

Brownstein

DATE: April 7, 2022

TO: Interested Parties

FROM: Brownstein Hyatt Farber Schreck

RE: Senate Finance Committee: “The IRS, the President’s Fiscal Year 2023 Budget, and the 2022 Filing Season”

On Thursday, April 7, the Senate Finance Committee held a hearing entitled, “The IRS, the President’s Fiscal Year 2023 Budget, and the 2022 Filing Season.” Testifying before the committee was Charles Rettig, commissioner of the Internal Revenue Service (IRS).

Member Opening Statements

Chair Ron Wyden (D-OR) attributed the tax return processing backlog to proposed budget cuts and unnecessary complexities imposed by the Tax Cuts and Jobs Act (TCJA, P.L. 115-97), both of which he attributed to Republicans. In addition, Wyden said the IRS has significantly reduced its number of employees over the past decade, causing an overall deterioration in customer service. Further, he said the IRS is not equipped with proper enforcement resources to prevent tax evaders. However, he said the increase in funding proposed by the president’s fiscal year (FY) 2023 budget request would allow the agency to dedicate resources to customer service. Finally, he expressed support for an expansion of free electronic filing. Ranking Member Mike Crapo (R-ID) expressed concern about various issues at the IRS, including the persistent return backlog and delays taxpayers endure when contacting the agency. However, he said funding is not the reason for these shortcomings. He instead suggested the IRS could implement certain reforms that would address these issues, such as expanding e-filing options and implementing 2-D barcodes on paper returns. These measures would reduce the need for IRS agents to transcribe paper returns. Finally, Crapo criticized other components of the administration’s budget request, including new reporting, compliance and enforcement regimes. Chair Wyden said Ranking Member Crapo has “a very good point” with respect to the barcodes.

Key Themes

- **Information Technology (IT) Infrastructure:** Sens. Chuck Grassley (R-IA) and Steve Daines (R-MT) asked how Congress could trust that additional funding would result in updated technology systems at the IRS. Commissioner Rettig said the agency launched a six-year business modernization plan in 2019 that has only received 57% of the necessary funding. Despite this, he highlighted the agency’s success in delivering economic recovery payments and Advanced Child Tax Credits during the COVID-19 pandemic as evidence of its capability to meet taxpayer needs. Ranking Member Crapo asked if the agency’s six-year plan would update IT processes without the need for future funding. Rettig said private sector financial institutions often invest around \$13 billion annually in their IT infrastructure. He said the IRS, by comparison, receives only \$2.7 million for such purposes, which is one reason it cannot keep pace with evolving technology. Ranking Member Mike Crapo (R-ID) asked when existing IRS account holders would be forced to move their accounts to ones that require a stricter authentication tool. Rettig said the IRS has no plans to require any account holders to move, though he said the agency is exploring options with ID.me to provide meaningful online self-service. Rettig also said the IRS is considering other options like login.gov but added that the website cannot currently handle IRS capacity. Login.gov

is a secure sign-in service for accessing government services, although it does not perform the same kind of facial identity verification techniques employed by ID.me.

- The President’s Fiscal Year 2023 Budget: Rep. Thomas Carper (D-DE) asked how long-term funding would help address taxpayer services and overall IRS efficiency. Commissioner Rettig said it is impossible to build robust and meaningful technology infrastructure without consistent, multiyear funding. Making things more difficult, Rettig said, is that the IRS received omnibus funding with only six months left in the year. Sen. Robert Menendez (D-NJ) asked if the current budget request includes funding for implementing scanning technology or 2-D barcodes. Rettig said there is, adding that the IRS has requested funding for 2-D barcodes for several years.

Sen. Bill Cassidy (R-LA) asked if permanent legislation allowing automatic penalty-free withdrawals from qualified retirement plans pursuant to a presidentially-declared disaster is preferable from a tax administration standpoint to passing last minute tax law changes. Rettig supported permanent legislation and explained that IRS requirements to implement unemployment, pandemic recovery and earned income tax credit legislation resulted in additional manual processing of tax returns.

- IRS Staffing Challenges: Chair Wyden asked when the IRS could achieve a reasonable level of phone service. Commissioner Rettig said the president’s budget request included \$389 million to achieve a target level of 85% phone service, which he said is reasonable and can be obtained after the paper filing backlog is reduced. Sens. Tom Carper (D-DE) and James Lankford (R-OK) asked how the IRS would implement its direct hiring authority from the omnibus package. Rettig said Congress “rescued” the IRS with this new authority, which he said will allow the agency to hire 2,200 new employees who could be onboarded within 30–45 days. Sen. Robert Menendez (D-NJ) asked how many employees the IRS is seeking to hire in the near-term. Rettig said the agency expects to hire 5,000 employees before the end of next year, as well as transition several hundred seasonal employees to full-time roles.
- Tax Evasion: Chair Ron Wyden (D-OR) asked if the IRS is producing more up-to-date estimates on the tax gap. Commissioner Rettig said the agency will soon release tax gap information for the 2014–2016 filing seasons, which will include projections for the 2019 gap. He explained the IRS is working with the Department of Justice’s (DOJ) “John Doe” summons tool, which he said has informed the agency of significant noncompliance from reporting in the virtual currency world. Sen. Sheldon Whitehouse (D-RI) asked about the agency’s ability to effectively identify individuals that avoid paying taxes. Rettig stressed the importance of the agency receiving information on bad actors, and he said the beneficial ownership rules are helpful in that regard. Sen. Sheldon Whitehouse (D-RI) asked about the mechanisms that allow 501(c) tax-exempt affiliates to deploy a workaround by registering multiple entities that share a workforce and board of directors. Rettig said while foreign actors may take advantage of this and pump money into the U.S. political system, the agency’s tax exempt team would be able to identify the existence of a money circle. Sen. Elizabeth Warren (D-MA) asked if the IRS currently evaluates non-liquid assets and if it is capable of taxing wealthy individuals that do not pay federal taxes. Rettig said the agency employs the most sophisticated financial examiners on the planet that require meaningful tools and training to support them.

- Cybersecurity: Sen. Mark Warner (D-VA) asked about the level of protection against cyberattacks at the IRS. Rettig said the IRS receives about 2.5 million sophisticated cyberattacks each day and that the agency has been working with DOJ to take down large dark-money sites. Sen. John Thune (R-SD) asked if private information stolen from the IRS and published by the media undermines public trust in the agency. Rettig said any data breach causes significant reputational harm at a minimum, though he said a top priority of the agency is securing the private information it requires from its customers.

Next Steps

Congress will continue debating government funding legislation over the next few months. Lawmakers must enact spending legislation or a continuing resolution by the end of the fiscal year, Sept. 30, or risk a government shutdown.