call centers. The private sector has long recognized these issues and has responded by instituting telecommuting policies for these functions. The expansion of telecommuting might also allow the IRS to expand its current telephone-based customer services to later evening hours and weekends.
7. Expand the use of the Federal Career Intern Program. The Federal Career Intern Program is not subject to the same procedural restrictions as the normal competitive process within the IRS. It is an "Excepted Service Program" and, as such, is less labor intensive for recruiters and involves less wait time for recruits.
8. Streamline the IRS's current competitive process. Although streamlining the IRS's current competitive process would probably involve the input and action of individuals and groups outside the IRS, such as the National Treasury Employees

Union, the Office of Management and Budget, and potential legislative action, it is suggested that the increase in hiring efficiency obtained would justify the effort.

9. Work with Treasury to determine whether there is any way to more precisely coordinate the foreseeable hiring needs of the IRS with the reality of the existing budget process. As of August 25, 2006, there were three different budget proposals for the fiscal year ending September 30, 2007 regarding the hiring of new Revenue Agents in the LMSB Division. The President's proposal allowed for 350 new Revenue Agents. The Senate proposal allowed for the hiring of 600 new Revenue Agents. The House proposal allowed for no new Revenue Agents. Because of the competing views on the appropriate budget regarding the future funding of IRS personnel, it is very difficult for those IRS employees responsible for planning future hiring initiatives to prepare with any degree of certainty. It also can make it difficult to extend offers to desirable recruits and may result in offers to desirable recruits being delayed. This results in a loss of talent and wasted recruiting effort. The entire process is made even more difficult by the fact that frequent changes to the Internal Revenue Code occur with little consideration to the staffing needs of the IRS.
10. Expand recruiting efforts at the IRS Nationwide Tax Forums. One of the questions most frequently asked by forum attendees was: "How can I become an IRS employee?" While there were organized recruiting efforts at two of the forums, the IRSAC believes that it would be productive to have such an effort at all of the forums.

11. Investigate the feasibility of developing a student loan deferral or forgiveness program as a recruiting tool. Such programs have been effective in drawing talented applicants to other areas of public service.
12. Determine whether there is a way to simplify the number of steps it takes to use the IRS online Career Connector function. One of IRSAC's members accessed the IRS online Career Connector function as a test. The test suggested that the system needs simplification.

ISSUE TWO: BURDEN REDUCTION

Executive Summary

The size and complexity of the Internal Revenue Code and regulations place burden on both the taxpaying public and IRS employees. Burden increases the tax gap by increasing the likelihood that normally compliant taxpayers will become non-compliant and reduces the effectiveness of the IRS by increasing the number of examinations required. To counteract this, the Office of Taxpayer Burden Reduction (OTBR) must be a focal point for burden reduction projects and decisions within the IRS. OTBR has had some successes, but to be an even more effective force, OTBR should improve its decision-making process by developing more precise, quantifiable methods and criteria for determining appropriate burden reduction projects. We commend IRS burden reduction efforts to date and recommend increased funding for this function.

Background

Taxpayer burden is defined as the cost and time incurred by taxpayers to comply with the Federal tax system. OTBR was formed in 2002 to address increasing taxpayer burden, resulting largely from frequent tax law changes and the ever-increasing size and complexity of the Internal Revenue Code and regulations. OTBR is currently staffed by fewer than ten employees, mostly analysts. It works with the IRS Taxpayer Burden Reduction Council, a group of top level executives representing all major operating units within IRS, to recommend and implement burden reduction projects. In fact, IRS estimates that burden, since the creation of OTBR, has been reduced by more than 200 million hours. We commend these efforts by the IRS. However, despite this

achievement, taxpayer burden has increased from 6.4 billion hours in FY2005 to 6.65 billion hours in FY2006.

The mission of OTBR is to reduce burden for taxpayers. To accomplish this goal, OTBR is allowed to consider the effect a taxpayer burden reduction project will have on IRS expenses, but must otherwise focus on taxpayer burden – not IRS burden. OTBR receives recommendations for burden reduction projects from:

- Form 13285, “Taxpayer Burden Reduction Referral Form,” submitted by IRS employees and the similar Form 13285-A, “Reducing Tax Burden on America’s Taxpayers,” used by the taxpaying public.
- Industry Issue Resolution (IIR) requests, often submitted by industry associations
- Advisory councils such as the Internal Revenue Service Advisory Council (IRSAC) and the Information Reporting Program Advisory Committee (IRPAC)
- Stakeholder forums
- Taxpayer Advocacy Panel

Although OTBR has had many successes, we believe there have been some missteps, most notably the 944 project, whose effectiveness has been broadly questioned by the payroll industry and the Taxpayer Advocate Service. To enhance the IRS’ ability to define and implement burden reduction projects and to avoid questionable projects, we have a number of recommendations.

Recommendations

1. OTBR currently considers many criteria in determining a burden reduction project's potential. However, there is little quantification that takes place. There should be more metrics used to clearly define which projects are worthy of advancement and which are not. At the very least, OTBR should develop a checklist that weighs the various aspects of a project by assigning each aspect a numerical value and a weight. For example, the effect on the tax gap could be given a numerical value of 1-10 and would be weighted more heavily in the overall calculation than the amount of postage the project could save. Similarly, increasing taxpayer confidence in the fairness of our tax system and, thus, encouraging voluntary compliance should be reflected in the project's score. This type of quantification could be a first step in a multi-step process of determining project viability. Some areas where impact should be quantified: tax gap, IRS resources, revenue, complexity of taxpayer decisions, compliance, post-filing notices, and visibility.
2. Although monetary incentives are currently given to IRS employees, they are usually very small. IRS should provide significant monetary incentives to IRS employees whose suggestions are selected for implementation. These incentives should be large enough to make the completion of Form 13285 a worthwhile effort and should be more widely publicized within the IRS workforce than is presently done.
3. IRS should make similar incentives available to tax preparers. Many preparers, if provided with compensatory incentives, might be motivated to share burden

- reduction ideas. Form 13285-A should be more widely advertised through trade associations.
4. OTBR must always analyze the end-to-end process when deciding upon a burden reduction project. It is important to realize that requiring a taxpayer to step through a complex decision tree, in itself, creates burden. For instance, there is some question as to whether a single employment tax deposit schedule (semiweekly or monthly) for everyone might be a better alternative than the current system that depends on lookback periods and undeposited liability (for \$100,000 deposits). In fact, in 2005, the Taxpayer Advocate Service listed the complexity of the employment tax deposit system as one of the most serious problems encountered by taxpayers. In this case, aspects such as pre-deposit decision making, IRS system complexity, and post-deposit penalty notices should be weighed against revenue considerations. In addition, it should be noted that simplicity could lead to improved taxpayer behavior (particularly in the cash economy) and a reduced tax gap.
 5. In addition to taxpayer burden reduction projects, OTBR should pursue burden reduction projects that are primarily for IRS benefit, such as electronic delivery of notices to tax preparers. Often, what reduces burden within the IRS also reduces burden for the taxpayer and/or tax preparer. However, a litmus test for IRS-centric burden reduction projects should be whether the project adversely affects taxpayers or preparers. If it does, then it probably is not an appropriate burden reduction project. In light of this recommendation, we suggest that the name of

the department be changed to the Office of Burden Reduction to more clearly describe its role.

6. Unless there are valid, overriding considerations, burden reduction implementations should be voluntary. Taxpayers should have the ability to pursue compliance as they previously had prior to the implementation of the project. For instance, OTBR is currently considering adding a simplified method for calculating the home office deduction. Instead of the current, complex “percent of total” calculation, taxpayers will be able to choose to deduct a specific amount per square foot. In this respect, a parallel to the automobile standard mileage deduction can be drawn – it is voluntary. While the square foot calculation would be simple, a taxpayer who has been using the “percent of total” calculation for years should and, if implemented as planned, will be allowed to continue using that methodology. In other words, burden reduction projects should be implemented as opt-in rather than opt-out. Failure to do this was the mistake made when the 944 project was launched. It was implemented as a mandatory, opt-out program, rather than a voluntary, opt-in program. In many cases, it has increased burden both for the taxpayer and the IRS. For example, some smaller payroll providers may decide to only partially support 944 filing, causing taxpayers, who were previously e-filed as part of an automated 941 process, to have their 944 filed on paper via a manual process.
7. OTBR and the IRS’ desire for burden reduction should be better publicized to taxpayers and practitioners. Advertising spots could be included on Tax Talk Today. Also, Form 13285-A could be provided in the participant packet, and

workshops on burden reduction included, at the Nationwide Tax Forums.

Colleges should be encouraged to include a burden reduction exercise as part of federal tax courses.

8. OTBR should become the expert focal point for burden reduction within the IRS. OTBR should be consulted on burden reduction projects that emanate from, or are driven by, other areas of the IRS. For instance, OTBR should be consulted on burden impact for projects such as the recently implemented change in W-4 submission requirements. Because of the change in the lock-in timing, the employer's administrative burden has actually increased as a result of this project, which was originally intended to be beneficial to the employer.
9. Monetary thresholds are low hanging fruit for burden reduction and should be reviewed on a regular basis. These thresholds, such as the change of the FUTA deposit requirement from \$100 to \$500 or the increased threshold for Form 1040EZ and 1040A filers, have been the subject of several effective burden reduction projects. The implementation of threshold changes, assuming no legislative authority is required, is much simpler than the typical burden reduction project because there is minimal effort required in systems reprogramming, employee training, or process change.
10. Burden reduction projects should simplify processes, including calculations, whenever possible, so that taxpayers can more easily understand their obligations. For instance, an online interest calculator similar to the EITC Assistant and the AMT Calculator, which were previously implemented, would benefit taxpayers

by allowing them to verify interest charged, thus increasing their confidence in the system.

11. The IRS should be wary of any burden reduction project or IRS pronouncement that requires taxpayers to submit information that may not be used. Scheduled reviews of reporting requirements should be done to determine if requested information is being used or is needed.
12. OTBR uses focus groups to analyze proposed projects. We applaud this practice and hope that it will be continued and expanded. In all stages of development, projects that have been vetted through diverse focus groups (IRS employees, taxpayers, tax practitioners) should benefit from the feedback and result in better decision-making and more successful projects.
13. In general, we commend the IRS initiatives that were described in OTBR Acting Director Beth Tucker's testimony before the House Committee on Government Reform on July 18, 2006. In light of the current limited staffing of OTBR and our belief that OTBR should be taking on additional responsibility for the oversight of burden implications, IRS should allocate additional resources to the burden reduction function.