

**WRITTEN TESTIMONY OF
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BEFORE THE
HOUSE APPROPRIATIONS COMMITTEE
SUBCOMMITTEE ON FINANCIAL SERVICES
AND GENERAL GOVERNMENT
ON FY 2012 IRS BUDGET
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INTRODUCTION & SUMMARY

Chairwoman Emerson, Ranking Member Serrano, and Members of the Subcommittee, thank you for the opportunity to appear today to discuss the President's FY 2012 Budget Request for the Internal Revenue Service (IRS).

This Budget was crafted during a time of fiscal austerity and belt tightening for the nation and it is incumbent upon all of us in government to be as efficient as possible and spend taxpayer dollars wisely. That means finding savings where we can, and continuing to invest in strategic priorities that allow us to continuously improve.

Against this backdrop, it is clear that the IRS is vital both to the functioning of government and keeping our nation and economy strong. In FY 2010, the IRS collected \$2.345 trillion in gross revenue to fund the federal government, approximately 93 percent of all federal receipts. Moreover, for Fiscal Year 2010, we processed more than 140 million individual income tax returns and issued 109.5 million refunds to individual taxpayers totaling \$366 billion.

A Record of Success

The IRS is proud of its implementation track record over the past few years.

We have run smooth filing seasons for the last several years, despite new tasks being added to our agenda and late passage of legislation.

We have also made good strides in cracking down on international tax evasion. We struck a landmark deal with the government of Switzerland, and for the first time received information on thousands of Americans hiding assets in Swiss bank accounts. As we turned up the pressure on those not paying taxes on overseas assets, we had approximately 15,000 voluntary disclosures from individuals who came in under our special Voluntary Disclosure Program (VDP). Since the special program closed, we received an additional 3,000 voluntary disclosures from individuals with bank accounts from around the world.

Many of these voluntary disclosure cases involve significant amounts of previously unpaid tax.

However, collecting such substantial additional revenue for past misdeeds is not the only important consideration here. Regardless of dollar size, it is important that we are bringing thousands of US taxpayers back into the system so they properly report and pay their taxes for years to come on their offshore accounts.

Last month, the IRS announced a new special voluntary disclosure program designed to help people with undisclosed income from hidden offshore accounts get current with their taxes.

In 2010, the IRS also took a major step towards transparency with Announcement 2010-9 to require business taxpayers to report basic information regarding their uncertain tax positions (UTP) when they filed their tax returns.

This new requirement helps to achieve what most taxpayers and the IRS strive for: certainty, consistent treatment and the efficient use of government and taxpayer resources by focusing on issues and taxpayers that pose the greatest risk of tax noncompliance.

One of the most important initiatives that the IRS has undertaken in recent memory is the return preparer initiative, which is now being implemented. In September 2010, we launched the new online PTIN (Preparer Tax Identification Number) application system. It is up and running with hundreds of thousands of preparers already registered in the system.

More than just an identification number, the PTIN registration process gives the IRS an important and better line of sight into the return preparer community than we have ever had before. We can leverage that information to help us better communicate, analyze trends, spot anomalies and potentially detect fraud.

The registration process will help us build in several years a publicly-accessible database of preparers who are authorized to prepare returns. This is an extremely important tool for consumers as they will be able to search the database to ensure that their preparer is registered. It will also make it easier to find and track the bad actors out there. They will not be able to pull up stakes and move around anonymously.

The IRS is also very proud of its work in implementing the tax-related provisions of the American Recovery and Reinvestment Act (ARRA) and other economic recovery legislation. We put billions of dollars to help people buy homes and stabilize the housing market through the First-time Homebuyer Credit, and we added \$400 to \$800 to families' paychecks through the Making Work Pay Credit, just to name two provisions.

The IRS continues to provide taxpayers with quality customer service and different service channels and products. They run the gamut from traditional walk-in sites for those who need to see an IRS representative face-to-face, to toll-free automated and assistor telephone service, to web-based applications and social media. All make it easier for taxpayers to file and pay their taxes.

Telephone level of service is recovering after several challenging years. Toll-free assistor level of service (LOS) increased by 4 percent over the previous year to 74 percent. Toll-free tax law accuracy remained at 93 percent, and the overall toll-free customer satisfaction rating stood at 92 percent. Last year, we also saw a 70 percent e-file rate for individuals as compared to a mere 10 percent 15 years ago. As noted in the next section, this translates into a huge savings.

IRS.gov has become the favorite source of information for millions of taxpayers. For FY 2010, there were almost 305 million web page visits to IRS.gov –a 14 percent increase over the same time period in FY 2009. Use of the “Where’s My Refund” electronic tracking tool continued to post double-digit yearly gains.

The IRS is increasingly communicating with taxpayers who may not get their information from traditional sources, such as newspapers and broadcast and cable news. By employing social and new media, such as YouTube, Twitter and even iTunes, we are able to reach these taxpayers with important service and compliance messages.

In January 2011, the IRS also unveiled IRS2Go, its first smartphone application that lets taxpayers check on the status of their tax refund and obtain helpful tax information. This new smartphone app reflects our commitment to modernizing the agency and engaging taxpayers where and when they want.

Finally, the IRS continues to run robust compliance programs. We continue to have appropriate and balanced audit coverage rates across taxpayers and to innovate in our collection programs.

In short, despite a quickly evolving taxpayer base and unprecedented demands on IRS resources, the IRS continues to deliver for the American people.

Working Smarter and Greater Efficiencies

The IRS continues to reap the financial benefits of the E-File program, one of the most successful modernization programs in government. Today we receive nearly 100 million tax returns electronically. In the past these returns had to be opened, sorted, and transcribed manually. The efficiency savings have allowed us to reduce our submission processing sites in half. This year we are closing our 5th of the original 10 sites.

The FY 2012 Budget Request includes almost \$190 million in efficiency savings, reductions, and non-recurs. While these targets are substantial, I am confident that we will meet them and more, by finding cost-savings in our operations wherever we can.

I have also challenged the IRS leadership and indeed, all IRS employees, to take a hard look at their operations and look for potential savings and efficiencies.

Even in a tough budget environment, I am confident that the IRS will continue to deliver value for the American taxpayer and will emerge as a stronger agency in the years to come.

I am particularly pleased with the progress that we are making in achieving efficiencies in our technology operations. The IRS has embarked on a multi-year effort to streamline and standardize processes that will allow for substantial efficiency gains. For example, the Information Technology Infrastructure Library is a collection of best practices used to aid in the implementation of a lifecycle framework for IT Service Management. In September 2010, an independent third party found that the IRS recently reached Capability Maturity Model (CMM) Level 2 based on established criteria.

Achieving this level allows standardized project management practices across projects. This will improve our agility and quality in delivering software to our business customers and the taxpaying public, as well as reduce the cost of developing and maintaining products, and improve the cost of engineering services.

Investing in Core Programs

Indeed, it is in recognition of the critical role that the IRS plays in the economy that the FY 2012 Request includes a judicious investment in the IRS' core service and enforcement programs and initiatives. Enforcement and customer service are not an either/or proposition. Accomplishing our mission requires that we do both well.

The Request also includes the necessary funding for completing on time for the 2012 filing season the core taxpayer account database. A fully operational customer account database will mean faster processing of returns, expedited refunds for 140 million individual taxpayers and enhanced data security.

The funding in the President's Budget Request will be used to carry out the IRS' strategic and balanced agenda that includes:

- Improved service to taxpayers, including enhancements to the IRS.gov website to meet taxpayer needs and growing demand for more e-services;
- Robust and targeted enforcement programs to address offshore tax evasion and improve tax compliance for corporate and high-income taxpayers;
- Completion of the new taxpayer account database and enhancements to our electronic filing platforms;
- Leveraging the Return Preparer Program to reduce non-compliance;
- Implementation of our Uncertain Tax Position reporting requirements;

- Combat errors and fraud for refundable tax credits, such as the Earned Income Tax Credit.
- Better use of data, such as credit card and securities basis information reporting;
- Implementation of new tax provisions, such as the Affordable Care Act (ACA);
- Workforce development to ensure that we have a talented and capable workforce for the foreseeable future; and
- Enhance workplace/physical security for IRS employees.

The IRS will also administer those portions of ARRA that were extended into 2011. These include the expanded Earned Income Tax Credit for families with three or more children, and the American Opportunity tax credit to help pay tuition and other expense for individuals enrolled in institutions of higher education. In addition, we continue to administer the Health Coverage Tax Credit (HCTC) that was enacted as part of the Trade Adjustment Assistance Reform Act of 2002.

The new enforcement personnel included in the request will generate more than \$1.3 billion in additional annual enforcement revenue once the new hires reach full potential in FY 2014. The return on investment (ROI) estimate does not include the indirect revenue effect of the deterrence value of these investments and other IRS enforcement programs, which is conservatively estimated to be at least three times the direct revenue impact.

THE ADMINISTRATION'S FY 2012 BUDGET REQUEST FUNDS KEY PRIORITIES

The IRS funding level for FY 2012 is \$13,283,907,000, which includes \$85,754,000 for maintaining current levels, a decrease of \$22,090,000 from non-recurring activities, a decrease of \$167,867,000 from efficiencies and savings, and a program increase of \$838,836,000 to improve taxpayer service, implement enacted legislation, strengthen enforcement, and continue migration of applications to the new taxpayer account database, CADE 2. By FY 2014, the revenue-producing enforcement investments are projected to increase annual enforcement revenue by more than \$1.3 billion annually.

The Budget Request supports these activities by providing:

- \$114,307,000 to improve taxpayer service and the IRS.gov website;

- \$605,671,000 to implement legislative mandates, handle new information reporting requirements, increase compliance efforts to address offshore tax evasion, focus on corporate and high-wealth returns, increase examination and collection coverage, and enforce tax return preparer compliance; and
- \$118,858,000 to enhance employee security, develop disaster recovery systems capability, and develop the information technology, infrastructure, and systems to implement the various ACA provisions.

Building on the FY 2010 Enacted Level

The FY 2010 enacted level for the IRS was \$12,146,123,000, supporting an estimated 94,766 FTE.

Maintaining Current Levels

- ***Adjustment to Reach FY 2011 President's Policy Level +\$401,665,000 / +1,653 FTE*** Adjustment from the FY 2011 Annualized Continuing Resolution Rate to reach the FY 2011 President's Policy Level. The President's Policy Level is equal to the FY 2011 President's Budget Request as adjusted for the proposed pay freeze.
- ***Adjustments Necessary to Maintain Current Levels +\$85,754,000 / 0 FTE*** Funds are requested for inflation adjustments in non-labor expenses such as GSA rent adjustments, postage, supplies and equipment and health benefits and the increase in Federal Employee Retirement System participation. No inflation adjustment is requested for pay in FY 2012.

Base Adjustments

- ***Technical FTE Adjustments \$0 / +501 FTE*** This adjustment reflects permanent changes made to ensure FTE levels are fully funded in the base budget.

Efficiencies and Savings

- ***Non-Recur Savings -\$22,090,000 / 0 FTE*** This is the net of reductions of non-recurring, one-time costs associated with the IRS FY 2011 enforcement initiatives (e.g., IT equipment and training).
- ***Increase e-File Savings -\$22,444,000 / -416 FTE*** This decrease is a result of savings from increased electronic filing (e-file). Savings are based on e-file projected growth, modernization, and the completion of the phased implementation of the Worker, Homeowner, and Business Assistance Act of 2009 (Public Law 111-92), which requires all paid tax return preparers who expect to

file more than 10 tax returns to file such returns electronically. electronic filing by tax return preparers.

- ***Reduce IT Infrastructure -\$75,000,000 / 0 FTE*** The IRS will reduce the unit costs of infrastructure through use of the Capability Maturity Model (i.e., a process improvement approach that yields efficiencies in software engineering); the Information Technology Infrastructure Library (ITIL) that will allow the IRS to improve the quality of IT services; and the further consolidation of security activities in the Cybersecurity organization to leverage security best practices.
- ***Reduce Contracts -\$20,754,000 / 0 FTE*** In accordance with Presidential guidance on controlling contracting costs, the IRS will achieve targeted savings through reduced contracting expenses.
- ***Reduce Administrative Expenses -\$14,331,000 / -66 FTE*** The IRS will reduce administrative expenses, including targeted attrition through hiring freezes.
- ***Eliminate Lockbox Fees -\$4,000,000 / 0 FTE*** The IRS will eliminate lockbox fees that now will be paid by taxpayers in installment agreements.
- ***Reduce Certain Mailings -\$4,000,000 / 0 FTE*** The IRS will eliminate printing and mailing of certain forms and publications and reduce the number of inserts in mailings.
- ***Reduce Training, Travel and Programs -\$27,338,000 / -41 FTE*** The IRS will reduce agency-wide non-technical training, non-case related travel, and the taxpayer communication and education program.

Program Reinvestment

- ***Submission Processing Consolidation (Atlanta) +\$1,486,000 / 0 FTE*** Increased use of e-file has led to consolidation of individual return processing sites. A portion of the increased e-File savings will be reinvested to fund the one-time separation costs associated with the September 30, 2011 closure of the Atlanta submission processing site. As the Atlanta consolidation approaches, the IRS will assist employees to find employment either in or outside the organization.

Program Increases

- ***Improve Taxpayer Service +\$81,307,000 / +519 FTE*** Funding for this initiative and the \$25.9 million increase from the FY 2011 President's Policy level will provide staffing to address rising demand and This initiative also includes funding to assist taxpayers in understanding ACA provisions and to make related call center and infrastructure changes to handle anticipated ACA-related service inquires.

- ***Expand Online Options through IRS.gov Improvements +\$33,000,000 / +15 FTE*** This initiative will continue the multi-year effort to replace the outdated web portal environment and provide additional online services to taxpayers. The Taxpayer Assistance Blueprint, Phase 2, targeted migration to the electronic channel and services as one of the five areas for improvement of IRS service delivery. IRS will achieve efficiencies by moving high-volume transactions to IRS.gov, improving taxpayer self-service, reducing taxpayer burden, increasing compliance, reducing costs, improving security, and these improvements will position IRS.gov as the preferred delivery channel of choice for taxpayer service.
- ***Increase International Service and Enforcement +\$72,596,000 / +377 FTE*** The IRS will implement reporting, disclosure and withholding requirements and expand coverage of international filings, conduct more in-depth international compliance work, strengthen compliance efforts related to offshore activity and grow the Global High-Wealth compliance group. This initiative will increase examinations of employment tax specialty program audits, individual audits, business audits; and criminal investigation case closures. As part of this overall effort, IRS will also implement changes contained in the Foreign Account Tax Compliance Act (FATCA).
- ***Increase Collection Coverage +\$52,000,000 / +413 FTE*** This initiative will expand work on the collection inventory and improve collection processes to bring taxpayers who fail to pay their tax debt into compliance. This funding will expand the Automated Collection Systems (ACS) program, address the increased workload for the Offers in Compromise (OIC) program due to program improvements and to more taxpayers experiencing economic hardship, and improve efficiency through innovative approaches to inventory selection. The additional staff will resolve an additional 144,300 tax delinquency accounts (TDA) (i.e., balance due accounts where returns were filed, but the taxes have not been paid) and 25,200 tax delinquency investigations (TDI) (i.e., investigations of taxpayers with unfiled returns who have not responded to a notice).
- ***Implement Merchant Card and Basis Reporting +\$35,730,000 / +415 FTE*** This initiative will staff programs to implement information reporting on merchant payment card and third party reimbursements enacted in the Housing and Economic Recovery Act of 2008 (Public Law 110-289) and basis reporting on security sales enacted in the Emergency Economic Stabilization Act of 2008 (Public Law 110-343).
- ***Increase Coverage to Address Tax Law Changes and Other Compliance Issues +\$96,718,000 / +497 FTE*** This initiative addresses compliance issues and new responsibilities arising from recent tax law changes included in major legislation such as ARRA and the ACA. This initiative will fund compliance programs needed for new provisions such as direct-pay bonds, new requirements on tax-exempt hospitals, a new fee on manufacturers and importers of branded prescription drugs, the excise tax on indoor tanning, and will also increase the

number of specialty program (i.e., employment tax, excise tax, and estate and gift tax) audits.

- ***Ensure Accurate Delivery of Tax Credits*** +\$260,293,000 / +834 FTE This initiative recognizes the important role IRS plays in delivering economic incentives through tax credits by improving the delivery of existing credits through a combination of improved technology tools and increased enforcement staffing. The initiative largely funds the information technology and other systems required to implement the new ACA premium assistance tax credit, which becomes effective in 2014. IRS must build new systems to support eligibility determination based on household income, and modify existing tax processing systems to support reconciliation of advance payments of the credit. The initiative also funds the appropriate compliance resources for the small employer tax credit that came into effect in 2010.
- ***Administer New Statutory Reporting Requirements*** +\$58,505,000 / +187 FTE Recent legislation establishes significant new information reporting and sharing requirements from third parties (such as employers, health insurance providers), and the Health Insurance Exchanges (the “Exchanges”) to administer the premium assistance tax credit, the individual coverage requirement, and the employer responsibility payment. Effective implementation will require significant enhancements to existing information returns systems to handle the additional volumes and new information reporting categories. The ACA also includes provisions that allow the IRS to share tax data with state and federal entities for the purpose of determining eligibility for the advance premium credit. This request also includes resources to ensure secure exchange of information and provides the initial staffing to establish the program to handle the additional inventory of non-filer assessments expected because of the expanded 2012 information reporting requirement for businesses to report all aggregate purchases of services or property greater than \$600.
- ***Leverage Return Preparer Program to Reduce Noncompliance*** +\$16,600,000 / +108 FTE The IRS is increasing tax return preparer oversight to ensure that tax return preparers are competent and to help ensure that the IRS collects the right amount of taxes. This initiative will ensure uniform and high ethical standards of conduct for tax return preparers by enforcing preparer compliance with IRS rules, increasing preparer examinations, and pursuing preparers engaged in fraudulent activities. This initiative is key to the IRS’s tax gap strategy and will increase government revenue.
- ***Address Appeals Workload Growth*** +\$9,100,000 / +66 FTE This initiative will allow the IRS to increase Appeals staffing. Despite improvements in cycle time and increased efficiency in working cases, Appeals continues to experience rising inventories, and because of the nature of Appeals work, the cases must be processed manually. The funding in this initiative will reduce, but not eliminate,

the stress put on the appeals process because of increased caseload. In addition, Appeals settlements generate increased revenues for the federal government.

- ***Implement Uncertain Tax Position Reporting Requirements*** +\$4,129,000 / +20 FTE This initiative will allow the IRS to provide guidance and certainty on UTPs and meet increasing taxpayer demands for this service. This increased workload is expected as a result of changes IRS has proposed for certain large business taxpayers to report information about their uncertain tax positions. It is a critical part of IRS's work to gain greater transparency into large corporate tax returns
- ***Enhance Security and Disaster Recovery Systems Capability*** +\$12,000,000 / +5 FTE This initiative is part of a multi-year improvement strategy to support the continued deployment of critical disaster recovery capabilities. It supports two critical business processes: Processing Remittances and Processing Tax Returns by reducing the recovery time dramatically for the critical applications supporting these processes.
- ***Update Integrated Financial System (IFS)*** +\$27,500,000 / +5 FTE This initiative provides funds to complete the first phase of an initiative to update IFS. This request will ensure IRS compliance with future federal accounting requirements and allow implementation of standard interfaces and communication with other federal systems. The IRS current financial system is more than ten years old and SAP software no longer provides updates or changes to accommodate new legislative or other federal accounting requirements. Without a system that will allow implementation of new federal accounting requirements, IRS compliance with federal financial management standards could be jeopardized.
- ***Leveraging Data to Improve Compliance*** +\$1,400,000 / +5 FTE The IRS is focused on using a data-driven approach to continually innovate and improve its programs. This investment will capitalize on the significant increase in data reported to the IRS, with the goal of increasing compliance. Funding will increase compliance through leveraging such data and/or evaluating the effectiveness of tax-related programs.
- ***Enhance Physical Security for Federal Employees*** +\$15,481,000 / +10 FTE The February 2010 attack against the IRS in Austin, Texas killed one IRS employee and injured several others. This initiative will provide investments needed to update and/or upgrade the physical security of IRS facilities. The investments will enhance the overall security of IRS employees in the work place, while maintaining open access for the taxpayers that they serve.
- ***Implement Individual Coverage Requirement and Employer Responsibility Payments*** +\$62,477,000 / +65 FTE This initiative will fund the development of the information technology, infrastructure, and systems to implement the ACA provision that establishes shared responsibility payments for both individuals and employers. Beginning in 2014, the ACA requires individuals who are able to

afford health insurance to obtain minimum essential coverage or pay a penalty, and large employers – those with 50 or more full-time employees – to make a shared responsibility payment if they do not provide affordable coverage to their employees, and at least one of their employees benefits from the premium assistance tax credit.

ENFORCEMENT PROGRAM

The FY 2012 President's Budget Request is \$5,966,619,000 in direct appropriations and an estimated \$75,902,000 from reimbursable programs for a total operating level of \$6,042,521,000. The total direct appropriations level includes an additional appropriation for tax enforcement and compliance activities funded through a program integrity allocation adjustment totaling \$1,257,000,000, of which \$936,000,000 will be funded from the Enforcement account. The allocation adjustment increases the Financial Services Committee's 302(b) level by the amount of the allocation adjustment. Congress used such an allocation adjustment mechanism to fund IRS enforcement initiatives in both FY 2009 and FY 2010 and the Administration proposed an adjustment of \$1,115,000,000 for FY 2011. This appropriation funds the following budget activities. This appropriation funds the following budget activities.

- **Investigations (\$678,849,000 from direct appropriations and an estimated \$66,567,000 from reimbursable programs)** This budget activity funds the criminal investigations programs that uncover criminal violations of the internal revenue tax laws and other financial crimes; enforces criminal statutes relating to these violations; and recommends prosecution as warranted. These programs identify and document the movement of both legal and illegal sources of income to identify and document cases of suspected intent to defraud. It provides resources for international investigations involving U.S. citizens residing abroad, non-resident aliens and expatriates and includes investigation and prosecution of tax and money-laundering violations associated with narcotics organizations.
- **Exam and Collections (\$5,103,420,000 from direct appropriations and an estimated \$8,761,000 from reimbursable programs)** This budget activity funds programs that enforce the tax laws and increase compliance through examination and collection programs that ensure proper payment and tax reporting. It also includes programs such as specialty program examinations (employment tax, excise tax and estate and gift exams), international collections and international examinations. The budget activity also supports appeals and litigation activities associated with exam and collection.
- **Regulatory (\$184,350,000 from direct appropriations and an estimated \$574,000 from reimbursable programs)** This budget activity funds the development and printing of published IRS guidance materials; interpretation of tax laws; advice on general legal servicing, ruling and agreements; enforcement of regulatory rules, laws, and approved business practices; and supporting taxpayers in the areas of pre-filing agreements, determination letters, and advance pricing

TAXPAYER SERVICE

The FY 2012 President's Budget Request is \$2,345,133,000 in direct appropriations, an estimated \$22,924,000 from reimbursable programs, and an estimated \$130,962,000 from user fees, for a total operating level of \$2,499,019,000. This appropriation funds the following budget activities:

- **Pre-Filing Taxpayer Assistance and Education (\$701,035,000 from direct appropriations and an estimated \$863,000 from reimbursable programs)**
This budget activity funds services to assist with tax return preparation, including tax law interpretation, publication, production, and advocate services. In addition, funding for these programs continues to emphasize taxpayer education, outreach, increased volunteer support time and locations, and enhancing pre-filing taxpayer support through electronic media.
- **Filing and Account Services (\$1,644,098,000 from direct appropriations, an estimated \$22,061,000 from reimbursable programs, and an estimated \$130,962,000 from user fees)** This budget activity funds programs that provide filing and account services to taxpayers, process paper and electronically-submitted tax returns, issue refunds, and maintain taxpayer accounts. The IRS continues to make progress in decreasing paper returns and increasing the use of electronic filing and payment methods.

BUSINESS SYSTEMS MODERNIZATION

The FY 2012 President's Budget Request is \$333,600,000 in direct appropriations. This appropriation funds the following budget activity:

- **BSM (\$333,600,000 from direct appropriations)** This budget activity funds the planning and capital asset acquisition of information technology (IT) to continue the modernization of IT systems, including labor and related contractual costs. The completion of the core database is the cornerstone of modernization and is a prerequisite to developing the next generation of IRS service and enforcement initiatives. The integration strategy includes a particular focus on enhanced information technology security practices and robust accounting and financial management controls. This activity also funds the ongoing development of the Modernized e-File platform for filing tax returns electronically.

OPERATIONS SUPPORT

The FY 2012 President's Budget Request is \$4,620,526,000 in direct appropriations, an estimated \$39,446,000 from reimbursable programs, and an estimated \$73,466,000 from user fees, for a total operating level of \$4,733,438,000. The total direct appropriations level includes an additional appropriation for tax enforcement and compliance activities funded through a program integrity allocation adjustment totaling \$1,257,000,000, of which \$312,000,000 will be funded from the Operations Support Account. The allocation adjustment increases the Financial Services Committee's 302(b) level by the amount of the allocation adjustment. Congress used such an allocation adjustment mechanism to fund IRS enforcement initiatives in both FY 2009 and FY 2010 and the Administration proposed an adjustment of \$1,115,000,000 for FY 2011. This appropriation funds the following budget activities. This appropriation funds the following budget activities:

- **Infrastructure (\$986,045,000 from direct appropriations, an estimated \$516,000 from reimbursable programs, and an estimated \$22,095,000 from user fees)** This budget activity funds administrative services related to space and housing, rent and space alterations, building services, maintenance, guard services, and non-IT equipment.
- **Shared Services and Support (\$1,313,050,000 from direct appropriations and an estimated \$20,577,000 from reimbursable programs)** This budget activity funds policy management, IRS-wide support for research, strategic planning, communications and liaison, finance, human resources, and equal employment opportunity and diversity services and programs. It also funds printing and postage, business systems planning, security, corporate training, legal services, procurement, and specific employee benefits programs.
- **Information Services (\$2,321,431,000 from direct appropriations, an estimated \$18,353,000 from reimbursable programs, and an estimated \$51,371,000 from user fees)** This budget activity funds staffing, equipment, and related costs to manage, maintain and operate the information systems critical to the support of tax administration programs. This includes the design and operation of security controls and disaster recovery planning. This budget activity also funds the development and maintenance of the millions of lines of programming code that support all aspects and phases of tax processing and the operation and administration of the mainframes, servers, personal computers, networks, and a variety of management information systems.

Health Coverage Tax Credit (HCTC) Administration

The FY 2012 President's Budget request is \$18,029,000 in direct appropriations. This appropriation funds the following budget activity.

- **HTCA (\$18,029,000 from direct appropriations)** This budget activity funds costs 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.

AFFORDABLE CARE ACT

The IRS will need to implement and administer the tax provisions of the Affordable Care Act (ACA) (Public Law 111-148) in 2012. IRS seeks to be helpful to families and businesses that will benefit from ACA. In fact, some benefits have already begun. For example, upon enactment of the ACA, the IRS immediately began to make sure that small employers were aware of a significant new tax credit to help them provide health coverage to their workers.

Because the tax credit was enacted mid-year, and was effective immediately, the IRS conducted a significant outreach campaign to small businesses. In addition to mailing postcards to millions of employers alerting them to the new credit, the IRS held or attended more than 1,000 outreach events targeted at small businesses, and the tax practitioners who serve them.

Working with the Department of Health and Human Services, we also administered a program to provide \$1 billion in tax credits and grants to qualifying therapeutic discovery projects.

In addition, we have implemented or have begun to implement changes that expanded the tax credit for adoptive parents, a new exclusion for loan forgiveness programs for certain health professionals, and a new tax on indoor tanning services.

We are also working diligently to implement the tax law components of the changes made to the health insurance marketplace that will begin in 2014. Let me put these efforts in context by describing the activities that we are undertaking to plan for these upcoming changes.

The IRS also has significant information technology development work that must be completed in order to administer these provisions. The vast majority of the resources that IRS will require between now and 2014 will be dedicated to technology and the associated business process design required to effectively administer these new provisions.

Exchanges and Medicaid Health Coverage

Individuals seeking subsidized coverage will interact with the IRS at a few discrete points in the process:

1. Obtaining coverage through exchanges and/or Medicaid

The ACA outlines eligibility rules for the premium assistance tax credit, as well as Medicaid. In both cases, the household income as reported to the IRS by approximately 140 million taxpayers on the 2012 tax returns will be relevant to

eligibility determination. The IRS will alter its systems to take account of the new concept of household income, and is planning to provide significant educational tools to help individuals understand what household income represents. Furthermore, planning is underway to determine the best way to provide this information to taxpayers via the Web, telephone, and other channels.

2. Receiving advance premium tax credits

Individuals who are determined to be eligible for the premium assistance tax credit can receive the benefit through advance monthly payments that are made directly to the plan provider. Working with the Treasury Financial Management Service, the IRS will develop new systems to administer these advance payments. In addition the IRS will work with the exchanges, as appropriate, to conduct significant outreach and education to make taxpayers who are receiving the advance payments aware of the importance of reporting mid-year changes in circumstance that could affect their eligibility for, or the amount of the credit.

3. Reconciling the premium assistance tax credit with advance payments made through the year

The ACA provides that individuals will reconcile the amount of advance payments of the premium credit with the actual amount as computed on the tax return. In other words, advance payments made throughout 2014 will be reconciled with individuals' tax returns that are filed in the spring of 2015. To the extent that the ultimate credit amount is larger than the sum of the advance payments, the additional amount will be added to the taxpayer's refund. If the ultimate credit amount is lower than the sum of the advance credit, the taxpayer will owe additional tax on the return. The amount owed may be capped, subject to the schedule outlined in the Medicare and Medicaid Extenders Act of 2010.

Individual Coverage Requirement

The IRS will also be responsible for administering the requirement that individuals who can afford health coverage either obtain it, or make a payment to the IRS. While implementation of this requirement does not come into effect until 2014, and will appear on the 2014 tax forms that will be filed in the spring of 2015, we have nonetheless received a number of questions about how this provision will be implemented.

First, we anticipate providing significant outreach and education on this provision. This will come directly from IRS and in partnership with state and federal agencies, employers, tax return preparers, and others. Our experience in administering new tax laws suggests that the vast majority of individuals will successfully incorporate this provision into their tax year 2014 returns, filed in 2015.

The forms will provide instructions on how individuals can determine if they met the coverage requirement, and if not, how to compute the payment and include it in that

year's tax liability. We also plan to work closely with the tax return preparation industry to ensure that the professionals who advise taxpayers are fully informed about this provision. Today, approximately 60 percent of taxpayers use a return preparer; another 25 percent use software to prepare their own returns.

For the remaining minority who do not get it right, the IRS will follow up with the taxpayer. While it is early in the planning process, I can describe for you the general parameters of how this will work.

Employer Provisions

Finally, the IRS will administer the employer responsibility payment for large employers who do not offer affordable coverage, and have at least one employee who receives subsidized coverage through the exchange. This provision closely intersects with the rest of the exchange provisions, and we are working closely with the Department of Health and Human Services and the Department of Labor to reach out to the employer community; understand what questions and issues they foresee; and incorporate the feedback that we get into the upfront program design and regulatory guidance.

Tax Law Changes

The IRS is also working diligently to implement other tax law changes that come into effect over the next several years. Earlier in my testimony, I mentioned several that we are already implementing, and would be happy to answer any questions that you have on those, or the provisions coming into effect in the months and years ahead.

CONCLUSION

In conclusion, let me thank the subcommittee again for this opportunity to discuss the IRS Budget Request for FY 2012. It is fiscally prudent and makes wise investments in strategic priorities in enforcement, service, and business modernization. It will help ensure that the IRS will continue its vital role in keeping our nation and economy healthy and strong.