

**Statement of
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“Uncollected Taxes: Can We Reduce the \$300 Billion Tax Gap?”

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**Senate Homeland Security and Governmental Affairs
Subcommittee on Federal Financial Management,
Government Information, and International Security**

Chairman Coburn, Ranking Member Carper, and members of the Subcommittee, my name is Colleen Kelley and I am the National President of the National Treasury Employees Union (NTEU). As you know, NTEU represents 150,000 federal employees in 30 federal agencies and departments, including the men and women who work at the Internal Revenue Service. I appreciate you giving me the opportunity today to present NTEU's recommendations with regard to the tax gap and tax compliance.

My message today is simple: the IRS needs more federal employees on the frontlines of tax compliance and enforcement to help it close the \$350 billion tax gap. Rather than move forward with its plans to drastically cut customer service in order to expand its enforcement role, the IRS needs to strike a balance between offering adequate opportunities for taxpayers to voluntarily comply and enforcing the tax code. NTEU agrees with GAO's recent tax gap report (GAO-05-753) that a more regular compliance assessment is needed if the IRS wishes to obtain a clearer picture of the extent of the tax gap. But I would emphasize that the IRS must determine those factors which encourage and enable taxpayers to voluntarily comply as well as determine reasons for noncompliance.

The IRS also ought to use its trained workforce to collect all delinquent taxes when voluntary compliance fails. These are two areas where the IRS can achieve greater compliance and enforcement by utilizing the knowledgeable and skilled workers currently employed by the IRS. But if Congress is serious about closing the tax gap, then more frontline employees are needed in order to achieve this goal.

Budget Cuts

While NTEU agrees with IRS' goal of enhancing tax compliance and enforcement, we don't agree with the approach of eliminating front-line customer service employees in order to pay for additional compliance efforts. As the number of tax returns continues to grow, the number of IRS employees continues to shrink. As the Oversight Board pointed out in its 2003 Annual Report, IRS workload has increased by 16 percent while at the same time the number of full time equivalent employees has decreased by 16 percent from 1999 to 2002. This is caused by a number of circumstances, including an increasingly complex tax code and an increasing number of tax returns—paper as well as electronic returns. This has led to a serious decline in the size of the IRS workforce as a way to cope with increasing budgetary demands. Combined Collection and Examination function enforcement staff declined from 25,000 at the beginning of FY 1996 to 16,000 at the end of FY 2003, a 36 percent decline.

In its FY 2006 IRS Budget/Special Report, the IRS Oversight Board stated that it "agrees that investing in enforcement does pay for itself many times over, not only in increased revenues but by reinforcing the belief that all taxpayers are paying their fair share."

Also, the IRS should look at the management to bargaining unit employee ratio to find much needed resources for additional collection work. Although the number of frontline employees who do the work at the IRS has decreased by 5.1 percent since 2000, the number of managers who supervise these employees has *increased* by 1 percent over this same period. If the IRS decreased the number of managers and management officials at the same rate as it has decreased its rank and file employees, the Agency could put the savings toward bolstering Collections work.

As Congress considers ways to address the growing federal deficit, I urge you to avoid any across-the-board cuts to the IRS budget. The IRS is a revenue-generating federal agency. Any across-the-board funding cuts will hamstring the Agency from fulfilling its tax enforcement mission. IRS needs more resources if it is expected to seriously address noncompliance and the tax gap. By providing the IRS' full funding request, the IRS can ensure that other federal programs will have the necessary resources to keep the federal safety nets strong and solvent in times of crises.

Customer Service

Congress must continue to reject IRS' plans to implement draconian cuts to customer service. Customer service is one half of the compliance equation. The IRS' plan to close six call sites and 67 Taxpayer Assistance Centers (TACs) across the country is counterproductive to the mission of the IRS. This plan will exacerbate—not shrink—the tax gap. IRS Taxpayer Assistance Centers are taxpayers' frontline source for personal, face-to-face tax help. Taxpayers who have complex issues, need to resolve a tax problem, or are more comfortable talking with someone in person can visit a local Taxpayer Assistance Center. IRS representatives in these offices can help with inquiries or adjustments to tax accounts, payment plans for those who owe tax and cannot pay the full amount, questions about IRS letters and notices, and levies on wages or bank accounts.

Seniors, who rely on face-to-face contact more than younger taxpayers, will be forced to travel farther distances in order to get the tax assistance they need if the IRS follows through with its cuts to customer service. This also means that minorities and low-income taxpayers, who rely on the Centers to help with language barriers, the earned-income tax credit and general tax preparation, will also see the tax services they rely on cut.

As Janet Spragens, law professor and director of American University College of Law's Federal Tax Clinic, notes in her testimony before the IRS Oversight Board (February 1, 2005):

“...these taxpayers, many of whom have limited or no proficiency in English, are generally not part of the information age. They are not Internet connected...They tend to be helped better through local walk-in offices and opportunities for face-to-face meetings than with an organizational structure

based on specialization of function, remote offices, mailed documents, telephone trees with automated selections and electronic transfers.”

Earlier this year, the Treasury Inspector General for Tax Administration Russell George stated before the Senate Transportation, Treasury, HUD Appropriations Subcommittee (April 7, 2005), “TIGTA believes this information is insufficient to draw conclusions on the capability and likelihood that taxpayers who have used these centers in the past will be willing to use alternative methods of seeking help, such as the internet or telephone. I strongly recommend that the IRS further research these issues before closing TACs.”

The 2004 IRS Oversight Board Tax Compliance Study found that “the most heavily relied upon source of tax information and advice are IRS representatives” (82 percent see them as very/somewhat valuable). The study further shows that more than 90 percent of those surveyed said that IRS customer service is either very or somewhat important to them.

The statements from these reliable sources point to one conclusion: maintain customer service options for taxpayers. Both chambers of Congress have also come to the same conclusion with the language passed in H.R. 3058, the Transportation, Treasury, Housing and Urban Development, the Judiciary, the District of Columbia, and Independent Agencies Appropriations Act, 2006 which temporarily prevents cuts to customer service. Customer service is a critical part of the compliance equation and the IRS must not be allowed to slash customer service this year, or next year, for the sake of bolstering enforcement.

Private Tax Collection

NTEU strongly opposes the Administration’s plan to privatize IRS debt collection, as authorized by Congress last year in H.R. 4520, the American Jobs Creation Act of 2004. Under the statute, the IRS would be permitted to hire private sector debt collectors and pay them a bounty of up to 25 percent of the money they collect. NTEU opposes this short-sighted proposal, anticipates its complete failure as witnessed in a similar 1996 pilot program and will continue to work towards its repeal.

Last year, the House signaled its bipartisan disapproval of privatizing tax collections by passing legislation that would prevent the program from being authorized; however, under pressure from the administration, the language was removed in conference committee.

Representatives Rob Simmons (R-CT) and Chris Van Hollen (D-MD) introduced H.R. 1621, The Taxpayer Protection Act of 2005. The legislation would repeal the IRS’ recently enacted authority to hire private debt collectors to collect tax debt. The bill currently has sixty-five bipartisan cosponsors. The Taxpayer Protection Act would undo a serious mistake and NTEU strongly supports this legislation.

Proposals to allow private collection agencies to collect taxes on a commission basis have been around for a long time. As far back as 1986, the Reagan administration opposed the concept of privatizing tax collections. The Treasury Department warned then of considerable adverse public reaction to such a plan, and emphasized the importance of not compromising the integrity of the tax system, which is a longstanding inherently governmental function. President Reagan's Administration said this about such a proposal:

“The Department strongly opposes contracting out the collection of taxes because it is likely to result in considerable adverse public reaction. The public must be assured at all times that the person collecting taxes derives no personal benefits from that activity and that the integrity of the tax system will not be compromised.” (Treasury Department Statement to the House Judiciary Committee, August 8, 1986).

The IRS' proposal would risk the loss of confidentiality of millions of taxpayers' private information, would provide incentives for the use of abusive tactics by private debt collectors, and would cost U.S. citizens much more money than if IRS employees did the job. A two-year pilot project in 1996 was so unsuccessful it was cancelled after one year. The pilot project lost money, did not provide adequate protection of sensitive taxpayer data and allowed hundreds of taxpayers to be called outside of the times set by the Fair Debt Collection Practices Act—including calls at 4:19 a.m. (IRS Internal Audity Report No. 080805, December 19, 1997).

IRS Employees

IRS Collections employees have made considerable progress over this past year. In fact, Collections has already closed 100,000 more Taxpayer Delinquent Accounts (TDAs) than expected this year. The IRS has reported to NTEU that the successes of the Collection work increases is attributable to the employees approaching cases strategically, and taking multiple, parallel actions where available. NTEU is confident that the quantity and quality of work performed by the Collections employees will only continue to improve if more resources are devoted to Collections work. However, taking work away from IRS Collections and handing it over to private collection agencies (PCAs) could hinder the momentum and continuity of the Collections team.

The National Taxpayer Advocate Nina Olson has also expressed her concerns about handing this work over to PCAs in lieu of keeping it in-house. In her “Fiscal year 2006 Objectives Report to Congress” Ms. Olson stated, “the National Taxpayer Advocate has significant concerns about supplanting the trained professionals at the IRS with private debt collectors. A primary concern is the quality and quantity of training received by IRS employees versus the training received by private collection representatives.” Although the IRS has attempted to convince skeptics that the PCAs will receive adequate training, you simply cannot compare the years of dedicated service and successful performance of IRS employees to the temporary jobs of private collection agency employees. No amount of training can replace the institutional knowledge and respect for tax compliance and enforcement exhibited by IRS employees.

Problems with PCAs

The IRS will point to state tax revenue agencies that have contracted out state tax collection work to demonstrate successful privatization of tax collection work. However, what the IRS fails to mention is all of the problems that states have faced with private collection agencies. Just last year, an Ohio news station uncovered hundreds of documents that revealed the names, addresses and Social Security numbers of Ohio taxpayers and consumers in twenty-one other states. A private collection agency (PCA) reportedly left hundreds of pieces of confidential taxpayer information in a dumpster in the back of its office in Columbus, Ohio despite the agency's claims that it takes precautions to shred such information. The Ohio Attorney General's office canceled its contract with the PCA.

This past summer, the state of Montana also canceled its contract to collect state tax revenue because of numerous complaints from Montana residents of rude behavior from the contractor's employees. But the contract wasn't cancelled before the company walked away an 18.9 percent bounty—courtesy of Montana taxpayers. This should sound familiar as it is the exact same payment plan the IRS has proposed to its PCA contractors.

A Federal Trade Commission (FTC) report to Congress confirming skyrocketing consumer complaints against debt collectors should make the Internal Revenue Service (IRS) abandon its plan to turn over the personal and sensitive information of taxpayers to this most complained-about industry in America. According to the FTC annual report to Congress on the Fair Debt Collection Practices Act, third-party debt collectors generated 58,687 consumer complaints to the FTC last year—fully 17 percent of all complaints filed with the FTC last year, and a sharp increase from the 12.6 percent the year. This represents a 34.9 percent level of growth in complaints about third-party collectors in 1994. Even more striking though, is FTC's own belief "that the more than 58,000 consumers who complained last year is only a relatively small percentage of people who have problems with debt collectors. Most people simply do not tell the FTC." Certainly, this problem will only worsen once third-party debt collectors are allowed to go after delinquent U.S. taxpayers.

Case Selection and Security Technology

According to GAO's May 2003 testimony before the House Transportation-Treasury Appropriations Subcommittee (GAO-03-732T), one major concern the IRS must address prior to implementing tax collection outsourcing is the ability to identify "delinquent debts with the highest probability of resolution through PCA contacts. Earlier pilot efforts to study the use of PCAs in 1996 and 1997 were hindered, in part, because the IRS was unable to do this... While IRS proposes using the "case selection analytics" to identify appropriate cases, the analytical model has not been developed."

It appears as though the IRS has yet to address case selection even though contracts are scheduled to be awarded next year. According to the IRS' February 15, 2005 "Filing and Payment Compliance Modernization Briefing: The Use of Private Collection Agencies," there are five major issue areas that still need to be addressed before handing work over to the PCAs. One of the issue areas is selecting the workload for PCAs (called Filing and Payment Compliance), which will be part of the Business Systems Modernization Program (BSM). The IRS has experienced cost-overruns and major delays with the BSM contractor. Given its track record with technological innovation, the IRS cannot reasonably expect to provide case selection technology anytime soon. And as NTEU understands, systems being developed that are supposed to predict which cases are most appropriate to turn over to PCAs will not be available until 2011—long after the cases are handed over to the PCAs. Since case selection was a major obstacle for the IRS in its 1996 pilot program, the IRS should guarantee Congress and U.S. taxpayers that case selection technology is in place prior to handing over any work to the PCAs.

Furthermore, the IRS does not have the technology in place to ensure that taxpayer information is kept secure and confidential when it is handed over to the PCAs. The IRS expects to hand over taxpayer information, including Social Security numbers, to the private collection companies.

A serious lack of contractor oversight at the IRS will jeopardize the confidentiality of sensitive taxpayer information. In March 2004, the Treasury Inspector General for Tax Administration (TIGTA) noted that the IRS is still unable to oversee its contractors and ensure that sensitive taxpayer data is secure. TIGTA reports, "Contractor personnel assigned to an IRS modernization project committed numerous security violations that placed IRS equipment and taxpayer data at risk. In some cases, contractors blatantly circumvented IRS policies and procedures even when security personnel identified inappropriate practices. IRS employees did not carry out their responsibilities for ensuring adequate security on contractor workstations and servers and for overseeing contractor activities." (TIGTA Audit #200320010).

In GAO's report, "Internal Revenue Service Needs to Remedy Serious Weakness over Taxpayer and Bank Secrecy Act Data," (GAO-05-482), GAO discovered that the IRS has failed to implement 21 of 53 previously reported security weaknesses found in GAO's 2002 IRS security review. Furthermore, GAO found an additional 39 new information security control weaknesses that would impair the IRS' ability to ensure the confidentiality and integrity of sensitive taxpayer data. The primary reason for these security weaknesses is due to IRS' failure to implement an agency-wide information security program to effectively protect the taxpayer data. The Agency has failed to provide specialized security training to employees with significant security responsibilities—including government contractors! The IRS has also failed to establish a process to periodically test and evaluate its systems.

If the IRS does not have the systems in place to protect sensitive taxpayer and financial data currently, the flaws in security will only be made worse by hiring private contractors to handle IRS collections work.

Funding Source

One of the most often heard arguments in favor of the use of private collection agencies is that if they are paid out of the proceeds of what they collect, it increases the IRS' enforcement capabilities without having to increase appropriations. Numerous Congressional supporters said they would prefer to have tax collection done by federal employees, but would go along with the use of private collection agencies solely because it avoids the difficult issue of getting Congress to approve additional appropriations for the IRS.

The statute that gives the IRS the authority to use PCAs allows 25 percent of collected revenue to be returned to the collection companies as payment and 25 percent to be retained by the IRS for enforcement efforts, thereby circumventing the appropriations process altogether.

There is nothing magical about revenues collected by private collection companies. If those revenues could be dedicated directly to contract payments and IRS enforcement efforts, there is no reason some small portion of other revenues collected by IRS employees couldn't be dedicated to IRS enforcement efforts. This would allow for increased enforcement by IRS employees, which most people indicate is the preferable route and eliminate large payments (up to 25% of collections) to private collection companies, significantly increasing net revenue to the General Treasury. While legislation would be required to allow for this kind of dedication of revenue, I believe the precedent has now been set with the private collection agency funding provisions. Congress should consider supporting this approach as a common sense way to make real progress in closing the tax gap, lowering our deficits and making more funding available for our Nation's critical needs.

Privatizing tax collection is the wrong approach for the IRS and is not the most efficient or effective way to decrease the tax gap or increase taxpayer satisfaction. This plan will merely make confidential taxpayer information vulnerable to fraud and abuse, anger U.S. taxpayers who are approached by the PCAs, and cost the U.S. government more money than if the work were left in the capable hands of IRS employees.

Conclusion

Frontline IRS employees are the best defense against an increasing U.S. tax gap. But it is up to Congress to provide the funding necessary for these employees to do their job. Then, it is up to the IRS to utilize these employees to their fullest potential. Without a doubt, rank and file employees are committed to working with management to increase efficiency and customer satisfaction while decreasing the U.S. tax gap. NTEU is

committed to striking a balance between taxpayer satisfaction, business results and employee satisfaction. I urge Congress to join us in this endeavor.

I thank you for holding this important hearing today. NTEU supports and offers assistance in your mission to shrink the U.S. tax gap.