

**PREPARED TESTIMONY OF
ACTING COMMISSIONER OF INTERNAL REVENUE
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ENERGY POLICY, NATURAL RESOURCES,
AND REGULATORY AFFAIRS
HEARING ON
PAPERWORK BURDEN REDUCTION
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INTRODUCTION

Mr. Chairman, thank you for this opportunity to testify on the Internal Revenue Service's continuing efforts to reduce unnecessary taxpayer burden, and in particular, unnecessary paperwork burden. Our goal is to create the least amount of burden for taxpayers to meet their responsibilities under the tax law. That is a guiding principle for our Office of Taxpayer Burden Reduction, which is the lead organization for our efforts in this critical area.

Since last year's hearing, we have made progress on a number of fronts. For example, by raising the threshold for interest and dividend income, an estimated 15 million taxpayers no longer have to file a Schedule B. And because of our Industry Issue Resolution Program, family day care providers no longer have to keep detailed records and receipts of food purchased for use in their businesses. They may now choose instead to use a standardized rate to claim the deduction for meals provided to children in their care. These small businesses will save an estimated 10 million hours a year.

In addition, over two million taxpayers are enjoying the benefits of the innovative Free File initiative launched in January 2003. Businesses are also finding that they can unburden themselves of even more paper and perform more of their reporting and payment transactions on line. Soon, they will even be able to apply for an Employer Identification Number by going to *www.irs.gov*. We are also simplifying forms and notices to make them clearer and more easily understood. And we are tackling the major redesign of those schedules and forms with a huge impact on individual and business taxpayers, such as Schedule K-1 and Form 941.

Clearly, we have made some progress, but clearly too, reducing unnecessary taxpayer burden in all its many shapes and forms is an enormous challenge, especially when seen within the context of an extremely complex and ever changing Tax Code.

Indeed, as we seek to cut lines, simplify or eliminate forms altogether, and reduce the number of taxpayers having to file forms and schedules, we often must add lines to other tax forms to reflect new changes in the Tax Code that may benefit millions of taxpayers. For example, we added three lines to the Form 1040 for tax year 2002 to

accommodate statutory tax law changes relating to retirement, deductions for educators' supplies, and tuition and fees.

Frequent changes to the tax code and tax law complexity are perhaps the greatest hurdles to overcome as we work to reduce unnecessary taxpayer burden. There is even anecdotal evidence that tax law complexity may be a source of non-compliance, and even, non-filing. Confounded and confused by the complexity, some taxpayers just give up. Moreover, we estimate the cost to taxpayers for complying with the Code to exceed \$80 billion – more than 8 times the cost of the IRS budget.

In a speech delivered last month to the Federal Bar Association, Assistant Treasury Secretary for Tax Policy, Pam Olson, pointed to the fundamental problem that we as tax administrators and a nation of taxpayers face:

“A key way that companies have raised productivity is by simplifying. Take every process down to its constituent parts, and cut out the inefficiencies, the points of friction, the drags that prevent the most streamlined operation and the standardization of transactions. Instead of simplifying to increase productivity in tax compliance and administration, we keep adding complexity – more rules, more limitations, more terms, more conditions, more qualifiers, more provisos, more exceptions. The result is that our system gets slower and slower and more inefficient. We burn more fuel, and emit ever more heat and smoke, and yet with all that burning, there’s less and less light to show for it.”

That is a fair and correct assessment of our present situation. Our myriad efforts to reduce unnecessary taxpayer burden are producing tangible benefits to taxpayers, but we must still address tax law complexity in a meaningful way. If we fail to, we will have failed in our mission to reduce taxpayer burden. Most importantly, we will have failed America’s taxpayers.

PAPERWORK AND REGULATORY BURDEN REDUCTION INITIATIVES

Filing Requirements for Schedule B Changed

In September 2002, the IRS and Treasury Department announced an increase in the threshold for filing a separate schedule for interest or dividend income. The change means that more than 15 million taxpayers will have one less schedule to file with their tax returns this year. Based on the A. D. Little methodology – developed in the 1980s – the estimated burden reduction is 20 million hours.

For their 2002 tax returns, most taxpayers will no longer have to file a separate schedule if they have interest or dividend income of \$1,500 or less. Form 1040 filers use Schedule B, Interest and Ordinary Dividends, to list the names of those who paid them along with the amount; Form 1040A filers use Schedule 1.

The new IRS standard replaces the existing reporting threshold of \$400 that has been in place since 1974. Without the shift, more than 40 million taxpayers would have had to file Schedule B or Schedule 1 this year.

At the time of the announcement, Treasury Assistant Secretary for Tax Policy Pam Olson observed: "While much tax simplification and burden reduction requires Congress to change the law, there are a number of administrative measures the IRS and Treasury can take to reduce complexity and to reduce the paperwork burden on American taxpayers. This is one of those measures. We will continue our efforts to reduce the burden on taxpayers and simplify the tax code."

Our stakeholders also praised the change. Judith A. Akin, president of the National Association of Enrolled Agents commented: "We applaud IRS and Treasury for taking steps to simplify the income tax reporting requirements for taxpayers. We hope to see continued efforts toward tax simplification." NAEA represents approximately 10,000 tax professionals who are registered with the IRS and can represent taxpayers before the agency.

This change will also enable another 800,000 taxpayers to use the shorter Form 1040EZ or use TeleFile to file their tax returns by telephone by increasing the maximum amount of interest income they can report to \$1,500.

As in past years, certain taxpayers with bank or other financial accounts in a foreign country (and certain taxpayers involved in foreign trust transactions) must continue to file Schedule B, regardless of the amount of interest or dividends they receive.

Taxpayers with ordinary dividends and taxable interest, each of which, do not exceed the \$1,500 threshold will report only the totals on their Form 1040.

Increasing the filing threshold will not affect the IRS' efforts to ensure that individuals comply with tax law. The agency routinely receives third-party information returns from the thousands of banks and financial institutions that pay interest and dividends. The IRS then matches these figures to the interest and dividend income reported by taxpayers.

Under law, the threshold amount for filling out a Schedule B for Form 1040 or Schedule 1 for Form 1040A is set at the Commissioner of Internal Revenue's discretion.

Day Care Providers

Late last year, the IRS announced that family day care providers may now choose to use a standardized rate to claim the deduction for meals provided to children in their care. This is in lieu of keeping detailed records and receipts for food purchased for use in their business. Use of the standardized rate will significantly reduce the recordkeeping burden of family day care providers, which are predominantly small businesses.

The change means day care providers will save a conservatively estimated 10 million hours by using the standard meal rate. If these providers decide not to use the rates, they can continue to take the deduction based on the actual cost of the meals.

The guidance, detailed in Revenue Procedure 2003-22, is effective for tax years beginning after December 31, 2002. However, if taxpayers used the standard meal rates (USDA Tier I rates) for prior taxable years to claim their deductible food costs, then the IRS will not raise the issue of the amount of the deduction claimed in the prior years.

The Red Leaf Institute, a non-profit organization committed to improving the quality of family care, submitted the idea of allowing child care providers to use a standardized meal deduction to the IRS Industry Issue Resolution (IIR) Program. The IIR program is designed to address issues that are frequently disputed or burdensome and is discussed in greater detail later in this testimony.

The new rates for family day care providers are the same as the United States Department of Agriculture's Child and Adult Food Care Program (CACFP), Tier I rate in effect each December 31 of the year preceding the current calendar year. The current rate will soon be available on the small business section of the IRS Web site: www.irs.gov/smallbiz by clicking on "industries/professions" in the contents column and choosing "child care." The rates can also be found on the USDA site at www.fns.usda.gov/cnd/care by clicking on "Program Basics" and then selecting the notice under CACFP Reimbursement Rates for the appropriate year.

Checkbox on Social Security Benefits Worksheet

In November 2002, we deleted two checkboxes on the Social Security benefits worksheet used by individual taxpayers, reducing burden by as much as a million hours hours for filers of Form 1040.

Prior to 2002, if a taxpayer checked "No" on line 2, it meant the Social Security benefits reported in box 5 of Form SSA-1099 were less than zero and there would be no taxable benefits. If a taxpayer checked "Yes," the taxpayer would enter one-half of line 1. Since an amount reported in box 5 of Form SSA-1099 is rarely less than zero, the checkboxes have been deleted, thereby eliminating unnecessary burden. Line 2 has been replaced with "Enter one-half of line 1."

Paperwork Reduction in the Works for Tax Year 2003

For Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return, we are eliminating two lines and providing a clear and simplified explanation and computation of "Split Gifts." Scheduled for completion this year, this change will reduce burden for the more than 150,000 taxpayers who elect to split their gifts.

We are also revising the Tax Year 2003 Form 4626, Alternative Minimum Tax – Corporations to remove 4 lines. Three of the lines were little-used adjustments and the other was a line made unnecessary when the form was reduced from two pages to one.

Lastly, we are revising Form T-Timber, Forest Industries Schedule, to remove a section for reporting losses.

FORM REDESIGN

The IRS has adopted a “zero-based” accounting approach to forms redesign. This approach requires us to review each and every line of a form to determine if it is truly needed. In essence, we require that each line be justified. In other words, why is it needed? How is the information used in tax administration? Is the information key entered, i.e. the data is transcribed/captured from the paper document and entered into our computer systems? What are the compliance consequences of not capturing this information? In addition, the Office of the Privacy Advocate evaluates privacy implications in the collection of personal taxpayer information to minimize the gathering of personal information to only that which is necessary to meet the particular business objective.

Our redesign efforts balance the need to minimize unnecessary taxpayer burden and safeguard our tax system and compliance programs. We are applying this approach to our current redesign of the Form 941, Employers Quarterly Tax Return, and Schedule K-1 (partnership, S corporation, and estate and trust distributions).

Form 941 Redesign

The initial vetting of the “vision draft” with stakeholders/partners is planned for September 30, 2003. Thus far, the redesign group has identified existing space on the form used for internal processing that can be made available to allow for improved information formatting and readability. Additional analysis is being conducted to determine what additional steps can be taken to simplify the form. This redesign will affect 6.6 million employers who file quarterly returns.

Schedule K-1 Redesign

The initial vetting of the “vision draft” with stakeholders/partners is planned for July 31, 2003. As with all forms redesign efforts, the need to simplify the form and make it less burdensome, is balanced with the need to insure the integrity of the tax system and the compliance program. This initiative will have significant burden reduction impact, since approximately 23 million schedules are filed each year.

NOTICE AND PUBLICATION SIMPLIFICATION

We continue our efforts to communicate with taxpayers in plain English. Since last year’s hearing, we simplified 10 notices with a total volume of 5 million notices.

- LT-11, Collection Due Process, Intent to Levy
- 10, Math Error With Reduced Credit Elect
- 11, Math Error, Balance Due of \$5 or More
- 11A, EIC Math Error – Balance Due of \$5 or more
- 12A, EIC Math Error – Overpayment of \$1 or more
- 13, Math Error, Balance Due < \$5, Overpayment < \$1
- 13A, EIC Math Error – Balance Due < \$5, Overpayment < \$1
- 138, Notification That the Overpayment on the Return was Offset Against Another Tax Period with a Balance Due
- 139, Form 941, 942, or 940 may no longer be required
- 566B, EITC Examination Package – includes several forms and publications

The above notices are ones that caused significant hardship for taxpayers, or whose wording was perceived by some as intimidating or threatening. Since the simplification, we have received favorable feedback from practitioners on the EITC Examination Package because the new product has customized documents that require taxpayers to only respond to issues that relate to their specific account. The practitioners also praised the package's better organization. We will begin surveying certain notice recipients by June 2003 to capture their feedback.

From July 2003 through January 2004, we will simplify an additional 14 notices with a volume of 17 million. They are as follows:

- 21A, Data Processing Adjustment Notice, Balance Due of \$5 or more
- 21B, Data Processing Adjustment Notice, Overpayment of \$1 or more
- 21C, Data Processing Adjustment Notice, Balance Due <\$5, Overpayment <\$1
- 21E, Examination Adjustment Notice
- 22A, Data Processing Adjustment Notice, Balance Due of \$5 or more
- 22E, Examination Adjustment Notice
- 161, No Math Error, Balance Due (Except Form 1065)
- 2000, Underreporter Program Notice
- 101, Math Error, Balance Due of \$5 or more on Form 940/940EZ
- 102, Math Error Balance Due of \$5 or more on Forms 941, 941SS, 942, 943, 945
- 112, Math Error, Overpayment of \$1 or more on Forms 941, 941SS, 942, 943, 945
- 128, Balance Due remaining after offset
- 210, Audit/DP Tax Adjustment
- 220, Audit/DP Tax Adjustment, Notification

We are also revising a number of publications. For example, we are consolidating Publications 508, 520 & 970 into one publication about tax benefits for education, thereby making it easier for taxpayers and practitioners to research and get the

information they need about these important benefits. A total of approximately 500,000 copies of these publications were distributed last year.

In addition, we are evaluating customer satisfaction regarding the usefulness of Publication 17 – “Your Federal Income Tax” – the comprehensive tax guide for individuals. We will use information obtained last year from focus groups to determine what changes may be needed (including redesign) to better meet taxpayers’ needs for clear information. A total of approximately of 2.4 million copies of Publication 17 were printed last year.

REDUCING TAXPAYER BURDEN THROUGH ELECTRONIC TAX ADMINISTRATION (ETA)

The enormous popularity of e-file and its continued growth can be attributed largely to its value to taxpayers – and one of the greatest values is burden reduction. Taxpayers switching from paper to electronic filing find their burden reduced in a number of key areas. They spend less time filing and paying their taxes. With direct deposit of refunds, they are spared a trip to the bank, ATM or post office. And there are fewer errors with e-file, thereby sparing taxpayers potentially time-consuming interactions with the IRS.

Since its modest beginnings as a pilot in 1986, we have added more options each year to e-file to make it more attractive to taxpayers. They range from payment by credit card, direct deposit of refunds, and self-select PINs to adding more forms and joint filing of federal and state returns. For the 2003 filing season, we kept many of the options popular with taxpayers and added some new ones.

INDIVIDUAL E-FILE

On January 16, 2003, the Treasury Department, the Office of Management and Budget (OMB) and the IRS launched a free online tax preparation and filing service called Free File. It was made possible through a partnership agreement between the IRS and the Free File Alliance, LLC – a private sector consortium of tax software companies.

Free File can be accessed by going to our redesigned web site at www.irs.gov, or by going to www.firstgov.gov. These free services will be available this year through April 15, 2003. Some companies will also offer free services through October 15, 2003 to accommodate taxpayers who may need an extension.

The partnership agreement requires that the Alliance as a whole provide free tax preparation and filing to at least 60 percent, or approximately 78 million American taxpayers. The primary candidates for Free File are those taxpayers who prepare their own taxes and still file paper returns. Over 2 million taxpayers have used Free File this filing season.

Each participating software company sets its own eligibility requirements. Generally, these requirements may be one, or any combination of the following: (1) age;

(2) Tax Year 2002 Adjusted Gross Income; (3) eligibility to file Form 1040EZ; (4) eligibility to claim the Earned Income Credit; (5) State residency; and (6) active duty military status (if applicable). Unless noted, if the taxpayer is married and filing jointly, only one taxpayer must meet the eligibility requirement.

For 2003, taxpayers are also able to electronically file seven new forms related to their Individual Income Tax Returns:

- Form 970 – Application to Use LIFO Inventory Method
- Form W-2G – Guam Wage and Tax Statement
- Form 1099-G – Certain Government and Qualified State Tuition Program Payments
- Form 1310 – Statement of Person Claiming Refund Due to a Deceased Taxpayer
- Form 8594 – Asset Allocation Statement Under Sections 338 and 1060
- Form 8880 – Credit for Qualified Retirement Savings Contributions
- Form 8885 – Health Insurance Credit for Eligible Recipients

This year, taxpayers can also quickly check the status of a refund with a new Internet-based service available on the IRS web site, called “Where’s My Refund?” Taxpayers can get the information they need quickly, efficiently and safely. For FY 2003, we expect 15 million users of “Where’s My Refund?”

Simple online instructions guide taxpayers through a process that checks the status of their refund after they provide identifying information shown on their tax return. Once the information is processed, results can include one of several responses, including:

- That a return was received and is in processing;
- The mailing date or direct deposit date of the taxpayer’s refund; or
- Whether a refund has been returned to the IRS because it could not be delivered.

The results also include links to customized information that is based on the taxpayer’s specific situation. The links guide taxpayers through the next steps needed to resolve any issues that may be affecting their refund.

“Where’s My Refund?” is accessible to visually impaired taxpayers with the Job Access with Speech (JAWS) screen reader used with a Braille display and is compatible with different JAWS modes.

For the 2003 filing season, taxpayers are also able to select one of two options for signing their e-filed return. The Self-Select PIN and Practitioner PIN methods allow taxpayers to electronically sign their e-filed return by entering a five-digit PIN.

The Self-Select PIN Program began in 2001, and by 2002, PINs were used to e-file 9.8 million returns. For 2003, certain taxpayers under the age of 16, and those who are filing on behalf of a deceased taxpayer, can sign the return using a Self-Select PIN.

For 2003, the Practitioner PIN is open to all electronic return originators (no agreement required). First-time filers and taxpayers under the age of 16 are eligible to use the Practitioner PIN method.

ETA ALSO EASING BUSINESS TAXPAYER BURDEN

A strong ETA program may be even more important for reducing burden for businesses than for individual taxpayers. In addition to their annual income tax returns, businesses also have to file various employment tax returns and information returns. Businesses also make a lot of payments to the federal government, such as withholding and unemployment taxes. In fact, payments are a business' most frequent transaction with the IRS.

We want to convert all of these transactions to fast, accurate, paper-free electronic methods. And we are making progress on a number of fronts.

During FY 2002, over 3.2 million taxpayers made \$1.5 trillion in electronic tax payments through the Electronic Federal Tax Payment System (EFTPS), which now includes an online option. For 2003, IRS expects more than 4 million taxpayers to pay their taxes using the EFTPS System.

In FY 2002, we also received more than 2.5 million 941 *e-file* program returns (Employer's Quarterly Federal Tax Return) and 855,000 returns for 941 TeleFile and On-Line Filing Programs. In CY 2002, over 320,000 businesses used the 940 *e-file* Program (Employers Annual Federal Unemployment Tax Return), and more than 24,000 partnerships chose 1065 *e-file* (U.S. Return of Partnership Income) in FY 2002.

In 2003, the IRS plans to make even further progress serving business' electronic tax administration needs. For example, tax professionals are able to file employment taxes for business clients for the first time as part of a new Employment Tax e-filing System.

We also expect that coming e-file upgrades will continue to reduce the paperwork burden on small businesses. The enhanced e-file system is part of an ongoing effort to reduce small business burden and barriers to electronic filing. This e-file option will replace outdated technology that was a burden to both businesses and the IRS. Key benefits of the new system are:

- More flexible filing – Forms 941 and 940 can be filed in a single transmission;

- More specific error conditions – New error conditions pinpoint the location of the error and provide complete information for each error identified;
- Faster acknowledgements – Transmissions are now processed upon receipt and acknowledgments are returned in near real-time; and
- Integrated payment options – Eligible filers may submit a required payment along with their return, subject to limitations imposed by the Federal Tax Deposit Rules.

Businesses will also soon be able apply for an employer identification number (EIN) by using our new on-line EIN Application at *irs.gov*. When a business applies, its EIN will display on the SS-4 for printing and record keeping and each applicant will receive their formal validation letter.

REDUCING TAXPAYER BURDEN THROUGH INNOVATIVE ISSUE MANAGEMENT/PROBLEM RESOLUTION

Mr. Chairman, for many taxpayers, particularly business taxpayers, burden takes the classic form of time and money – the time and expense it takes to resolve an issue or problem that may affect one business or even, an entire industry. Ideally, we want to shift from addressing taxpayer problems well after returns are filed to addressing them as early as possible in the process, and in fact preventing problems wherever possible. To this end, we have created a number of programs in our operating and functional divisions to address issue management and problem resolution.

The Industry Issue Resolution Program

The Industry Issue Resolution (IIR) program began more than two years ago as an initiative under our Large and Mid-Size Business Operating Division's Issue Management Strategy. The IIR program provides guidance on frequently disputed or burdensome business tax issues. Benefits of the program include reduced costs and burden, and eliminating uncertainty regarding proper tax treatment, for both taxpayers and IRS. We estimate that it has provided millions of hours in taxpayer burden reduction.

For each issue, a multi-functional team, including LMSB, Treasury, Counsel, Appeals, Small Business/Self-Employed representatives, was formed to receive input from taxpayers and develop a resolution position.

The pilot program was evaluated and determined to be successful. In 2002, Notice 2002-20 was issued to announce the decision to make IIR a permanent program, expand the program to include Small Business/Self-Employed business issues, establish burden reduction as an issue criterion and invite issue submissions. For 2002, 38 issues were submitted from businesses, tax practitioners and associations and seven were accepted for the IIR program.

To date, resolution positions on the following 8 IIR issues have been announced:

- Revenue Procedure 2003-20 provides a safe harbor method of accounting to value re-buildable motor vehicle cores inventory.
- Revenue Procedure 2003-22, provides family day care providers with the option to use standard meal and snack rates in computing the deductible cost of food provided to eligible children under their care.
- Revenue Procedure 2002-41 provides employers in the pipeline construction industry an optional deemed substantiated method for reimbursing certain employee business expenses.
- Revenue Ruling 2002-9 provides that impact fees incurred in connection with the construction of new residential rental buildings are a capitalized cost of the building.
- Revenue Procedure 2002-12 provides taxpayers engaged in the trade or business of operating a restaurant or tavern with a safe harbor method of accounting for the cost of "smallwares."
- Revenue Ruling 2001-59 clarifies the necessary steps to record a loan as a "loss asset" under the bad debt conformity method of accounting for banks.
- Revenue Procedure 2001-56 provides a simplified method for automobile dealerships to determine the amount to include in employees' pay for use of demo vehicles.
- Revenue Ruling 2001-60 allows certain golf course land improvement costs to be depreciated.

IIR Issues Pending:

- Depreciation of cable television systems under section 168
- Tax treatment of pre-production costs of creative property
- Recovery period for depreciation of gasoline pump canopies
- Definition of highway tractors subject to the heavy truck tax under section 4051
- Deduction and capitalization of costs incurred by utilities for assets used for power generation
- Determining recoverable reserves of oil and gas for cost depletion purposes

IRS expects to announce resolution positions on these pending issues by the end of June 2003.

Fast Track Mediation (FTM)

Fast Track Mediation evolved from the Modernization/Re-Engineering process. It is designed to help Small Business/Self Employed taxpayers resolve disputes resulting from examinations and collection (offer in compromise, trust fund recovery penalty, and certain collection due process) actions. FTM reduces taxpayer burden by resolving disputes in a fair and impartial manner, as well as on a timely basis. Disputes will be resolved within 30 to 40 days compared to several months through the regular appeals process.

FTM began as a pilot program in June 2000, in four cities. During the pilot, 56 cases were mediated. The average time to close a case during the pilot was 48 days. Taxpayers rated the overall satisfaction with the process at 4.2 on a scale of 1 to 5, with 5 being the highest rating.

Due to the success of the pilot, on June 1, 2002, FTM was rolled out nationwide. To date, a total of 313 Appeals employees have been trained in mediation. Appeals expects to hold another 5 classes this fiscal year. All FTM training is contracted through the Federal Mediation and Conciliation Service (FMCS). Since the rollout, case receipts have been rising. In Fiscal Year 2002, Appeals received 86 cases from June to September, while total current receipts for Fiscal Year 2003 are 96 cases. The current overall customer survey satisfaction result is 4.0.

The FTM process involves Appeals personnel who have been trained in mediation to facilitate communication between the taxpayer and the IRS. The purpose is to help the parties reach a mutually satisfactory resolution of the issues that is consistent with applicable law. The mediator does not have settlement authority. If an agreement is not reached, the taxpayer maintains his or her normal appeal rights. If agreement is reached, Compliance uses standard closing procedures. For mediation to be successful, all decision-making parties must be present at the conference.

A revenue procedure on FTM is being reviewed by Chief Counsel's office. Publication 3605, Fast Track Mediation-A Process for Prompt Resolution of Tax Issues, lists cases excluded from the program.

The LMSB Fast Track Settlement Program

The LMSB Fast Track Settlement Program has effectively and significantly reduced taxpayer burden in numerous ways. A recent survey of taxpayers who completed the process asked them to identify what they expected to gain from the Fast Track process. The three top expectations (in order of number of responses) were: (1) quicker resolution of their cases, (2) lower non-tax costs, and (3) reduction in staffing demands. When asked if their expectations had been substantially met, the average agreement rate was 4.21 on a five-point scale where five is "strongly agree."

The survey asked taxpayers what they felt was the effect on examination cycle time, case resolution cycle time, their staff days applied to the examination process, and the effect on non-tax costs. Their responses reflect the following:

- 75% said examination cycle time was reduced
- 88% said the case resolution cycle time was reduced
- 79% said their applied staff days were reduced
- 79% said the Fast Track process reduced their non-tax costs

We estimate that the overall case resolution cycle time is reduced by approximately 920 days for cases participating in the Fast Track process.

A high overall satisfaction rating reflected on the Taxpayer LMSB Fast Track Survey also indicates burden reduction. The average satisfaction rating was 4.21 on a scale of 1 to 5, where 5 indicates a high degree of satisfaction.

A potential, but as yet unproven burden reduction method, involves the increased ability to utilize the LMSB Team Manager's ability to settle issues under the authority of Delegation Order 236. This delegation order gives the team manger the authority to settle issues on the same bases that Appeals has settled the issue in prior years' cases. Without Fast Track, the team manager frequently does not have the Appeals settlement in time to utilize it. Under Fast Track, the team manager will have settlement before the next examination cycle is started.

Limited Issue Focus Examinations

Our LMSB Division is implementing a new streamlined examination process called the Limited Issue Focused Examination, or LIFE.

This initiative will involve a formal agreement, a Memorandum of Understanding (MOU), between the IRS and taxpayer served by LMSB to govern key aspects of the examination. The MOU will contain dollar-limit thresholds, established on a case-by-case basis, below which the IRS will agree not to raise issues and the taxpayer will agree not to file claims. This will create, with the taxpayer's assistance, an atmosphere where the examination process is less difficult, less time-consuming, less expensive and less contentious for all involved.

Working together, both the IRS and the taxpayer will focus their resources and time on the issues most significant to the return under examination.

LIFE is a two-way street. Making it work will require taxpayers and the IRS to work cooperatively. Many of the resource benefits of this approach to taxpayers and the IRS will flow from taxpayers meeting the commitments they make at the commencement of a focused examination.

This new approach represents a major culture shift for LMSB. LIFE is an effort by LMSB to institutionalize best practices and provide consistency in the treatment of taxpayers. Training of IRS personnel is currently underway.

DEVELOPING A TAXPAYER BURDEN MEASUREMENT METHODOLOGY

In 1998, the IRS began work on a model that would provide better estimates of taxpayer burden. We wanted a tool both for measuring burden and for understanding how IRS administrative actions and tax legislation affect taxpayers' compliance burden. This new model could also satisfy the need for improved information for OMB's use in meeting the requirements of the Paperwork Reduction Act (PRA). Price Waterhouse, now IBM, was the contractor selected to do the work.

The project's massive scope necessitated doing it in steps. The initial work focused on individuals filing income tax Form 1040 and its many schedules and related forms. This was broken into two segments: Wage and Investment (W&I) and Self Employed (SE) taxpayers. Pre-filing and filing activities were included.

In March 2002, IBM delivered a burden simulation model, addressing the Federal income tax compliance burden of W&I taxpayers. The Integrated Taxpayer Burden Model (ITBM) was delivered in January 2003 and is undergoing final review. It integrates the W&I and Self-Employed populations to yield a comprehensive model of individual taxpayer compliance burden. Initial data from the new model indicate the time taxpayers spend complying with the federal tax code has been understated. The model will provide IRS with a new baseline for understanding the tax burden on our citizens.

The ITBM model will be able to provide the user with information unique to each taxpayer's burden. It can estimate taxpayer compliance costs in terms of time and out-of-pocket expenditures by: type of taxpayer (W&I, S/E), preparation method (paid preparer, self-prepared with software, self-prepared without software), submission method (paper, electronic), income classification (adjusted gross income), and taxpayer activities (e.g., record keeping, form completion).

The model has great potential for IRS because it can answer a variety of different needs. IRS management can prioritize initiatives by using the model to estimate the impact of an initiative on taxpayer burden. For example, the model could be used to estimate the impact of administratively changing various thresholds, e.g., interest and dividends. Also, the model can assist with the evaluation of tax policy. "What-if" scenarios reflecting potential legislative changes can be specified by model users to estimate the impact on burden. For example, the model could assess the effect on taxpayers of reducing the marriage penalty by increasing the standard deduction for married taxpayers.

IRS and IBM have recently begun work on a new model estimating the burden of income and employment taxes on small business taxpayers. The new model methodology will take into account the many differences between small business and individual taxes and be as consistent as possible with the ITBM. IBM is soliciting input from various individuals and stakeholder groups to validate assumptions and refine the focus and scope for the SB model covering filers of Forms 1065, 1120, 1120S and 940/941.

Ultimately, we hope to have taxpayer burden models covering most of the tax system, that is, mid-size corporations, tax-exempt entities, post-filing, and perhaps some other specialty taxes. In addition, the current work must be updated every five to seven years, depending on the changes in the law. These projects are costly, particularly because surveying is expensive; it has not been decided whether each of these projects will require surveys.

CONCLUSION

Mr. Chairman, in conclusion, I believe that the IRS continues to demonstrate progress in the fight against taxpayer burden in all of its forms. We will continue to seek administrative and other solutions to reduce taxpayer burden. However, at the same time, tax law complexity must be squarely addressed. Absent such a dual approach, we will never be able to reduce taxpayer burden in a meaningful fashion.