




TAX TIME 2016

HELP IS *NOT* ON THE WAY

By Phyllis Horn Epstein



“The 2015 filing season was akin to A Tale of Two Cities. For the majority of taxpayers who filed their returns and did not require Internal Revenue Service assistance, the filing season was generally successful. For the segment of taxpayers who required help from the IRS, the filing season was by far the worst in memory.”

— Nina E. Olson,
National Taxpayer Advocate

This year, as preparations are underway for the filing of annual income tax returns, congressional budget cuts to the Internal Revenue Service will be undermining the service that many take for granted.

In words that still resonate, IRS Commissioner John Koskinen testified before the U.S. Senate Finance Committee after his confirmation for the 2014 filing season: “I don’t know any organization in my 20 years of experience in the private sector that has said, ‘I think I’ll take my revenue operation and starve it for funds to see how it does.’ The IRS will have 11,000 fewer people working during this upcoming filing season while processing the largest number of returns in its history. I don’t care how efficient you become, that is not a recipe for success or improved compliance and taxpayer service.”



UNITED STATES

Internal Revenue Service Building

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The Cuts

Congress has consistently cut the IRS budget for each of the past five years, in part by the 2013 sequestration and in part by the move to reduce all federal discretionary spending. Since 2010, funding has been reduced by 18 percent adjusted for inflation from a budget of \$13.4 billion to \$10.9 billion in 2015. As a result the IRS operates with 13,000 fewer employees (a 14 percent decrease) and 10,000 fewer enforcement staff (a 20 percent decrease).

The trend continues for 2016. In a last-minute December compromise between the president and Congress, the fiscal year 2016 budget for the IRS was set at \$11.2 billion — a mere \$290 million increase over 2015. With an expected additional \$250 million in mandated costs, the IRS in 2016 will experience its lowest funding levels since 2008.

Six former IRS commissioners wrote to Congress on Nov. 9, 2015, protesting the cuts. The commissioners represent a bipartisan list from the administrations of Kennedy, Johnson, Reagan, Bush I, Bush II and Clinton. They wrote: “It is clear to each of us that the [reductions] over the last five years materially and adversely affect the ability of the IRS to assist taxpayers who are trying to comply with their tax obligations, as well as the ability of the IRS to detect and deter taxpayers who have not complied with their tax obligations.”

The IRS Is a Service Organization

While feared or dreaded by many, the IRS is a public-service organization, and when its funding is starved those services are impacted. Basic services provided by the IRS include the processing of all tax returns and information reporting, the issuance of re-

funds and the processing of deposits, collection operations, offers in compromise and installment agreements, issuance of responses to requests for technical advice and letter rulings, and responses to telephone calls and the mail.

For calendar year 2015, the IRS received approximately 100 million telephone calls, 160 million individual and business tax returns, 10 million pieces of correspondence and more than 5 million taxpayer walk-ins to IRS service centers. All of these services that taxpayers have come to rely upon are at risk.

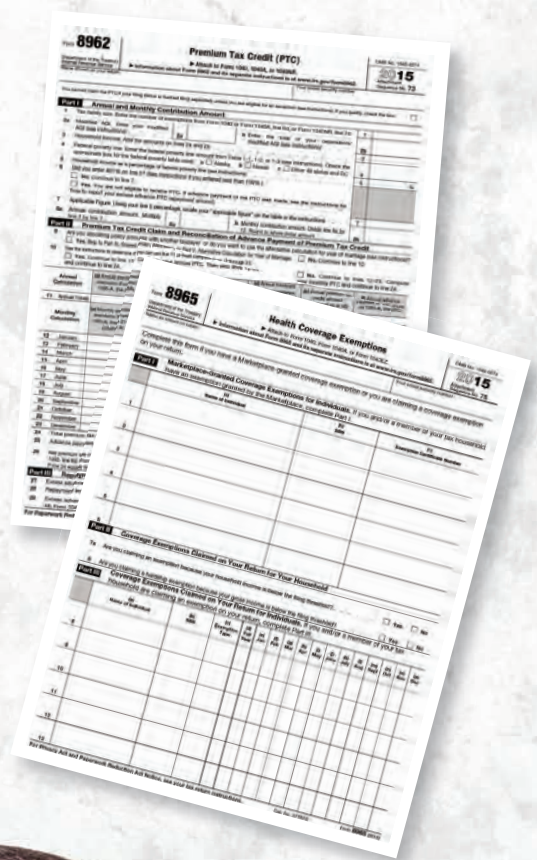
New Responsibilities

In spite of the significant funding cuts over the past five years, IRS responsibilities have increased. With the enactment of the Patient Protection and Affordable Care Act, the IRS must administer two new tax changes, the Premium Tax Credit (PTC) and the Individual Shared Responsibility Payment (ISRP). Both require technology upgrades and the issuance of guidance to taxpayers and enforcement agents. In 2015, 2.6 million returns were filed with new Form 8962 claiming the PTC; 6.6 million returns reported the ISRP; and 107 million returns were filed with Form 8965 claiming an exemption from health-coverage requirements.

The Foreign Account Tax Compliance Act (FATCA) requiring foreign financial institutions to report account information for U.S. taxpayers has created an additional tax-administration burden on the IRS, with more than 160,000 foreign financial institutions registering under FATCA and providing information to the IRS.

The explosion of taxpayer ID fraud has created enormous new burdens and responsibilities. There were 7 million more

individual tax returns filed this past year than in 2010, an increase of 5 percent, and a more than 700 percent increase in ID theft cases. In calendar years 2013 and 2014, there were a reported 730,000 cases involving ID theft. In comparison, IRS filters stopped 4.8 million tax returns between Jan. 1 and Nov. 30, 2015, for suspicion of fraud for refund claims — more than twice as many as the previous year. Also in 2015, the IRS received 1.6 million telephone calls during the filing season to the Identity Protection Specialized Unit hotline, where the level of service was around 25 percent. At one point the level of service was as low as 10 percent for three consecutive weeks. Each reported case of ID theft takes an average of six months to resolve.





Who Is Harmed?

In short, budget cutbacks cripple the IRS, diminish revenue collection and translate directly to reduced service to taxpayers. For individuals seeking help with filing or with relief from collection efforts the cuts have resulted in a serious decline in service.

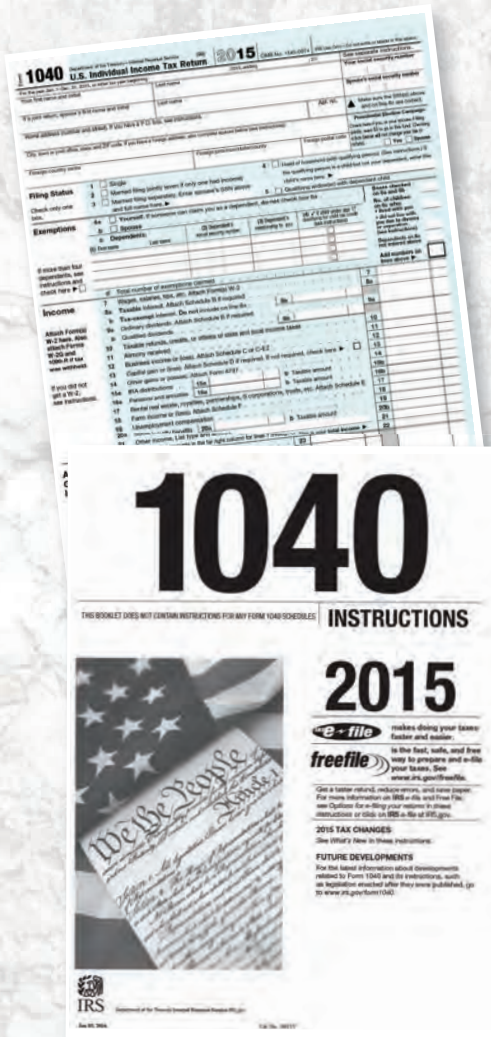
How Are Taxpayers Harmed?

Calls not answered. In 2015, 62 million of the approximately 100 million telephone calls made to the IRS were unanswered. (Stated another way, only 38 percent of calls to IRS customer service were answered.) In comparison, 87 percent of all calls to the IRS made in 2004 were answered. The average hold time for answered calls to the IRS in 2015 was more than 30 minutes, compared to 2.5 minutes in 2004. In 2015, 8.8 million taxpayers experienced a “courtesy call disconnect” compared to 544,000 taxpayers in 2014. A courtesy disconnect occurs when the IRS hangs up on the caller because of long wait times. In 2015, the IRS answered only 17 percent of calls from taxpayers who were notified that their returns were blocked by the taxpayer protection program on suspicion of ID theft.

Mail answered late. The three primary reasons taxpayers write to the IRS are to request penalty abatement, make balance-due inquiries and for miscellaneous account inquiries. According to Nina E. Olson, the IRS’s National Taxpayer Advocate, “taxpayers have a right to expect that their government will take their telephone calls and answer their letters.” But this is increasingly not the case. Only half of all correspondence to the IRS in fiscal year 2014 was answered on a timely basis, that is, within 45 days.

Local offices closed. As a result of staff cuts, the IRS has reduced paper tax-return processing sites from eight to three since 2003. Starting in 2014, the IRS no longer offers tax-preparation services at walk-in offices, services often relied upon by those with lower incomes, the disabled and the elderly. In 2004, 400 IRS sites offered such services.

Questions unanswered. Complex tax questions will no longer be handled personally but will be referred to online resources such as those found at IRS.gov. The IRS will only answer “basic” tax questions this year during the filing season and none outside of filing season. This will directly impact taxpayers who seek filing extensions. The e-help Desk service was reduced this past year “due to budget restrictions” so that extended weekday hours and Saturday and Presidents Day service would no longer be available. Refund inquiries are being redirected to automated services, and all responses are delayed until 21 days after a return is filed electronically or until six weeks later if filed by paper. Refund inquiries received in the first 21





days after a return is filed electronically will be redirected to the Where's My Refund? page under the Refunds tab on the IRS.gov website and an automated telephone line. New EIN (Employer Identification Number) requests will be referred to EIN online assistance rather than to a live IRS representative.

Declining help to resolve IRS collections.

Taxpayers are well aware that if they have a delinquent assessment with the IRS, steps will be taken to levy against their property. To work with the IRS on a payment plan requires the engagement of IRS personnel. One method of resolving an outstanding tax obligation is through the offer-in-compromise process wherein the IRS is asked to resolve a liability for a lesser amount. Offer-in-compromise staffing dropped by 9 percent between 2001 and 2014 while offer filings increased by 62 percent. As a result there has been a decline in the number of offers in compromise accepted, while others are placed in currently non-collectible status due to a lack of resolution.

A useful tool for resolving an outstanding liability is the IRS transcript, which is a record of what has been reported, assessed and paid. In 2014, the IRS introduced a new method for taxpayers to obtain their own IRS transcripts by using their Social Security numbers. In the hands of a criminal, a transcript is also a road map for identity theft. Unfortunately, because the system relied upon single-factor authentication, a result was rampant fraud, and the system was shut down in 2015.

Another procedural remedy for taxpayers is the appeals process. Although mandated by the Internal Revenue Service Restructuring and Reform Act of 1998, 12 states do not have an appeals office presence. These areas are serviced by circuit-riding personnel, the number of whom has declined by as much as 27 percent in recent years. It is estimated that relief in the appeals process can take an additional six months to resolve where there is a circuit appeals officer. This can also mean that appeals officers are no longer local and are unavailable for face-to-face meetings to resolve issues.

While feared or dreaded by many, the IRS is a public-service organization, and when its funding is starved those services are impacted.



In spite of significant cuts over the past five years, IRS responsibilities have increased.

The IRS continues to evaluate which services to provide on a diminishing budget. The budget reductions will mean reduced personal service by telephone and mail or at taxpayer service centers for the indefinite future and a shift to more online rather than personal service. Visits to the IRS.gov website increased from 296 million in fiscal year 2009 to 437 million in fiscal year 2014. But the reality is that not everyone is computer-literate. A 2013 Pew Research Center survey of adults online found that significant populations were not online: 44 percent of adults older than age 65; 41 percent of adults with less than a high-school education; 22 percent of adults with a high-school education; and 24 percent of households with less than \$30,000 in annual income. According to the Taxpayer Advocate Service (TAS), the IRS “should not impose a digital strategy on taxpayers that erodes taxpayers’ trust for the IRS’s own convenience.” And according to the IRS’s Olson, “it is wishful thinking, if not foolhardy, to expect taxpayers to rely on computer-driven systems for resolution of tax problems that, if not resolved fully, could lead to devastating financial consequences.”

Results

The National Society of Accountants, in an open letter to the chairs and ranking members of the Appropriations Committees of the U.S. Senate and House of Representatives, expressed their concern this way: “If you truly believe, as you state, that ‘We need the IRS to enforce tax laws, stop and prevent fraud, prepare forms and instructions, process refunds, collect revenue and assist taxpayers in complying with tax obligations,’ then the first step would be to develop a budget for the IRS that would actually provide the agency the means with which to do so.”

In addition to the loss of service personnel and enforcement staff, the cuts have also meant that the IRS has seen its budget for training agents drop from \$172 million in 2010 to \$22 million in 2015. The TAS has expressed concern that these cuts will cause “inappropriate adjustments and assessments” by auditors and “inappropriate levies [and] liens” by collection agents.

Conclusion

Why does this matter? This is a lose-lose situation for individuals and for our system of taxation, which is dependent upon voluntary compliance. Ninety-eight percent of tax revenue is derived from taxpayers who voluntarily file returns and pay their taxes without the necessity of any enforcement action by the IRS. The bedrock of voluntary compliance is a belief in the fairness of the system and a trust in how that system is operated.

Budget cuts and the resulting loss of service place the entire voluntary-compliance system at risk. And for the country this makes little sense. We know that for fiscal year 2015 the IRS collected \$300 for each \$1 in appropriated funds. To starve the insti-

tution that is responsible for collecting funds to run the government is hardly a strong business model, let alone a model for efficient government. The Treasury Inspector General for Tax Administration concluded in fiscal year 2014 that IRS revenue officers collected \$222 million (7 percent) less than in fiscal year 2011. IRS Commissioner Koskinen predicts a loss of nearly \$2 billion in revenue as a result of the IRS budget cuts. The TAS predicts that if voluntary compliance dropped by 10 percent, tax revenues would decline by more than \$280 billion.

As a result of the latest budget cuts, the country is experiencing the lowest individual and business audit levels in the past 10 years. Before celebrating, taxpayers should be aware that the decline in service can have a serious negative impact on their ability to deal with the IRS when they have an issue of collections or a question about reporting. A taxpayer has a strong interest in being able to contact the IRS by telephone or by mail to ask a question before preparing a tax return that has an erroneous item or to track down a missing payment. If the IRS disagrees with the taxpayer's reported position on a return, it will issue an assessment of tax, interest and penalties. Interest and penalties can often amount to more than the initial tax. It is also in the interest of the taxpayer to resolve an assessment before collection enforcement begins. In the view of the TAS, those who can afford to pay for assistance may fare better than others who cannot afford to have tax professionals negotiate the system for them.

Taxpayers who think they can get away with not filing are cautioned that the IRS has the authority to collect information from income-reporting entities such as banks, brokerage firms, employers, casinos or other places and to prepare a return for

the taxpayer from which they can make an assessment and pursue collection activities. Collection activities may be onerous, including liens on residential property, levies against Social Security checks and bank accounts, and criminal prosecution if warranted.

To quote from the TAS's 2014 annual report to Congress: "We do not think it is acceptable for the government to tell millions of taxpayers who seek help each year, in essence, 'We're sorry. You're on your own.'" And yet this is where we are and where we are heading as we brace for the 2016 filing season. The tax system has not only become more complex, it has become more remote and unresponsive when it can least afford to do so. ☞

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Phyllis Horn Epstein is a partner with the Philadelphia law firm of Epstein, Shapiro & Epstein PC, with more than 30 years' experience in taxation, corporate transactions, and trusts and estates. She represents clients before the IRS and the Pennsylvania Department of Revenue and in the U.S. Tax Court and the Orphans' Courts of Pennsylvania. She is a fellow of the American College of Tax Counsel and a recipient of a PBA Special Achievement Award for her three years of service as treasurer of the PBA.

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