

# Practice

## Two Cheers for Tax Enforcement

By Robert S. Horwitz\*

**O**n February 13, Charles P. Rettig was nominated by President Trump to serve as the Commissioner of Internal Revenue. In his 35+ years as a private tax practitioner, Chuck has often dedicated himself to improving the fairness of our nation's tax system and encouraging taxpayers to comply with their filing and reporting obligations. If confirmed, he will be taking over as head of the agency at a critical time in its history, when after almost a decade of budget cuts it is now tasked with implementing the largest overhaul of the Internal Revenue Code ("the Code") in over 30 years.

Senator Orrin Hatch has been at the forefront of Congressional critics of the IRS. As chair of the Senate Finance Committee, he has been instrumental in setting the IRS' budget. But in his February 14 opening statement at the Committee's hearing on the proposed FY 2019 IRS budget, he began to push for increased agency funding:

No one here needs to remind me about IRS missteps, regardless of which president or commissioner has been at the helm.

But, personally, I think it's high-time that Congress reexamines its approach to the agency.

Because IRS will bear the brunt of the burden in implementing and administering the tax code and the new tax provisions, it needs sufficient personnel and resources to carry out its important mission at this critical juncture.

Let's keep in mind that the IRS is the only agency in the government that touches every single American every single year. And that's why I've pushed for such robust oversight over the years. It is also why the IRS should get the resources it needs to do its job right.

For example, the IRS is still using computer software that is older than most of my committee staff. And, you can take a look at them—they're not all millennials.



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The agency is shedding staff and resources. Agency reductions might be a good thing in some cases, but it should be done through thoughtful reforms, not the blunt axe of blind budget cuts.

The administration, in its budget, has proposed additional cuts to funding for the IRS. I think that is a mistake. While I've had quite a bit to say over the years about the allocation of resources at the IRS, now, directly after passage of a major overhaul of the tax system, is not a great time to further reduce the taxpayer services budget of the agency that will do most of the work in implementing the updated tax code.

Acting IRS Commissioner David Kautter recently testified before the Senate Finance Committee that the agency needs \$397 million in additional funds to properly implement the Tax Cut and Jobs Act: "This funding is needed immediately to ensure that the IRS can start critical implementation activities on time." As a result of the new law, the IRS must reprogram some 140 return processing systems and create or revise 450 tax forms, at the same time as it attempts to provide some meaningful degree of taxpayer assistance and educational outreach. Mr. Kautter also stated that 59 percent of the agencies hardware is beyond its useful life and one-third of the software was two or more releases behind the latest commercially available programs.

*Does the proposed fiscal 2019 budget provide the increased funding? Let's take a look.*

House Ways and Means Committee Chairman Kevin Brady agreed that lawmakers should consider increasing the IRS budget "Now, we have a new tax code, a new acting commissioner." But he is less willing than Senator Hatch to admit that the IRS needs more funds. "It's not automatic. It needs to be proven."

Does the proposed fiscal 2019 budget provide the increased funding? The proposed budget seeks funding for the IRS in four areas: Taxpayer Services, Enforcement, Operations Support and Business Systems Modernization. Let's look at each component of the budget and how the proposed budget compares with those for fiscal 2017 and 2018.

## Taxpayer Services

Taxpayer Services include pre-filing assistance and education, filing and account services, and other services to help taxpayer's understand their obligations, correctly file their returns and pay their taxes when due. These services are provided in person, by phone and by Internet. During 2017, there were more than 490 visits to the IRS website, *www.IRS.gov*. Taxpayer Services also include taxpayer advocacy services. After an increase in fiscal 2018, the fiscal 2019 budget proposes cutting funding and employees for Taxpayer Services below the 2017 level (*see* Table 1):

TABLE 1.

	FY 2017 (actual)	FY 2018 (est.)	FY 2019 (est.)
Funding	\$2.484 billion	\$2.533 billion	\$2.345 billion
Employees	28,694	27,804	24,668

## Enforcement

Enforcement is the area many readers know best: collection, examination and criminal investigation. This portion of the proposed budget provides funds for the IRS to determine and collect taxes, to conduct criminal investigations, to provide legal and litigation support and to enforce criminal laws related to violations of the internal revenue laws and other financial crimes (think Bank Secrecy Act violations). It also provides funds for IRS appeals, for regulations and technical rulings, for monitoring pension and profit-sharing plans, and for determining the qualifications for organizations seeking tax-exempt status. It also provides funds "to purchase and hire passenger motor vehicles" and other services authorized by statute. Funding and employment for enforcement will increase from fiscal 2018 (*see* Table 2):

TABLE 2.

	FY 2017 (actual)	FY 2018 (est.)	FY 2019 (est.)
Funding	\$4.730 billion	\$4.656 billion	\$4.864 billion
Employees	36,552	34,662	36,158

If you look closely, the increase in funding for Enforcement (\$208 million) is almost the same as the decrease for Taxpayer Services (\$188 million). The increase in employment for Enforcement (almost 1,500) does not offset the decline in employment for Taxpayer Services (over 3,100). So in the critical areas of Taxpayer Services and Enforcement, under the proposed fiscal 2019 budget

overall funding will remain about the same while employment will decrease.

## Operations Support

Operations Support is IRS logistics. It provides the funds for “rent payments; facilities services; printing; postage; physical security; headquarters and other IRS-wide administration activities; research and statistics of income; telecommunications; information technology development, enhancement operations, maintenance and security; the hire of passenger motor vehicles (31 USC 1343(b)); the operations of the Internal Revenue Service Oversight Board” and other services authorized by statute. This portion of the IRS budget will see an increase of almost 15 percent over the 2017 budget (see Table 3):

	FY 2017 (actual)	FY 2018 (est.)	FY 2019 (est.)
Funding	\$4.150 billion	\$4.396 billion	\$4.754 billion
Employees	10,869	10,813	11,154

## Business Systems Modernization

Business Systems Modernization is the part of the proposed IRS budget that pays for planning and capital asset acquisition needed to modernize the IRS’s administrative systems. This is the smallest component of the IRS budget. The fiscal 2019 budget proposes a cut from prior years (see Table 4):

	FY 2017 (actual)	FY 2018 (est.)	FY 2019 (est.)
Funding	\$315 million	\$278 million	\$258 million
Employees	28,694	27,804	24,668

Overall, the budget request will increase slightly over the proposed IRS fiscal 2018 budget, with the increase coming in Operations Support. If the IRS can make the case that it needs additional funds to implement the new tax law, Congress may appropriate more than the proposed budget requests, increasing the IRS budget to fulfill its mandate.

## Additional Budget Proposals

There are several additional proposals in the budget related to the IRS. In 2011, the IRS issued regulations requiring

paid return preparers to pass an initial certification exam, pay a fee and take continuing education. The regulation was invalidated in *S. Loving*.<sup>1</sup> The budget proposal includes authorizing the IRS to regulate paid return preparers since “ensuring that these preparers understand the tax code would help taxpayers get higher quality service and prevent unscrupulous tax preparers from exploiting the system and vulnerable taxpayers.” Previous budgets contained similar proposals that Congress refused to enact. President Trump’s proposed fiscal 2018 budget contains a similar proposal. Whether Congress will enact legislation providing the IRS oversight authority this time remains to be seen.

*Budget cuts also reduce the IRS ability to issue regulations and rulings, conduct audits, investigate criminal violations of the internal revenue laws, and collect past due liabilities.*

In her 2013 Annual Report to Congress, the National Taxpayer Advocate listed some of the ways in which budget cuts hurt taxpayers by reducing taxpayer services and IRS employee training. Budget cuts also reduce the IRS ability to issue regulations and rulings, conduct audits, investigate criminal violations of the internal revenue laws, and collect past due liabilities. One of the reasons Congress required the IRS to outsource collections to private collection agencies was the IRS’s lack of resources. If Congress increases IRS funding it may be able to fulfill its core mission of collecting tax owed to the United States.

The proposed fiscal 2019 budget also contains a proposal that will increase the IRS’s authority to correct errors to include cases where (1) the information provided by the taxpayer does not match information the IRS has in its databases; (2) the taxpayer has exceeded the lifetime limit for claiming a particular credit or deduction; or (3) the taxpayer has failed to include with the return required documentation. According to the budget proposal, this “would keep refunds from being issued to taxpayers who are not eligible” and “allow the IRS to resolve simple issues quickly without having to direct enforcement resources away from more difficult cases.” The proposed fiscal 2017 budget contained a similar proposal. National Taxpayer Advocate Nina Olson has criticized the proposals concerning database matching and incomplete documentation in her blog.<sup>2</sup>

The third proposal would require a return to have a valid social security number in order to claim the child tax credit and the earned income tax credit. This is being proposed to “ensure that only individuals authorized to work in the United States could claim these credits.”

The latter two proposals would primarily impact law and moderate-income taxpayers. If they are enacted, Congress should include provisions that ensure that affected taxpayers are provided adequate notice and a meaningful opportunity to challenge the IRS action.

In 2017, the IRS processed more than 246 million tax returns and forms, collected more than \$3.4 trillion in revenues and issued over \$430 billion in refunds. The proposed budget for fiscal 2019 estimates that increased funding of the IRS of \$15 billion over the next 10 years will result in approximately \$44 billion in increased collection, for a net increase of \$29 billion.

Shortchanging the agency that collects more than 90 percent of federal revenues is ultimately a losing financial proposition. Taxpayer Services and Enforcement have each suffered significantly as a result of budget cuts. Congress may finally be waking up to the fact that adequately funding the IRS is a sensible proposition. Adequate funding and efficient management of resources can help ensure that the IRS provides an appropriate measure of taxpayer services balanced with the fair and equitable enforcement of this country’s tax laws.

#### ENDNOTES

- \* The author is also a former Chair of the Taxation Section of the State Bar of California.
- <sup>1</sup> *S. Loving*, CA-DC, 2014-1 USTC ¶50,175, 742 F3d 1013.
- <sup>2</sup> See <https://taxpayeradvocate.irs.gov/news/correctible-error-authority-part-2-why-correctible-error-authority-creates-more-problems-than-it-resolves>.

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