

**WRITTEN TESTIMONY OF
DANIEL WERFEL
COMMISSIONER
INTERNAL REVENUE SERVICE
BEFORE THE
HOUSE WAYS AND MEANS COMMITTEE
ON THE FILING SEASON AND IRS OPERATIONS
FEBRUARY 15, 2024**

INTRODUCTION

Chairman Smith, Ranking Member Neal and members of the Committee, thank you for the opportunity to discuss the 2024 filing season and IRS operations.

After nearly a year as IRS Commissioner, it remains an honor for me to lead this great institution. My respect for the agency's role and admiration for its workforce continue to grow. I'm pleased to report the 2024 tax filing season opened on schedule on January 29, and is going smoothly so far. Through February 2, the IRS received more than 15.3 million individual income tax returns and issued more than 2.6 million refunds for approximately \$3.65 billion.

Along with delivering the filing season and other day-to-day activities, we have a tremendous amount of transformation work taking place at the IRS. These changes, which are made possible by the Inflation Reduction Act (IRA) funding, touch every part of our operations, from taxpayer service to tax enforcement to information technology and data security.

We have a unique opportunity – a once-in-a-generation chance – to envision and realize a future of tax administration that meets the evolving needs of taxpayers and the nation. Using IRA funding, there are three central themes I've been reminding taxpayers about this filing season:

- Ensuring taxpayers can easily contact the IRS – whether in person, on the phone or online – and get help navigating complex tax laws and accessing the credits they deserve;
- Identifying the growing number of taxpayers with complex returns – including certain wealthy individuals, large corporations and complex partnerships – who are shielding income to evade their tax responsibility and collect from them what is owed; and
- Addressing the growing risk of tax scams and schemes by protecting honest taxpayers from them and rooting out the nefarious actors that perpetrate them.

The IRS has many other goals and objectives supporting this effort as part of our Strategic Operating Plan. This includes making dramatic improvements to our Information Technology (IT) infrastructure and design, and delivering modern

technology platforms that center around data and applications. These efforts will support all our transformation work.

Achieving this ambitious transformation agenda requires us to rebuild areas in the IRS that have suffered from more than a decade of underfunding that preceded the IRA. A critical change we are making involves providing our IRS workforce with the right tools – including training, technology and smarter processes – so we are ready now and in the future to meet our core mission of supporting taxpayers and the nation.

IRA investments are allowing us to strengthen the overall effectiveness of IRS operations to deliver results for taxpayers. The difference between the pandemic-era filing seasons, where the IRS struggled to meet basic taxpayer service needs, and the post-IRA funding is dramatic. For example, last filing season, IRA resources – on top of the IRS discretionary budget – allowed us to meet our goal of an 85% level of service, up from just 15% the prior filing season, and during 2023 we answered more than 18 million calls. We opened or reopened 54 Taxpayer Assistance Centers to provide more in-person help to taxpayers. We have also expanded digital options to save taxpayers time and money, begun work to improve fairness in our enforcement activities, enhanced data security, and completed key milestones of foundational technology changes to retire and replace our outdated legacy systems.

While we have made important progress so far, many more changes are on the horizon. Some changes will be seen in the current filing season – as described in more detail later in this testimony – and others in the months and years ahead. For these improvements to continue and accelerate, however, a consistent, reliable funding stream remains critical for the agency – both in regard to our annual appropriations and maintaining the IRA funding.

The decision about whether to adequately fund the agency comes down to a fundamental choice: Whether or not we will have an IRS that:

- taxpayers can easily interact with to meet their tax responsibilities or resolve issues if they arise,
- ensures fairness in the tax system through its enforcement activities,
- quickly and effectively addresses tax scams that exploit vulnerable populations, and
- has updated IT infrastructure and modern technology platforms capable of supporting our transformation work.

For the IRS to be able to do all these things, adequate annual discretionary funding and complementary long term mandatory funding is essential.

UPDATE ON THE FILING SEASON AND TRANSFORMATION EFFORTS

The IRS remains focused on improving service to taxpayers, offering them more in-person and online resources as part of our effort to deliver another successful tax season this year. Taxpayers and tax professionals will see additional improvements in our operations and service that will make it easier for them to prepare and file taxes.

The IRS has been working hard to ensure this filing season builds on the accomplishments of last year. We have several transformation goals for this filing season, including:

- Again committing to an 85 percent level of service on our main toll-free phone line during the filing season, meaning the vast majority of callers routed to live assistors will connect and get support.
- Committing to an average call wait time of 5 minutes or less on the agency's main taxpayer helpline.
- Giving taxpayers the ability to opt for a call back from the IRS if their wait time on the phone is more than 15 minutes.
- Increasing self-service support in a number of areas, such as the Where's My Refund and Where's My Amended Return tools, which will use conversational voice bot technology for the first time to help taxpayers get answers on the status of their refund or amended return more quickly.
- Providing more in-person help at our Taxpayer Assistance Centers (TAC). The goal is to provide over 8,500 more hours of in-person assistance than we did last filing season. We are expanding hours at nearly 250 TACs around the country during the filing season; again offering special Saturday hours at certain TAC locations; and opening more pop-up centers to reach taxpayers who do not live near a TAC.

These goals are ambitious, but I am confident this IRS workforce is up to the challenge. The progress we made last year using IRA funding shows what is possible in the upcoming filing season and the years ahead.

I'll speak about our efforts to provide world class service, but first I'll turn to enforcement, where we've seen early success in ensuring the wealthiest Americans with ongoing issues pay what they owe.

On the compliance side we continue to take swift and aggressive action to ensure that high-income taxpayers who evade taxes play by the same rules as everyone else. We are increasing scrutiny of these taxpayers as we work to reverse the historically low audit rates for large corporations, complex partnerships, and high-wealth individuals that existed since before the IRA was passed.

As an example, we have concentrated our revenue officers' work on those taxpayers with more than \$1 million in income and more than \$250,000 in

recognized tax debt. Over the past year, the total we have recovered through these new initiatives is \$520 million. **That's half a billion dollars recovered from fewer than 1,000 millionaires and billionaires.** That is just the beginning: Our revenue officers continue to work on hundreds of these cases to recover more back taxes from delinquent high-wealth individuals.

We are also closely examining potential noncompliance among the largest U.S. corporations and partnerships that were identified as higher risk for tax noncompliance with the help of new artificial intelligence tools. As of December, the IRS had open audits of 76 of the largest U.S. partnerships. On average, they each have more than **\$10 billion** in assets and represent a cross-section of industries that include hedge funds, real estate investment partnerships, publicly traded partnerships, large law firms and other industries. IRA funding is also helping us expand our Large Corporate Compliance Program, which covers entities with average assets of more than **\$24 billion** and average taxable income of about \$526 million per year, and our hiring of new staff has allowed us to open 60 new audits of taxpayers in this group.

In all its compliance work, the IRS's focus is on those posing the greatest risk to our nation's tax system in terms of ensuring fairness. As I have previously stated, we remain committed to following the Secretary of the Treasury's directive not to increase audit rates relative to historical levels for small businesses and households earning less than \$400,000 per year. All of this work will be with an eye toward fairness and always respecting taxpayer rights. Although focusing on these types of complex issues will be resource intensive, achieving our goals will result not only in a fairer tax system, but also in benefits for taxpayers and the nation, because detecting and stopping noncompliance in these areas will result in significant additional revenues and reduce the deficit.

Launching the Direct File Pilot

As part of our effort to deliver significantly improved taxpayer services, this filing season, the IRS is conducting a limited-scope pilot of a system that would allow taxpayers to prepare and file a tax return for free, online, directly with the IRS, called Direct File. This year, eligible taxpayers in 12 participating states will have the option to file their return this way. The pilot will allow us to assess customer and technology needs, so we can evaluate and develop solutions and make a recommendation about the future of a Direct File system.

Our work on Direct File is an important innovation in our ongoing efforts to transform the IRS and lead the agency into a digital, taxpayer-focused future.

A core part of the IRS's mission is to meet taxpayers where they are and ensure they have options to fulfill their tax obligations that meet their needs. I want to emphasize that taxpayers will always have choices for how they file their taxes. They can file using a trusted tax professional, our Free File program, tax

software, or free tax preparation services such as the Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs, or they can file a paper return. Taxpayers should use the filing option that works best for them and their personal financial situation. Direct File is designed to be an additional option for some taxpayers this year that is simple, secure, accurate and free.

Progress on Transformation

IRA resources have been fundamental in our efforts to modernize our operations. The IRS is using this funding to upgrade our information technology infrastructure and improve the experience for those who choose to interact with us online. By utilizing technology, we are making the IRS more efficient while meeting taxpayers where they are.

Along those lines, we continue to enhance our online offerings. We have expanded the capabilities of the IRS Online Account and Tax Pro Account so this filing season taxpayers and tax professionals will be able to perform more types of transactions in their accounts. We also launched a Business Tax Account to make interacting with us easier for small business owners as well.

We have also made critical progress on our Paperless Processing Initiative. While online options for taxpayers have increased, the IRS has continued to be flooded with paper, including tax returns and correspondence. We had been working toward digital scanning of paper forms and returns for some time, but the IRA funding has allowed us to greatly accelerate these efforts. For example, during Calendar Year 2023, we scanned more than 1.5 million forms and returns we received on paper.

Additionally, we are making progress toward our five-year goal of giving taxpayers the ability to securely file all documents and respond to all notices online and securely access and download their data and account history. We met our first goal of this initiative three months ahead of schedule. Taxpayers are now able to digitally submit all correspondence and responses to notices.

Complementing these efforts, the IRS last month announced a sweeping initiative to simplify and clarify about 170 million letters sent annually to taxpayers. The Simple Notice Initiative builds on notice-redesign efforts already in place for the 2024 tax season and expands on a recent successful pilot involving identity theft letters. The redesign work will accelerate during the 2025 and 2026 filing seasons, improving common IRS letters going out to individual taxpayers and then expanding into notices going to businesses.

The IRS also made significant progress in bringing our paper inventory back to manageable levels after COVID-related interruptions in our operations resulted in historic backlogs. Inventory challenges involving original returns have been completely resolved.

Taken together, these initiatives will make it easier for taxpayers to respond to notices from the IRS. They have the option to go paperless and conveniently submit necessary responses online, and they will receive clearer and more concise IRS notices, so they can better understand the actions they need to take.

ENHANCING DATA SECURITY

The IRS works continuously to preserve taxpayer privacy and protect our computer systems from cybersecurity incidents through a combination of preventative and detective controls. IRS systems withstand well over 1 billion cyberattacks annually (including denial-of-service attacks, unsuccessful intrusion attempts, probes or scans, and other unauthorized connectivity attempts). Since I became Commissioner, I have seen teams across the IRS make amazing progress to improve our security posture, permanently closing gaps utilizing IRA funding to make needed updates, and we continuously work to ensure that taxpayers and our own systems are protected.

We continue to strengthen our systems, training and overall infrastructure under the Strategic Operating Plan, funded by the IRA. Measures we have taken include (but are not limited to):

- **Further restricting user access.** We restructured our operations to reduce the number of people with access to the most sensitive taxpayer datasets.
- **More robust protective security controls.** We updated data protection mechanisms (e.g., encryption, anonymization) to better protect taxpayer information.
- **Improved firewalls.** We have added additional firewalls between key taxpayer information and the rest of the IRS, providing additional monitoring capabilities.
- **Stronger 24/7 monitoring.** We have expanded advanced analytics to detect and prevent risky data usage, providing improved insight into suspicious activities around the clock.
- **New tools.** We are adding new analytical tools and dashboards to monitor user activity involving sensitive data. These tools will help to improve the detection of potential data misuse.

The bottom line is that as Commissioner I have made it a priority to improve the data security protections at the IRS against internal and external threats. Taxpayer data must always be protected and safeguarded, and any unauthorized disclosure will not be tolerated. We've made remarkable progress and have dramatically reduced risk in all aspects of data security, and we will remain focused on this in the future.

COMBATTING FRAUD: EMPLOYEE RETENTION CREDIT

The IRS is committed to protecting hard-working people and small businesses from scammers and fraudsters who try to use the tax system for their schemes. Along those lines, we continue to face a major challenge related to scams involving the Employee Retention Credit (ERC).

The ERC provided a financial lifeline to millions of businesses and exempt organizations during the pandemic. The IRS has worked hard to implement this credit, and we have processed about 3.6 million ERC claims worth approximately \$230 billion to businesses. However, promoters have been aggressively misleading people and businesses that are not eligible into claiming the ERC, even though they do not qualify.

The IRS has been flooded with ERC claims, and we are concerned that many of these claims are not being filed by businesses that qualify. We appreciate the patience of businesses and tax professionals as we continue our effort to protect against fraud. Since last fall we have been intensifying our compliance work in this area.

To combat this problem, we have taken a number of actions:

- Last September, as we were being inundated by questionable ERC claims, we announced a moratorium on processing new ERC claims to allow us time to make adjustments and add taxpayer protection provisions into the program, including options for businesses that may have been unduly pressed by a promoter.
- In December we sent letters to more than 20,000 businesses notifying them of disallowed claims.
- We are offering a withdrawal option for businesses with a pending ERC claim. This gives them a chance to withdraw their claim if they are concerned it may not be legitimate – for instance, if they were pushed into applying due to false promises by a promoter. This withdrawal option allows certain employers that filed an ERC claim – but have not yet received a refund – the ability to withdraw their submission and avoid future repayment, interest and civil penalties on a refund for which they are ineligible. Claims that are withdrawn will be treated as if they were never filed.
- We have a special ERC Voluntary Disclosure Program running through March 22, 2024, that allows voluntary repayments by businesses that received an improper ERC payment. Those accepted into the program need to repay only 80 percent of the credit they received.

During this period, we have processed some ERC claims, but at a much slower rate than before our approach changed in the summer and fall. While we continue to process ERC applications received prior to the moratorium, our progress is hampered by the fact that all amended returns come in on paper and

require time-sensitive manual processing. We are developing a scanning process for both pre- and post-moratorium paper returns so that we can digitize the information from other pending claims and expect that process to be completed this spring.

This current situation is an excellent example of where IRA funding will make a difference in the future. These claims are all being filed on paper. The IRA funding will give us improved capability to receive digital information, whether on amended returns or other information such as taxpayer correspondence. In turn, this will help us more rapidly identify risks and develop response strategies – the exact issue that we have confronted with the ERC claims.

Additionally, the IRS remains very serious about tracking down unscrupulous promoters of the ERC. We have specially trained auditors examining ERC claims that pose the greatest risk. Also, our Criminal Investigation Division is working to identify fraud and those who promote fraudulent claims, with more than 350 criminal investigations being worked that involve claims worth nearly \$3 billion.

As we have worked through this issue, I want to acknowledge the House Ways and Means Committee's action that would change the deadline for submitting ERC claims. We believe this will be helpful for our tax administration work. We also appreciate the assistance provided by the House Ways and Means Oversight Subcommittee at its hearing on the ERC on July 27, 2023. The discussion and insights at this hearing helped us calibrate the right approach to this problem, and contributed to our decisions on the ERC.

IMPLEMENTING FORM 1099-K CHANGES

Form 1099-K, *Payment Card and Third Party Network Transactions*, first issued more than 10 years ago, is used to report payments from payment apps or online marketplaces and from credit, debit or stored-value cards. Congress passed legislation in 2021 lowering the 1099-K annual reporting threshold. The new threshold is \$600 per year, changed from the previous threshold of more than 200 transactions per year when those transactions exceed an aggregate amount of \$20,000. Reporting requirements do not apply to personal transactions such as giving birthday or holiday gifts, sharing the cost of a car ride or meal, or paying a family member or another for a household bill.

The IRS delayed the effective date for the new threshold in November 2023, for a second time, in response to continuing concerns from taxpayers, tax professionals, and payments processors. The additional time is necessary to help reduce confusion among taxpayers and provide more time for taxpayers to prepare for and understand the new reporting requirements.

It will also allow the IRS to make the necessary updates to the tax forms for 2024 that will make the reporting process easier for taxpayers. For tax year 2024, the

IRS plans for a threshold of \$5,000 as part of a phased-in implementation of the \$600 reporting requirement. As we go forward, we will work closely with third-party groups, tax professionals and others to find the smoothest path to ensure compliance with the law.

CONCLUSION

Chairman Smith, Ranking Member Neal and members of the Committee, thank you again for the opportunity to update you on the filing season and IRS operations. The 2024 filing season is off to a strong start, and, assuming the agency receives adequate funding going forward, the future holds great promise for the agency and the taxpayers we serve. As Commissioner, I remain committed to leading the IRS's transformation efforts in close collaboration with your Committee, and I look forward to working with you to achieve a more modern and high-performing IRS, which will better serve taxpayers and our nation.