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ON THE 2014 FILING SEASON AND IMPROPER PAYMENTS
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I. INTRODUCTION

Chairman Boustany, Ranking Member Lewis and Members of the Subcommittee, thank you for the opportunity to appear before you today to update you on how the 2014 filing season went for the IRS under our current funding levels and to discuss the issue of improper payments with you.

As you know, the IRS is vital to the functioning of government and to keeping our nation and economy strong. We support the nation's tax system by providing taxpayer service to help people understand and meet their tax responsibilities while ensuring enforcement of the tax laws. The agency plays a unique role in government, and resources invested in the agency lead to significant revenue increases for the nation.

Despite the extraordinary efforts of our employees to ensure a smooth filing season, I remain concerned about the very tight budget constraints under which the IRS has been operating since 2010. Our funding for Fiscal Year (FY) 2014 was set at $11.29 billion, which is more than $850 million below our level in FY 2010. Over the same time period, we lost almost 10,000 full-time permanent employees. It is important to note that the IRS continues to operate at near sequestration levels, with the agency's FY 2014 funding less than one percentage point above FY 2013 levels. The solution to the funding problem we face begins with the Administration's FY 2015 budget request, which, with the inclusion of the program integrity cap adjustment and the Opportunity, Growth and Security Initiative, totals $12.64 billion. This is approximately $1.35 billion above the FY 2014 enacted level. This amount includes a $480 million program integrity cap adjustment to vitalize tax compliance and a $165 million additional investment through the Opportunity, Growth and Security Initiative to deliver performance enhancements that taxpayers deserve. In the absence of these additional resources, our ongoing funding shortfall has major, negative implications for taxpayers and the tax system.

In discussing our budget situation, we recognize that there has been a loss of confidence among taxpayers and particularly within Congress in regard to the way we manage operations, particularly the management problems that came to light last year in the section 501(c)(4) area. One of my responsibilities is to ensure that we are minimizing risks and quickly solving management and operational problems that may arise, so that Congress can be confident that, when we request additional funding, the money will be used wisely. Taxpayers provide the funds we receive and they deserve to be confident that we are careful stewards of those resources.

II. IRS PERFORMANCE: FY 2013 AND CURRENT FILING SEASON

Despite the limits on our resources, I remain impressed with the professionalism and commitment of our workforce. Our employees have continued, throughout these challenging times, to perform critical work for the IRS and the nation – helping people understand and meet their tax responsibilities while ensuring enforcement of the tax laws. They are making every effort to ensure a smooth experience for taxpayers despite the funding shortfall.

Filing Season

The IRS delivered another successful tax filing season in 2014, rising to the challenges posed by an incredibly tight budget. Through April 25, 2014, the IRS received more than 134 million individual income tax returns, of which about 87 percent were filed electronically.

As the result of concentrating our resources during the filing season, our level of phone service improved this year during filing season as compared to the average for FY 2013. We have been able to maintain a level of phone service of around 70 percent, meaning that about 70 percent of taxpayers who called this filing season got through to the IRS. One reason may be that the volume of calls to our toll-free lines is actually down somewhat. We believe that is largely because there were no significant tax law changes enacted in 2013. In addition, we continue to provide more resources to taxpayers on our website, which we believe offers an alternative to the phone.

However, with the exit of seasonal employees at the end of filing season, wait times will increase, and we expect that the average level for the entire year will drop below 70 percent and end up closer to last year’s 60.5 percent. This is an unacceptable level of service that especially concerns our employees, who believe taxpayers deserve better. We will continue to monitor telephone service levels and work to maintain as high a level of phone service as possible within our resource limitations.

Another area of concern this year is the amount of time people have had to wait to get in-person help at our Taxpayer Assistance Centers (TACs). We have had reports from field staff of taxpayers lining up outside TACs well before the centers open in the morning to make sure they receive service the same day. We also have had reports of people waiting 90 minutes or more to be helped once they arrived inside the TAC and taken a number for service. Unfortunately, given our resource limitations we have few options to drive down these wait times.

Also, with our current resources, it is taking much longer for us to respond to taxpayer correspondence. Historically, 70 percent of letters we receive have been answered within 30 days, but we expect that more than half of all correspondence this year will take more than 45 days to answer.

In short, as *Forbes* magazine recently noted, a reduction in IRS funding that erodes service levels “punishes” taxpayers.

Taxpayer Service

Providing taxpayers with top-quality service and helping them understand and meet their tax obligations remain top priorities for the IRS. In the past 18 months we have updated forms to help taxpayers comply with filing requirements, converted forms for visually impaired taxpayers, and translated more tax products into multiple languages. In addition, the IRS continued its effort to redesign taxpayer correspondence in plain language and in a consistent format to make it easier for taxpayers to understand their obligations.

The IRS continued to provide alternative service options by increasing the amount of tax information and services available on IRS.gov. During the 2014 filing season just completed, taxpayers viewed IRS.gov web pages more than 270 million times. Thus far in 2014, taxpayers have used the “Where’s My Refund?” online tool about 162 million times. The IRS also deployed a new telephone and web tool last year called “Where’s My Amended Return?” in both English and Spanish that allows taxpayers to check the status of their Form 1040X amended tax returns for the current year and up to three prior years.

This year, we have several new digital applications that expand what taxpayers can do online. An excellent example of these is “Get Transcript”, which is a secure online system that allows taxpayers to view and print a record of their IRS account, also known as a transcript, in a matter of minutes. During the 2014 filing season there were more than 7.8 million downloads of this application which otherwise would have required taxpayer calls or personal appointments to request their transcripts, which we would then have to mail to the taxpayers.

The IRS continues to improve and expand on its outreach and educational services through partnerships with State taxing authorities, volunteer groups, and other organizations. Volunteer Income Tax Assistance (VITA) and Tax Counseling for the Elderly (TCE) sites provide free tax assistance for low-income individuals, the elderly and disabled, and individuals with limited proficiency in

English. This filing season nearly 90,000 volunteers prepared federal returns at over 12,000 sites across the country.

I am pleased to report that the IRS' technology efforts in relation to improving taxpayer service recently received public recognition. In March, the Excellence.gov Awards Program sponsored by the American Council for Technology and the Industry Advisory Council recognized the IRS' Virtual Service Delivery (VSD) program for Excellence in Customer Experience. VSD technology units allow face-to-face contact between IRS employees and taxpayers at remote sites through two-way video conferencing. These units help the IRS resolve taxpayer issues remotely at understaffed and unstaffed Taxpayer Assistance Centers, Taxpayer Advocate Service sites, and Low Income Taxpayer Clinic locations.

Tax Compliance

This fiscal year the IRS' key enforcement programs will operate well below historical levels. We will perform 100,000 fewer individual audits, and individual exam coverage rates will be at an historic low. There will be similar declines in audits of high wealth-individuals, businesses and partnerships along with an estimated 190,000 fewer collection activities. We estimate that the government will lose almost $3 billion in revenues as a result.

The IRS has continued to focus on service and compliance activities in regard to tax return preparers. Return preparers play a key role in increasing taxpayer compliance and strengthening the integrity of the U.S. tax system. The IRS requires anyone who prepares or assists in preparing federal tax returns for compensation to have a valid Preparer Tax Identification Number (PTIN). PTINs allow the IRS to collect more-accurate data on who is preparing returns, the volume and types of returns being prepared and the qualifications of those doing return preparation. Additionally, PTIN data is essential in determining where to direct compliance and educational outreach efforts for erroneously prepared tax returns. The IRS recently held a successful PTIN renewal season, offering enhanced PTIN system usability, troubleshooting tips, and other tools. As of March 2014, the number of valid PTINs totaled approximately 677,000.

The IRS criminal investigation program examines potential criminal violations of the Internal Revenue Code and related financial crimes such as money laundering and tax-related identity theft fraud. Even with declining resources, our Criminal Investigation (CI) division has already this year initiated 2,015 investigations, recommended 1,663 prosecutions and secured 1,590 convictions.

III. IRS EFFORTS TO REDUCE IMPROPER PAYMENTS

Making Progress on Identity Theft

The IRS has a comprehensive and aggressive identity theft strategy that focuses on preventing refund fraud, investigating these crimes and assisting taxpayers victimized by identity thieves.

Refund fraud detection

The IRS stopped 5 million suspicious returns in Calendar Year 2012 – up from 3 million suspicious returns stopped in CY 2011. This upward trend has continued: in CY 2013 we suspended or rejected 5.7 million suspicious returns, worth more than $17.8 billion. This year, through April 17, about 3 million suspicious returns have been stopped.

In 2008, we began placing an indicator on the accounts of taxpayers who had experienced identity theft. These indicators initially served two primary purposes: to speed up account reconciliation for the legitimate taxpayer, and to reduce the likelihood that a taxpayer's information could be used for a fraudulent refund claim in subsequent years.

In 2011, we launched a pilot program to test the Identity Protection Personal Identification Number (IP PIN). The IP PIN is a unique identifier that authenticates a return filer as the legitimate taxpayer at the time the return is filed. The IP PIN is sent to the taxpayer immediately before the filing season for use on the return that will be filed during that filing season and is valid for only one filing season. The growth in the use of the IP PIN has been significant, from 250,000 IP PINs issued in filing season 2012 to more than 1.2 million IP PINs this filing season. Also this year, we offered a limited pilot program to test the idea of issuing IP PINs to individuals who have not previously been identity theft victims, but who reside in locations with high incidences of identity theft. This could prove to be a valuable initiative for next year's filing season.

Over the last two fiscal years the IRS has made numerous improvements in our efforts to protect identifying information as well as catch fraud before refunds are issued:

- We have implemented new identity theft screening filters to improve our ability to spot false returns before we process them and issue refunds. We have also accelerated, to the extent we can under the present law, the use of information returns in order to identify mismatches earlier.

- In cases where dozens or even hundreds of refunds go to a single bank account or single address, we added identity theft filters last year that flag these multiple refund situations for further review. We plan further actions in this area for the next filing season.

- We have implemented a variety of mechanisms to stop the growing use by criminals of deceased individuals' identity information to perpetrate fraud. We routinely lock accounts of deceased taxpayers, and have locked more than 25 million accounts to date. Also, the Bipartisan Budget Act of 2013 included the President's proposal to limit public access to the Death Master File, the intent of which is to help reduce identity-theft related tax fraud.

- We have developed better procedures to use information about identity theft victims received from law enforcement officials who discover this information in the course of investigating identity theft schemes or other criminal activity. We use the data to flag taxpayer accounts and block returns filed by identity thieves.

- Another important part of protecting taxpayers' identities is the IRS' Social Security Number (SSN) Elimination and Reduction program. Under that program, we eliminate or reduce the use of SSNs within our systems, forms, notices and letters where the collection or the use of the SSN is not necessary. To date, we have eliminated or reduced the use of the SSNs on 70 different non-payment notices that we mail to taxpayers. Also, we recently began to deploy SSN masking on eight additional notices with an annual estimated volume of 36 million notices mailed to taxpayers who request installment agreement payments.

- We have developed procedures to better stop the processing of fraudulent returns from prisoners. We have been helped by a number of actions in this area, including the Bipartisan Budget Act of 2013, which includes the President's proposal to give the Treasury Department the legal authority to obtain the Social Security Administration's (SSA) Prisoner Update Processing System (PUPS) data. Additionally, the IRS has collaborated with the Federal Bureau of Prisons, and also with Departments of Correction (DOC) in states that choose to partner with us, to help identify prisoners who may be engaged in tax fraud. Our authority to share return information with prisons, made permanent in the American Taxpayer Relief Act of 2012, helps us as well.

- We are collaborating with software developers, banks, and others to determine how we can better partner with them to address identity theft and prevent federal monies from reaching the hands of identity thieves. For example, we established the External Leads Program for receiving leads from partner financial institutions. In 2013, we had 286 institutions partnering with us, which resulted in 198,000 returned tax refunds in the amount of $574 million. The IRS has also established relationships with representatives of the prepaid access card industry, which has enabled us to leverage their security protocols designed to detect and prevent fraudulent use of prepaid cards. In many cases, these companies can identify potentially fraudulent tax refunds and freeze or cancel the cards.

The IRS' current fraud detection capability is strong but is limited by our current funding levels. There has been some recent attention to our computer systems that we use to combat identity theft. I want to note that we are not ending the Electronic Fraud Detection System (EFDS); it remains in operation and continues to perform well in providing protections to taxpayers and the tax system. Additionally, we also use our Dependent Database (DDb) System to identify identity theft returns. The DDb system is flexible, and we are able to program new filters quickly as we identify new schemes. So far this year, we have stopped more than half a million potential identity theft returns through DDb. Our significantly improved refund fraud system, the Return Review Program (RRP) has had its development delayed due to funding constraints. If fully deployed, the program would allow us to adjust our filters during the filing season as new schemes appear, rather than making such adjustments only at the end of filing season.

Even with the progress we have made in the battle against refund fraud, I have asked our senior leadership team to reevaluate everything we are doing and to consider additional steps we could take to reduce refund fraud. As discussed later, this will require some assistance from the Congress with regard to legislative changes.

Assisting victims

Being victimized by identity theft is a frustrating, complex situation. The IRS has 3,000 people working directly on identity theft related cases – more than double the number in late 2011. And we have trained 40,000 employees who regularly work with taxpayers to help with identity theft situations when they arise.

Critical to the IRS' efforts to assist identity theft victims is our Identity Protection Specialized Unit, which provides taxpayers with a single point of contact at the IRS via a special toll-free telephone line. We also have several identity theft specialized groups to assist with processing identity theft cases.

During FY 2012, the IRS reengineered its identity theft process to close cases more efficiently, accurately, and in a less burdensome manner. In FY 2013, taxpayers who became identity theft victims had their situations resolved in roughly 120 days, far more quickly than in previous years, when cases could take over 300 days to resolve. While this marks a significant improvement, we are continuing to find ways to shorten this time and ease the burden identity theft places on these victims. In CY 2013, the IRS worked with victims to resolve and close approximately 963,000 cases. So far in FY 2014, more than 181,000 cases have been closed and our backlog has been reduced from 260,000 last year at this time to 98,000 now.

Investigating fraud-related crimes

The investigative work done by the IRS is a major component of our efforts to combat tax-related identity theft. CI investigates and detects tax and other financial fraud, including fraud related to identity theft. CI recommends prosecution of refund fraud cases, including cases involving identity theft, to the Department of Justice.

So far in FY 2014, CI has opened more than 500 new investigations into identity theft and refund fraud schemes, bringing the total number of active cases to more than 1,800. In addition, there have been 478 recommendations for prosecution and 342 sentences so far this year, with an average time to be served of more than 40 months. Our intensified activity in the criminal investigation area in relation to identity-theft related refund fraud follows a surge in the number of investigations opened in the last two years – 900 in FY 2012 and 1,500 in FY 2013.

State and local law enforcement agencies also play a critical role in fighting identity theft. CI regularly collaborates with these agencies, and, in March 2013, the IRS announced the nationwide expansion of the Law Enforcement Assistance Program, which began as a pilot program in Florida in 2012. This program provides for the disclosure of federal tax returns and return information associated with the accounts of known and suspected victims of identity theft when the victim provides express written consent for disclosure. To date, more than 5,000 waivers have been provided in 44 states.

Improvements to the ITIN Program

Individual Taxpayer Identification Numbers (ITINs) assist with the filing and collection of taxes from foreign nationals, resident and non-resident aliens, and others who have filing or payment obligations under U.S. law but who do not qualify for SSNs.

ITINs play a critical role in the tax administration process, as they are essential to the processing of tax returns that report tens of billions of dollars in taxable income and billions in tax revenue for individuals who have a U.S. tax filing obligation and otherwise would not have a U.S. taxpayer identification number.

The IRS has taken steps to improve the process of issuing ITINs in order to verify the applicant's identity and foreign status. We will continue to strengthen our efforts in this critical and complex area.

ITIN application process

Under procedures in place since last year, the IRS, with few exceptions, only issues ITINs to taxpayers and dependents who provide original documentation, such as passports and birth certificates, or copies of these documents certified by the issuing agency, to verify their identity.

These procedures also include tighter requirements for becoming a Certifying Acceptance Agent (CAA) and remaining in the CAA program. CAAs play an important role in the ITIN application process as intermediaries who review identity documents of the applicant. Under the tighter requirements, CAAs must certify to the IRS that they have verified the authenticity of the original or issuing agency-certified documents supporting the ITIN application. CAAs are also now required to undergo forensics training, and the IRS has begun compliance reviews of CAAs.

Investigating and detecting ITIN fraud

Reducing refund fraud involving the misuse of ITINs, in which individuals use ITINs to file returns claiming tax credits to which they are not entitled, continues to be a priority for the IRS, and we have made important progress in this area. Our CI division has increased investigative time spent on ITIN investigations by approximately 400 percent since 2008. Between 2008 and April 15, 2014, CI identified approximately 2,725 ITIN schemes that encompassed more than 323,000 ITIN returns. Several fraud detection filters are in place specifically to help detect issues with the Child Tax Credit (CTC) and Additional Child Tax Credit (ACTC).

Notably, last year the IRS detected specific patterns indicating potential fraud in returns with ITINs and was able to develop filters on a real-time basis during the filing season to stop these refunds from being issued. In addition, we have developed new methods of clustering suspicious returns together to catch large numbers of returns that appear similar. These clusters include identifying multiple returns using the same address or the same filing and refund patterns.

Strengthening Tax Compliance in Regard to Refundable Credits

Refundable tax credits play an important role in fulfilling Congressional policies, but they are inherently subject to a number of tax administration challenges. There are numerous refundable credits currently administered by the IRS, including the Earned Income Tax Credit (EITC), the CTC and the American Opportunity Tax Credit (AOTC). The IRS has a dual mission when it comes to administering refundable credits. We must balance the mandate to get refunds out as quickly as possible to those who qualify with the need to ensure that the money goes only to individuals who are eligible to receive it.

There are a number of factors that present challenges to our compliance efforts as they relate to refundable credits. They include the following:

- *Complexity*. Complexity in the rules governing eligibility for and the operation of certain refundable credits creates challenges for both taxpayers and the IRS. Mistakes in the application of the law cause a significant portion of claims that are made in error.
- *Lack of Third-Party Data*. In many cases, the IRS lacks real-time third-party data sources that could be used to verify taxpayers' eligibility. In many cases, definitive third-party data verifying eligibility does not exist. Even if data exists, the IRS is often in the position of having to process returns and determine the validity of a refund before receiving the third party data that could be matched against the return to verify data. For example, Form 1098-T, which helps the IRS verify the eligibility for the AOTC, is not due to be filed with the IRS until after most refunds claiming the credit are processed.
- *Cash Payments*. Refundable credits allow for payments beyond income tax liability. This makes refundable credits particularly enticing targets for certain types of fraud.

Given these challenges, the IRS has dedicated significant attention and resources to improving tax compliance in regard to claims made for refundable credits in order to reduce improper payments associated with these credits. One of the biggest enforcement priorities for us in this area is the EITC.

Enforcing EITC rules

Congress created the EITC as part of the Tax Reduction Act of 1975, to offset Social Security taxes. The credit has evolved into an important program that now lifts millions of children and families above the poverty line each year.

To qualify to claim the EITC, individuals generally must: have earned income; have a valid SSN for themselves and for each qualifying child they claim; meet certain filing status and income limits; have investment income of no more than a certain amount ($3,300 for 2013); and be a U.S. citizen or resident alien for the entire year for which the credit is claimed.

The amount of the EITC that an individual may claim varies based on whether the individual has any qualifying children, and if so, the number of qualifying children that the individual is able to claim. For a child to be considered a qualifying child, the following tests must be met:

- *Age:* The child must be under age 19 at the end of the year (under age 24 in the case of a student) and younger than the taxpayer (or younger than both the taxpayer and the taxpayer's spouse if filing a joint return), or the child must be permanently and totally disabled at any time during the year for which the EITC is claimed;

- *Residency:* The child must have lived with the taxpayer for more than half of the year for which the credit is being claimed, although certain exceptions to this rule apply; and
- *Relationship*: The child must be the taxpayer's son, daughter, stepchild, eligible foster child, brother, sister, stepbrother, stepsister or a descendant of any of these individuals, such as a grandchild, niece or nephew. Adopted children also qualify, including those lawfully placed with the taxpayer for legal adoption.

In addition, a taxpayer claiming the credit cannot be the qualifying child of another taxpayer, and cannot use the "married filing separately" filing status. Additional requirements apply for individuals who do not have qualifying children. Given the complex nature of the rules governing eligibility, the IRS engages in significant education and outreach efforts so that taxpayers are aware of their potential eligibility for the credit.

The IRS' EITC-focused enforcement programs currently protect approximately $4 billion annually. The following programs contribute to the broader strategy of identifying improper EITC refund claims as early in the process as possible:

- *Math error*. This refers to an automated process in which the IRS has been granted statutory authority to identify certain math or other irregularities on the return and automatically adjust the return for a taxpayer.
- *Document matching*. This process involves comparing income information provided by the taxpayer with matching information from third-party returns, such as Form W-2 and Form 1099, to identify discrepancies. The IRS conducted almost 1 million of these reviews in FY 2013, in addition to 500,000 audits.
- *Examinations*. The IRS identifies tax returns and amended returns for examination and in most cases holds the EITC portion of the refund until an audit can be completed. Of the approximately 500,000 EITC audits conducted by the IRS each year, 70 percent are conducted before the EITC portion of the refund is paid. The tax returns to be examined are selected using an effective risk-based audit selection model, resulting in a change rate of more than 90 percent. Examinations protected almost $2.1 billion against improper EITC refund claims each year.
- *Soft notices*. The IRS uses soft notices as a low-cost alternative to audits. They help educate taxpayers on their compliance responsibilities and are an inexpensive way of recovering payments. In FY 2013, the IRS sent more than 110,000 letters to alert taxpayers that an exemption or qualifying child for the EITC claimed on their returns had also been claimed by another person.

- *Two- and 10-year bans*. Under section 32(k), the IRS is authorized to ban taxpayers from claiming the EITC for two years if it determines during an audit that they claimed the credit improperly due to reckless or intentional disregard of the rules. The IRS can impose a 10-year ban in cases of fraud. When a ban is imposed, taxpayers are provided their full appeal rights. Last year there were more than 67,000 two-year bans and 45 10-year bans in effect.

The IRS continues working to improve and expand its existing compliance efforts to stop improper EITC payments. Notably, our increased efforts in regard to identity theft-related fraud detection have helped improve EITC enforcement results.

In spite of these accomplishments, it is important to note the significant degree of difficulty in enforcing compliance with the EITC, which derives in large part from its eligibility requirements. EITC eligibility depends on items that the IRS cannot readily verify through third-party information reporting, including marital status and the relationship and residency of children. In addition, the eligible population for the EITC shifts by approximately one third each year, making it difficult for the IRS to use prior-year data to assist in validating compliance.

Given this situation, and given that approximately 57 percent of the returns claiming the EITC are prepared by tax return preparers, we believe that one of the keys to driving increased EITC compliance continues to be strategic programs addressed to the return preparer community, such as our return preparer initiative referenced above. Other examples of our preparer-related activities include: compliance and warning notices sent before and during the filing season to preparers who preparer large numbers of EITC returns to educate them on their responsibilities and the consequences of noncompliance; preparer audits done by field examiners to make sure preparers are complying with EITC due diligence rules; and “knock-and-talk” visits to preparers by CI agents and auditors, to educate them on EITC laws.

Additionally, the IRS has expanded its traditional treatment of EITC preparers to test a new early-intervention component. Over the previous two years the IRS has used data analytics - including an innovative approach - to significantly reduce improper payments associated with the EITC as well as the CTC.

Using this approach, a small data-driven pilot in 2012 identified a group of tax return preparers with a history of submitting incorrect or potentially fraudulent tax returns falsely claiming the EITC, then designed and implemented interventions with these preparers to stop improper claims. The interventions included letters, calls and site visits to selected preparers, both before and during tax filing season to allow preparers to immediately adjust their practices. These efforts reduced improper EITC payments in 2012 by an estimated $198 million for returns prepared by preparers who received the interventions.

An expanded preparer pilot in 2013 protected an additional $590 million in revenue from being paid out improperly. The 2013 pilot program included a broader set of randomly selected preparers and a broader set of interventions, including the addition of preparer-focused taxpayer audits (for returns that otherwise would have qualified for audit even absent the pilot). Many preparers whose error rates did not improve as a result of interventions during the 2012 pilot did so in 2013 after being subject to additional intervention. Preparers who had improved due to IRS interventions during the initial 2012 pilot generally maintained their improved behavior with respect to EITC and related tax credits claimed on returns and claims filed during 2013. Use of interventions for preparers before and during the filing season continued on an expanded basis in 2014.

Despite all of the efforts described above, we continue to be concerned that the improper payment rate for the EITC has remained too high throughout the program's history. (For FY 2013, the EITC improper payment rate was between 22 and 26 percent.) Therefore, we recently initiated a major review of our activities in this area. As part of this review we are assessing our many past and current efforts, and are exploring new possibilities, such as options for simplifying EITC eligibility requirements and finding more-efficient ways to distinguish valid claims from excessive claims. We also think the legislative proposals presented next will play a critical role in our effort to lower the improper payment rate.

Administration's Green Book Proposals

Congress can help us further enhance our efforts to reduce improper payments, particularly those involving the EITC, by approving the program integrity cap adjustment referenced above and a number of legislative proposals contained in the President's FY 2015 Budget, including the following:

- ***Correctible error authority***. As noted above, the IRS has limited statutory authority, known as "math error authority," to identify certain computation or other irregularities on returns and automatically adjust the return for a taxpayer. These upfront systemic processing checks protect approximately $320 million in improper EITC payments annually. At various times, Congress has expanded this limited authority on a case-by-case basis to cover specific newly enacted tax code amendments. The Administration's proposal would replace the existing specific grants of this authority with more general authority covering computational errors and incorrect use of IRS tables. Further, the proposal would expand IRS' authority by creating a new category of "correctible errors," allowing the IRS to fix errors in several specific situations, such as when a taxpayer's information does not match the data in government databases. Without correctible error authority, any obvious errors in a return can only be fixed after an audit, which requires far more resources than we presently have.

- ***Acceleration of information return filing dates***. Under current law, most information returns, including Forms 1099 and 1098, must be filed with the IRS by February 28 of the year following the year for which the information is being reported, while Form W-2 must be filed with the SSA by the last day of February. The due date for filing information returns with the IRS or SSA is generally extended until March 31 if the returns are filed electronically. The Administration's proposal would require information returns to be filed with the IRS (or SSA, in the case of Form W-2) by January 31, except that Form 1099-B would have to be filed with the IRS by February 15. The proposal would also eliminate the extended due date for electronically filed returns. In addition, it would rationalize income tax return dates so that taxpayers would receive Schedule K-1 before the due date for filing their tax returns.

- ***Authority to regulate return preparers.*** In light of recent court decisions striking down the IRS' authority to regulate unenrolled and unlicensed paid tax return preparers, the Administration's proposal would explicitly authorize the IRS to regulate all paid preparers. In explaining the reason for this proposal, the Treasury Department noted that the regulation of all paid preparers, in conjunction with diligent enforcement, will help promote high quality services from tax return preparers, improve voluntary compliance, and foster taxpayer confidence in the fairness of the tax system. Treasury also noted the harms caused by incompetent and dishonest preparers to the tax system, including increased collection costs, reduced revenues, the burden placed on taxpayers by the submission of incorrect returns on their behalf, and a reduction in taxpayers' confidence in the integrity of the tax system.

- ***Preparer penalty***. Under current law, the penalty imposed on preparers for understatement of tax on a federal return due to an unreasonable position taken on the return is the greater of $1,000 or 50 percent of the income derived by the preparer from preparation of the return. A separate penalty can be imposed if the understatement is due to the preparer's willful or reckless conduct. That penalty is the greater of $5,000 or 50 percent of the income derived by the preparer from preparation of the return. The Administration's proposal would increase the penalty in cases of willful or reckless misconduct to the greater of $5,000 or 75 percent of the income derived by the preparer (instead of 50 percent). Treasury has said this proposal is necessary because in many cases, 50 percent of income derived by the preparer is far greater than the fixed dollar penalties imposed, so that, under the present penalty regime, preparers who engaged in reckless or willful conduct would end up paying the same dollar penalty as preparers whose conduct did not rise to that level.

- ***Due diligence***. Return preparers who prepare tax returns on which the EITC is claimed must meet certain due diligence requirements to ensure their clients are in fact eligible to receive this credit. In addition to asking questions designed to determine eligibility, the preparer must complete a due diligence checklist (Form 8867) for each client, and file the checklist with the client's return. The Administration's proposal would extend the due diligence requirements to all federal income tax returns claiming the CTC and the ACTC. The existing checklist would be modified to take into account differences between the EITC and CTC.

There are a number of other legislative proposals in the Administration's FY 2015 Budget request that would also assist the IRS in its efforts to combat identity theft. They include the following: Giving Treasury and the IRS authority to require or permit employers to mask a portion of an employee's SSN on W-2s, an additional tool that would make it more difficult for identity thieves to steal SSNs; adding tax-related offenses to the list of crimes in the Aggravated Identity Theft Statute, which would subject criminals convicted of tax-related identity theft crimes to longer sentences than those that apply under current law; and adding a $5,000 civil penalty to the Internal Revenue Code for tax-related identity theft cases, to provide an additional enforcement tool that could be used in conjunction with criminal prosecutions.

V. CONCLUSION

Chairman Boustany, Ranking Member Lewis and members of the Subcommittee, thank you again for the opportunity to update you on the 2014 filing season and discuss our efforts to reduce improper payments. To improve our ability to increase enforcement of the tax code, it is vital that we find a solution to our budget problem, so that the IRS can be on a path to a more stable and predictable level of funding. I look forward to working with Congress and this Committee to do just that. This concludes my statement, and I would be happy to take your questions.