

**WRITTEN TESTIMONY OF
DANIEL WERFEL
COMMISSIONER
INTERNAL REVENUE SERVICE
BEFORE THE
HOUSE WAYS AND MEANS COMMITTEE
ON THE FILING SEASON AND THE IRS BUDGET
APRIL 27, 2023**

INTRODUCTION

Chairman Smith, Ranking Member Neal and members of the Committee, thank you for the opportunity to discuss the 2023 filing season and the IRS budget.

I am honored to serve as the 50th IRS Commissioner and have the chance to lead a group of extremely dedicated and talented public servants at a pivotal moment in IRS history. My first few weeks as Commissioner have reinforced my belief in the importance of the IRS to the nation, as I have witnessed the ongoing efforts of our workforce to fulfill the critical mission of administering the nation's tax system. This includes administering the tax filing season, which has gone smoothly in terms of processing tax returns, the operation of our information technology systems and improvements in taxpayer service.

As I begin my new role, I have a unique opportunity coming into the agency to bring a fresh perspective on our operations, examining them to determine where improvements can be made and what processes and controls need to be strengthened to better fulfill our mission. Ensuring a high-performing IRS is critical for our nation, as the agency collects more than \$4 trillion in revenues each year, generating about 96 percent of the funding that supports the federal government's operations – everything from roads and other infrastructure to education and the nation's military.

We greatly appreciate the funding provided by Congress in the Inflation Reduction Act of 2022 (IRA), which has already allowed us to make improvements in many areas, including our levels of service on the phones and in person during the 2023 filing season. In tandem with the IRS' annual discretionary budget, this critical, sustained multi-year funding will allow the agency to transform its operations— through improved taxpayer service, smarter enforcement, upgraded technology, and better data security.

As we continue implementing the IRA, we welcome Congressional oversight of our efforts. I believe in the oversight role of this Committee and others, and I will always strive to be accountable to you for the investments we make using the IRA funding. Accountability will be essential for the IRS to maintain public trust.

We must be transparent about our work, be responsible stewards of the taxpayer dollars we receive, and collaborate with Congress and other oversight entities. A good example of how we are striving for better transparency is the IRA Strategic Operating Plan we issued earlier this month. This plan lays out our objectives, initiatives and milestones for transformation of the agency, and will be described in more detail later in this testimony. In all of our efforts, our ultimate goals are to provide all taxpayers with world-class customer service and implement the tax code in a way that safeguards the rights of taxpayers and promotes tax fairness.

UPDATE ON THE 2023 FILING SEASON

I am pleased to report the 2023 tax filing season, which began on time on January 23, has gone well. Through April 14, the IRS received more than 117 million individual federal tax returns and issued more than 75 million refunds totaling more than \$215 billion. It is important to note that, although we are now past the April 18 filing deadline, the work of the filing season continues, as IRS employees continue to process tax returns, including amended returns and returns for which taxpayers have requested an extension through mid-October.

This filing season, following the infusion of IRA funding, the IRS has been able to provide taxpayers with a substantially better experience than they have seen for several years. Notably, we have answered more calls from taxpayers seeking our help than in 2022, and we have significantly reduced their wait time on the phones, provided more in-person assistance at our Taxpayer Assistance Centers (TACs) around the country, and provided more online services for taxpayers who prefer using this service channel.

Examples of the improvements seen this filing season include:

- **Phone service.** We hired more than 5,000 additional customer service representatives (CSR) for our toll-free lines. That allowed us to achieve a level of service (LOS) on the phones averaging 85.4 percent this filing season through April 14. This is a significant increase from approximately 16 percent for the same period last year. Our CSRs have answered over 2 million more calls this filing season compared to this time last year during filing season. The IRA resources also have allowed us to reduce the average time it takes to answer a taxpayer call to about three minutes, compared with 28 minutes a year ago.
- **In-person assistance.** We have already hired hundreds of new employees for our TACs, with more to come. So far this year through April 14, TACs have provided face-to-face service to more than 523,000 taxpayers, compared with 399,000 during the same period last year. IRA funding has also allowed us to reopen many TACs that were closed due to lack of resources. As of early April, 334 of our 362 TACs are open, with 28 closed or unstaffed. That compares with August 2022, when we had 317

TACs open out of a total of 359, with 42 closed or unstaffed. Additionally, again this year, we have had special Saturday openings of certain TACs in dozens of locations across the country to assist taxpayers.

- **Electronically filed forms.** We launched an online portal, the Information Returns Intake System (IRIS) for businesses to electronically file 1099-series forms, saving time and effort for both businesses that issue these forms and the taxpayers that receive them. Though available to businesses of all sizes, IRIS is especially helpful to small businesses that currently submit their 1099 forms on paper.
- **Scanned returns.** We began a new initiative called Digital Intake to scan paper tax returns to save time and effort for taxpayers and businesses, as well as for the IRS. We have scanned more than 474,000 paper Forms 940, *Employer's Annual Federal Unemployment Tax (FUTA) Return*, since the start of 2023. In March, we expanded this effort to include scanning of Form 1040, *U.S Individual Income Tax Return*, and Form 941, *Employer's Quarterly Federal Tax Return*. We hope to scan more than a million forms this year, a major accomplishment for the agency.
- **Easier response to IRS notices.** We gave taxpayers the option to respond to a range of IRS notices by uploading documents electronically using our Document Upload Tool. At the current stage of this ongoing effort, we estimate this can help serve more than 500,000 taxpayers each year who respond to these notices, which include military personnel serving in combat areas and recipients of important tax credits such as the Earned Income Tax Credit.
- **Faster refunds on amended returns.** This filing season, for the first time, taxpayers who electronically filed Form 1040-X to amend their tax returns had the option to choose direct deposit for their refund – which can save weeks over delivery of a paper refund check. This helps a significant segment of taxpayers, as a total of 3 million amended returns are filed each year.

TRANSFORMING THE IRS: IRA STRATEGIC OPERATING PLAN

The IRA legislation provides the IRS with a unique opportunity to transform our agency and the taxpayer experience over the next decade. To ensure we are on the right path in implementing the IRA, we recently issued our Strategic Operating Plan, which provides a long-term vision for how we will use these historic investments to better serve taxpayers. This robust plan provides the roadmap for the IRS to enhance the taxpayer experience, improve fairness in tax administration by reducing the tax gap, and strengthen our operations to be more efficient.

By implementing the plan, the IRS will provide the American public the customer experience they deserve, modernize outdated technology and tools for taxpayers, and deliver more effective enforcement of tax laws that apply to high-income taxpayers, large corporations, and complex partnerships which do not

pay the taxes they legally owe. This plan, which IRS and Treasury staff started working on in advance of my confirmation as IRS Commissioner, lays out a solid foundation for transforming the IRS. This vision is achievable with the long-term funding provided by the Inflation Reduction Act and assuming the IRS receives sufficient discretionary funding each year through the annual appropriations process.

Taken as a whole, the plan provides a vision for the future of the IRS as an organization that will deliver:

- A world-class customer service operation where taxpayers can engage with the IRS in a fully digital manner if they choose, where helpful tools for taxpayers to navigate the complexity of our tax laws are deployed and then refreshed and updated regularly based on taxpayer feedback, and where our customer service workforce is maintained at the right size and with the right resources and training to always be ready to meet the taxpayer demand for assistance.
- New capacities, including specialized skills, to unpack the complex filings of high-income taxpayers, large corporations, and partnerships so Americans have confidence that all taxpayers, regardless of means, are doing their part to meet their responsibilities under our tax laws.
- Modern technology that provides taxpayers with increased confidence that data is secure and that we are prepared and able to more rapidly meet new requirements or responsibilities as they emerge in the future.

The plan is organized around five objectives:

- Dramatically improve services to help taxpayers meet their obligations and receive the tax incentives for which they are eligible.
- Quickly resolve taxpayer issues when they arise.
- Focus expanded enforcement on taxpayers with complex tax filings and high-dollar noncompliance to address the tax gap.
- Deliver cutting-edge technology, data, and analytics to operate more effectively.
- Attract, retain, and empower a highly skilled, diverse workforce and develop a culture that is better equipped to deliver results for taxpayers.

The IRS that emerges from this plan will deliver an improved taxpayer experience that mirrors what best-in-class public and private organizations now provide. Among the improvements, taxpayers and tax professionals will have the ability to interact with the IRS in the way they prefer, whether online, over the phone, or in person. This approach will also help the IRS reach more underserved communities, providing the assistance to taxpayers in the ways that they want and deserve.

Along with improving the taxpayer experience, another component of the plan involves enforcement to ensure fairness in tax administration and address the tax gap. This focus will not be a concern to compliant taxpayers; the emphasis will

be on pursuing those who do not follow the tax law. In conducting these enforcement activities, we are committed to following the Treasury Department's directive not to increase audit rates relative to historical levels for small businesses and households earning \$400,000 per year or less.

To be clear, we have years of work ahead of us where we will be 100% focused on building capacity for higher income individuals, large corporations and complex partnerships. During this time, the audit rate for average, hard-working taxpayers will not be increasing, and these rates are at historical lows. People who get W-2 forms or receive most of their income from Social Security or have a small business should not be worrying about some new wave of IRS audits. Instead, our focus will be on other high-dollar areas for quite some time, because there is a lot of work to do in those more complex areas of tax law that will take a number of years to accomplish.

Instead, our compliance efforts will focus on complex issues and high-dollar noncompliance. This is important, because over the past several years, our ability to enforce the tax laws against non-compliant taxpayers with complex returns – including large corporations, complex partnerships, and high-wealth individuals – has been hampered by a lack of resources. We have been unable to audit a reasonable percentage of these groups, and we are often limited in the issues reviewed among those we do audit. Many of these taxpayers can afford to spend large amounts to drag out proceedings unnecessarily or bury the government in paper, leaving us unable to assure a reasonable degree of compliance with the laws passed by Congress.

Funding provided under the IRA will allow us to hire and train more specialists across a wide range of complex areas needed to assist with the audits of the complex issues we will be focusing on. For example, we will focus the IRA enforcement resources on hiring the accountants, attorneys, engineers, economists, and data scientists needed to pursue high-income and high-wealth individuals, complex partnerships, and large corporations that are not paying the taxes they owe. Using improved data and analytics, we will enhance detection of noncompliance and increase enforcement activities for such high-risk and novel emerging issues as digital assets, listed transactions, and certain international tax issues. All of this will be done with an eye toward fairness and always respecting taxpayer rights.

It is important to note that our plan to focus on these types of complex issues will be resource intensive. But 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 would result in significant additional revenues and reduce the deficit.

This plan is only the beginning of our work. As we stand up the IRS Transformation and Strategy Office and begin specific implementation sequencing and planning efforts, we will provide additional information to the

Treasury, to our oversight bodies, and to the American people outlining the details of our transformation.

We will hold ourselves accountable to achieving the plan's vision by regularly monitoring and reporting to Congress on our progress. We will also update the plan's details as we learn more about what works and as the operating environment changes. More important than any detail in this plan, however, is our responsibility to improve the customer experience we provide to the American people. The IRS looks forward to demonstrating how the actions under this plan will translate into real improvements in how taxpayers engage with us and in the assistance we provide. The plan articulates how, through both service and technology enhancements, the experience of the future will look and feel much different from the IRS of today.

I also want to note that the IRS will continue looking for feedback from Congress, from people inside and outside the tax community, including taxpayers, as we work to put these changes in place. This feedback is important to make sure that we strengthen IRS operations and transform the agency to serve taxpayers and the nation.

THE PRESIDENT'S FISCAL YEAR (FY) 2024 BUDGET

The President's FY 2024 Budget proposal for the IRS provides \$14.1 billion in discretionary appropriations, an increase of \$1.8 billion, or about 15 percent, above the 2023 enacted level of \$12.3 billion. This request provides funding to maintain basic IRS service, operations and technology functions, which, when paired with IRA funding, will ultimately lead to increased voluntary tax compliance. The request also aims to ensure the IRS stays current with paper inventory and can provide both live phone assistance and in-person service; facilitates optimal oversight of high-income, large corporate and large partnership tax returns; and maintains digital tools to enable efficient and cleaner communication with taxpayers.

As noted above, the historic funding provided by Congress under the IRA will allow us to transform tax administration and taxpayer service in ways not possible under the annual budget alone. Years of underfunding left the IRS understaffed and unable to deliver the modern customer service experience taxpayers deserve, and also left the agency with challenges operating on outdated information technology systems and unable to keep up with a changing economy. But the transformative investments to be made using IRA funding can only be put to work if Congress continues annual funding for steady-state maintenance of agency operations.

The IRS's plan for IRA implementation assumes that IRA funds will support transformation efforts, while day-to-day operations would continue to be supported by annual appropriations. Any reduction in annual discretionary funds – including failing to sufficiently provide for inflationary increases to maintain

current levels – would require IRA funding to be shifted to general operations. This would mean worse service for the taxpayer.

The President's FY 2024 Budget requests total program increases of approximately \$1 billion, including the following:

- **Improving the Taxpayer Experience:** \$41.4 million. This investment will allow the IRS to continue helping taxpayers and tax practitioners meet their tax obligations. Funding will be used to maintain and expand the number of digital assistance options taxpayers may use to access resources for complying with the tax laws. Additional online self-service options to be funded include account updates, secure messaging and notice delivery, and refund tracking.
- **Green Tax Credit Implementation:** \$105.6 million, which will be used to support the various IRA tax credit provisions. This funding will supplement IRA funding for this area to develop and modify forms, instructions and notifications; conduct taxpayer education and research; address increased taxpayer demand for assistance with the new credits; and ensure compliance with tax credit requirements.
- **Improving Phone Level of Service (LOS)/Reducing Paper Inventory:** \$267.2 million. This investment will enable the IRS to achieve and maintain high LOS performance outcomes and exceed FY 2023 levels. This is important, given that taxpayer research continues to indicate phone service is a preferred service channel. Research also shows that inadequate phone service causes taxpayers to increase usage of other service channels, such as paper correspondence, so keeping phone LOS high will reduce incoming paper inventory.
- **Restoration of Staffing Levels:** \$167.6 million. This investment will restore discretionary funding for the IRS staffing levels in place prior to enactment of the IRA. While the IRA provided the IRS with significant resources for a transformative expansion of its tax enforcement related to large and complex tax returns as well as increasing taxpayer services efforts, there remains a need for a reversal of the multi-year inflation-adjusted decline in the IRS's foundational staffing resources.
- **Sustaining IT Capabilities:** \$55.9 million. The IRS intends to use funds provided under the American Rescue Plan Act and the IRA to accelerate the modernization of its core foundational technology. But it must continue to operate the existing core tax processing system while planning and executing the modernization initiatives. This funding will allow the IRS to fund operations and maintenance of these key existing systems.
- **Business Systems Modernization:** \$289.6 million. This investment will restore discretionary IT modernization funding to help the IRS continue to develop into a 21st century tax administrator. Although the IRA provides funding for business systems modernization, sustained annual discretionary funding is necessary for the envisioned transformative modernization to be realized and sustained going forward.

LEGISLATIVE PROPOSALS IN THE PRESIDENT'S FY 2024 BUDGET

Along with the funding requested in the President's FY 2024 Budget request, we are also requesting legislative proposals that would improve tax administration, including the following:

- ***Direct Hire Authority and Streamlined Critical Pay.*** The President's Budget includes two administrative provisions within the appropriations language designed to expand Direct Hire Authority (DHA) and provide the ability to offer Streamlined Critical Pay (SCP) to certain new hires to accelerate IRS hiring efforts. DHA provides the ability to expedite the normal hiring process to hire more efficiently when there is a severe shortage of highly qualified candidates or during a critical hiring need. DHA has helped the IRS address the backlog of paper returns and other issues. Expanded DHA will help ensure hiring delays are not an obstacle to implementing plans for utilizing IRA resources and achieving broad mission-related functions. SCP authority gives the IRS a management tool to quickly recruit and retain a limited number of employees with high levels of expertise in technical or professional fields that are crucial to the success of the IRS's transformative efforts.
- ***Information reporting by financial institutions and digital asset brokers for purposes of exchange of information.*** Over time, the U.S. has established a broad network of information exchange relationships with other jurisdictions based on established international standards. The information obtained through those relationships has been central to recent successful IRS enforcement efforts against offshore tax evasion. The ability to exchange information reciprocally is particularly important in connection with the implementation of the Foreign Account Tax Compliance Act (FATCA). Currently, however, the U.S. provides less information to foreign governments than we receive from them. The proposal would expand reporting by financial institutions and digital asset brokers in a number of ways – for example, by requiring financial institutions to report the account balance for all financial accounts maintained at a U.S. office and held by foreign persons. These new reporting requirements would enable the IRS to provide equivalent levels of information to cooperative foreign governments in appropriate circumstances to support their efforts to address tax evasion by their residents. The proposal would be effective for returns required to be filed after December 31, 2025.
- ***Require reporting by certain taxpayers on foreign digital asset accounts.*** Section 6038D(b) of the Internal Revenue Code contains an annual reporting requirement for individuals in regard to two categories of foreign financial assets, but there is no reporting requirement under this section for digital assets. Against this backdrop, tax compliance and enforcement with respect to digital assets is a rapidly growing problem.

The global nature of the digital assets market offers opportunities for U.S. taxpayers to conceal assets and taxable income by using offshore digital asset exchanges and wallet providers. The proposal would amend section 6038D(b) to require reporting with respect to a new third category of asset: that is, any account that holds digital assets maintained by a foreign digital asset exchange or other foreign digital asset service provider. Reporting would be required *only* for taxpayers that hold an aggregate value of all three categories of assets in excess of \$50,000. The proposal would be effective for returns required to be filed after December 31, 2023.

- ***Extend the statute of limitations for certain tax assessments.*** Section 6501 of the Internal Revenue Code generally requires the IRS to assess a tax within three years after the filing of a return. But for complex audits in the largest cases, critical issues may not be identified until late in the process of an examination, and in many cases these issues cannot be pursued further due to time and resource constraints. The proposal would amend section 6501 to extend the three-year statute of limitations to six years if a taxpayer omits from gross income more than \$100 million on a return. This change would give the IRS enhanced agility and flexibility in evaluating and staffing its case inventory and appropriately allocating its limited enforcement resources.
- ***Increase oversight of paid tax return preparers.*** Paid tax return preparers have an important role in tax administration because they assist taxpayers in complying with their obligations under the tax laws. The proposal would amend Title 31, U.S. Code (Money and Finance) to provide the Secretary with explicit authority to regulate all paid preparers of Federal tax returns, including by establishing mandatory minimum competency standards. The proposal would be effective on the date of enactment.
- ***Expand and increase penalties for return preparation and e-filing.*** Inappropriate behavior by paid tax return preparers harms taxpayers through the filing of inaccurate returns, erroneous refunds and credits and personal tax return noncompliance. Tax return preparer misconduct continues, in part, because the amounts of the penalties under current law do not adequately promote voluntary compliance. The proposal would increase the amount of the tax penalties that apply to paid tax return preparers for willful, reckless or unreasonable understatements, as well as for forms of noncompliance that do not involve an understatement of tax.
- ***Expand authority to require electronic filing for forms and returns.*** Under this proposal, electronic filing would be required for returns filed by taxpayers reporting larger amounts or that are complex business entities, including: (1) income tax returns of individuals with gross income of \$400,000 or more; (2) income, estate, or gift tax returns of all related individuals, estates, and trusts with assets or gross income of \$400,000 or more in any of the three preceding years; (3) partnership returns for partnerships with assets or any item of income of more than \$10 million in any of the three preceding years; (4) partnership returns for partnerships

with more than 10 partners; (5) returns of real estate investment trusts, real estate mortgage investment conduits, regulated investment companies and all insurance companies; and (6) corporate returns for corporations with \$10 million or more in assets or more than 10 shareholders. Further, electronic filing would be required for the following forms: (1) Forms 8918, *Material Advisor Disclosure Statement*; (2) Forms 8886, *Reportable Transaction Disclosure Statement*; (3) Forms 1042, *Annual Withholding Tax Return for U.S. Source Income of Foreign Persons*; (4) Forms 8038-CP, *Return for Credit Payments to Issuers of Qualified Bonds*; and (5) Forms 8300, *Report of Cash Payments Over \$10,000 Received in a Trade or Business*. Return preparers that expect to prepare more than 10 corporation income tax returns or partnership returns would be required to file such returns electronically. The Secretary would also be authorized to determine which additional returns, statements, and other documents must be filed in electronic form in order to ensure the efficient administration of the internal revenue laws without regard to the number of returns that a person files during a year.

- ***Improve reporting for payments subject to backup withholding.*** The proposal would treat all information returns subject to backup withholding similarly. Specifically, the IRS would be permitted to require payees of any reportable payments to furnish their Taxpayer Identification Numbers (TIN) to payors under penalty of perjury. The proposal would be effective for payments made after December 31, 2023.

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. This has been a strong filing season for the IRS, and the future holds great promise for the agency and the taxpayers we serve. As Commissioner, I am committed to leading the IRS's transformation efforts in close collaboration with this 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.