INTERNAL REVENUE SERVICE
ADVISORY COUNCIL
PUBLIC MEETING

OCTOBER 18, 2002
1111 CONSTITUTION AVENUE, NW
WASHINGTON, DC

INTERNAL REVENUE SERVICE
ADVISORY COUNCIL
PUBLIC MEETING - ROOM 2140 MAIN IR
OCTOBER 18, 2002
AGENDA

8:30 - 9:00	Meet & Greet	
9:00 - 9:30	Opening Remarks	Charles O. Rossotti Commissioner, Internal Revenue Bob Wenzel Deputy Commissioner, Internal Revenue
9:30 - 9:50	General Remarks	David R. Williams Chief, Communications & Liaison
9:50 - 10:45	General Report of the Council K-1 Matching - Ogden Campus Offers-in-Compromise	Roger N. Harris Chairman, Internal Revenue Service Advisory Council
10:45 - 11:00	BREAK	
11:00 - 12:00	Small Business & Self Employed Subgroup Report	Joe Kehoe Commissioner, Small Business & Self Employed Operating Division Michael Evanish, Chair, Small Business & Self Employed Subgroup
12:00 - 1:45	LUNCH To Be Provided	
1:45 - 2:45	Large & Midsize Business Subgroup Report	Deborah Nolan Deputy Commissioner, Large & Midsize Business Operating Division Eliot Kaplan, Chair, Large & Midsize Business Subgroup
2:45 - 3:00	BREAK	
3:00 - 4:00	Wage & Investment Subgroup Report	John Dalrymple, Commissioner, Wage & Investment Operating Division Gregory Steinbis, Chair, Wage & Investment Subgroup
4:00 - 4:15	Closing Remarks	Roger Harris
4:15	ADJOURN	

INTERNAL REVENUE SERVICE
ADVISORY COUNCIL

PUBLIC MEETING
BRIEFING BOOK

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OCTOBER 18, 2002

GENERAL REPORT OF THE INTERNAL REVENUE SERVICE ADVISORY COUNCIL

INTRODUCTION

The purpose of the Internal Revenue Service Advisory Council (hereinafter "IRSAC" or the "Council") is to provide an organized public forum for discussion of relevant tax administration issues between Internal Revenue Service (hereinafter "IRS" or the "Service") officials and representatives of the public. Membership on the IRSAC for the year ending 2002 consists of twenty-four individuals who bring a wide breadth of experience, disparate expertise, and diverse backgrounds to bear on the Council's activities.

The IRSAC has organized itself into three subgroups, corresponding to three of the four IRS' Operating Divisions: the Large & Mid-Size Business Subgroup (hereinafter the "LMSB Subgroup"); the Small Business/Self-Employed Subgroup (hereinafter the "SBSE Subgroup"); and the Wage & Investment Subgroup (hereinafter the "W&I Subgroup"). The reports of these subgroups that follow this general report are a result of three working sessions held in Washington during the year and numerous conference calls between IRSAC members and key IRS personnel. The members of the IRSAC would like to thank representatives of the Service for their time and commitment to the work of the Council. Special thanks must go to the staff of the Office of National Public Liaison for ensuring that Council members had the resources necessary to function properly as an advisory body.

This year, for the first time, members of the IRSAC attended the four mega-sites of the IRS Nationwide Tax Forums: Atlantic City; Atlanta; New Orleans; and Reno. Together with representatives of the Information Reporting Program Advisory Committee (hereinafter "IRPAC"), IRSAC members participated in focus groups intended to gather input from the practitioner and taxpaying communities with respect to issues the Council is and/or should be considering. We found that not only did our attendance

heighten Council members' awareness regarding problematic issues encountered by practitioners, but further, our attendance increased practitioner and taxpayer community awareness regarding the existence of and work performed by advisory groups such as the IRSAC. Accordingly, the IRSAC recommends that the Council's participation in the Nationwide Tax Forums continue in the future.

ISSUE ONE: ADEQUATE FUNDING

The IRSAC has strongly supported the need for consistent and adequate levels of funding for purposes of enabling the IRS to implement its programs. We again provide that support. The workload of the Service continues to increase each year. While the recently completed reorganization will help manage the increasing workload, only an increase in resources will permit the IRS to truly keep pace. Further, the IRSAC believes that the IRS must continue to improve its technology and increase its full-time staff to operate effectively.

The Service will continue to face difficult decisions with respect to allocating limited resources as between the compliance and service functions. While we recognize the importance of service to taxpayers, we believe that increased compliance efforts are critical to the proper functioning of our voluntary tax system. The IRSAC recommends that resource allocation decisions focus on ensuring that the compliance efforts of the IRS are maximized.

ISSUE TWO: K-1 MATCHING

The K-1 Matching Program has been a focal point of the work of this year's IRSAC. The IRSAC strongly supports the development of a K-1 Matching Program, believing such a program to be necessary. However, the IRSAC likewise believes that a K-1 Matching Program should not increase taxpayer/practitioner burden or needlessly consume precious IRS resources. While results from the compilation of K-1 matching data are not yet complete, the IRSAC believes that a matching program should focus on taxpayers who have omitted K-1's from their returns. Further, the IRSAC believes that an effective

matching program can be devised without imposing undo burdens on any party. If, however, the compiled data results indicate the need for a more extensive program, the IRSAC believes that the IRS should include representatives from all effected stakeholder groups in the design of such a paradigm.

The IRSAC was disappointed that the IRSAC K-1 Task Force recommendations included in our last Public Report were not considered (K-1 Task Force Report attached herein as Exhibit A), noting in particular the critical importance that attached to ensuring a viable K-1 Matching Program - before implementation - to avoid erosion of IRS' credibility. However, recent discussions with IRS executives have been straightforward and open. Members of the IRSAC were invited to visit the Ogden Service Center for the purpose of reviewing and discussing K-1 Matching Program operations with front-line employees having responsibility for administering the program. The openness of those discussions and the dialog that currently exists between the IRSAC and IRS executives demonstrate the sincere desire of all parties to create a viable, effective, properly administered program.

For purposes of emphasis, the IRSAC must restate its support for a viable, equitably administered K-1 Matching Program that does not impose undo burdens on any party or needlessly consume limited IRS resources. The SBSE Subgroup Report attached herein addresses the issues underlying the K-1 Matching Program in detail.

ISSUE THREE: THE NATIONAL RESEARCH PROGRAM

The IRSAC would like to offer its support for the National Research Program (hereinafter "NRP") that will begin this year. While most people recoil at so much as the thought of an audit, such exams are nevertheless a necessity if the integrity of our voluntary tax system is to survive. Accordingly, as long as audits are necessary, the selection of returns for examination is critically important given the limited resources that give rise to IRS' decisions with respect to how such resources will be allocated. As has been said by others before us, the IRSAC believes this program makes good business sense.

To date, the IRSAC has been briefed on the extensive planning that has gone into developing the NRP. It is apparent that a great deal of work has been done to ensure that the program yields contemplated results. As of our last meeting, the training program designed for the cadre of hand-selected auditors who will conduct NRP audits had just begun. Proper training, implementation, and communication are critical for this program to succeed. Members of the IRSAC were pleased to learn that representatives from external practitioner groups participated in training these IRS' auditors. The solicitation of external stakeholders' assistance with this training program demonstrates the importance placed on making the NRP a success within the IRS. The Council will continue to monitor this program as implementation begins in the field, and anticipates providing commentary on the progress of the NRP in its next report.

ISSUE FOUR: THE FILING SEASON AND ELECTRONIC FILING

The IRSAC is pleased to report that the past filing season appears to have gone well, and is particularly pleased to note the increase in electronic filing. While electronic filing numbers are encouraging, the Congressional mandate that eighty percent of all returns be electronically filed by fiscal year 2007 will not be met at the current rate of increase. The IRSAC hopes that the IRS will continue to work with external stakeholders, particularly practitioner groups, to accelerate electronic filing at rates that will reach the Congressionally mandated goal. The IRSAC believes that efforts focused on practitioners and practitioner groups will yield greater benefits than efforts directed at motivating/incentivizing individual taxpayers. As we look at programs such as K-1 Matching, it is readily apparent that increased electronic filing will facilitate more effective IRS' operations. Accordingly, the IRSAC looks forward to partnering with the IRS in the coming year to effect changes that will help reach this important goal.

CONCLUSION

The 2002 IRSAC is the last Council to have had the pleasure of working with Commissioner Rossotti. The Commissioner has always been accessible to IRSAC members and has unfailingly encouraged

us to provide honest input. We have also had the opportunity to personally view the improvement his leadership has made in the performance of the Service. A common theme emanating from virtually everyone is that the IRS is a much better organization today than it was five years ago. Much of the credit for this improvement goes to Commissioner Rossotti and his leadership. We would like to thank Commissioner Rossotti on behalf of the IRSAC, IRS employees, and all taxpayers for his leadership, vision, and dedicated service these past five years. The Commissioner will be sorely missed and we wish him and his family the best in the coming years.

INTERNAL REVENUE SERVICE ADVISORY COUNCIL

SMALL BUSINESS & SELF-EMPLOYED SUBGROUP REPORT

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October 18, 2002

I. INTRODUCTION

The SBSE Subgroup met in three working sessions held in Washington, D.C. and participated in several conference calls with Small Business/Self-Employed executives and personnel. In addition, as discussed in the General Report, many subgroup members participated in Nationwide Tax Forum focus groups across the country. The subgroup reviewed the Transition Report of the 2001 IRSAC SBSE Subgroup to begin this year's term, opting to primarily emphasize the areas of Budget, Compliance, Offers-in-Compromise, and K-1 Matching.

The Small Business/Self-Employed Operating Division serves the largest taxpayer segment of the four Operating Divisions; a responsibility compounded by the fact that the Operating Division's taxpayer base is at greatest risk to encounter compliance problems. Small Business/Self-Employed taxpayers often lack the requisite knowledge needed to comply with all areas of the tax law and can fall out of compliance quickly. It is for these reasons that the SBSE Subgroup, though not examining this area in 2002, would like to commend the IRS for its efforts in the areas of education and outreach. Education efforts will reduce taxpayer compliance issues in the future.

The mission of the Small Business/Self-Employed Operating Division is "to provide s[mall Business/Self-Employed] taxpayers with top quality service by educating and informing them of their tax obligations, developing educational products and services, and helping them understand and comply with applicable laws, and to protect the public interest by applying the tax law with integrity and fairness to all." However, the Division's ability to achieve this mission is complicated by a severe funding shortfall. That this problem can be resolved by Congress alone notwithstanding, the SBSE Subgroup believes that the accumulated shortfall has reached a critical point. Action is needed to prevent a dramatic decline in voluntary compliance. The number of field examiners must increase, as must the audit rate, and the growing perception that the "audit lottery" carries little risk must stop.

Problematic compliance issues will always exist, but the current economic environment that fosters rapidly increasing change requires an IRS that is fully staffed by adequately trained and versatile personnel, ready to meet the challenges created by such an economy. Large, centralized programs will help, but it will be the field examiners who surface new compliance problems. Accordingly, it is vital that these examiners receive adequate training and are given the authority to address the issues they discover.

The Offer-in-Compromise Program has been problematic for some time. In fiscal year 2002, steps were taken to improve processing and reduce the existing backlog. Work must begin to drill down Offer-in-Compromise Program data for the purpose of determining the cause or causes giving rise to an exponential increase in the number of taxpayers who find themselves in need of this program. A process must be put in place to monitor future compliance for taxpayers whose offers are accepted. Education and compliance elements must also be added to the program.

The K-1 Matching Program began in earnest during fiscal year 2002. Several problematic issues lead Small Business/Self-Employed executives and K-1 Program personnel to suspend the distribution of CP notices subject to an analysis of K-1 data that is currently underway. While the results of the compiled K-1 matching data are not yet available, as discussed in the General Report, the IRSAC believes that a matching program should focus on taxpayers that have omitted K-1's from their returns. Further, the SBSE Subgroup believes that the K-1 Matching Program is the first step in a much needed compliance effort involving all pass-through entities.

ISSUE ONE: THE BUDGET

The Small Business/Self-Employed Operating Division lacks the funding necessary to provide adequate resources for the wide-ranging taxpayer issues within its jurisdiction. The Division is under-staffed, audit rates are down, compliance issues are increasing, and implementation of new initiatives and much-needed programs is delayed. As the scope and complexity of Small Business/Self-Employed issues increase,

the corresponding need for enhanced training likewise increases, and management must allocate resources between service and compliance issues at the expense of many worthwhile compliance initiatives that cannot be undertaken due to budget constraints. In short, funding is not keeping pace with the frenetic growth of the workload. Indications suggest that in the coming years:

- the number of SBSE taxpayers will increase;
- the number of SBSE tax returns will increase;
- the complexity of tax returns will increase; and
- funding shortfalls will continue.

It is challenging for any management team to meet its mission without adequate staffing, and it is staff working face-to-face with taxpayers, staff working face-to-face with practitioners, and staff working manageable caseloads that make effective, customer-oriented compliance possible.

ISSUE ONE: RECOMMENDATION

Within the Small Business/Self-Employed Operating Division, increased resources are necessary to meet the challenge of an increasing taxpayer base and the increasing complexity of the tax law. While funding for critical infrastructure has been secured, and the badly needed upgrade of computer systems is underway, a long-term budgetary commitment in the area of staffing is essential to achieve necessary compliance levels. The human element must not be forgotten. Notwithstanding the quantity and quality of equipment or the inventiveness of computer programmers, it is the front-line employees who are most essential.

Given the current staffing shortages within the Small Business/Self-Employed Operating Division, the SBSE Subgroup believes that Small Business/Self-Employed management and staff should be commended for their achievements across the past few years. Accordingly, we recommend that sufficient resources be provided to fully staff Small Business/Self-Employed in a manner compatible with good

management practices, which will provide proper staff training. We understand that this will require a multi-year commitment of both funding and implementation. We further recommend that funding be part of all mandates from Congress.

ISSUE TWO: COMPLIANCE

We examined and support implementation of the following priority compliance programs that were outlined for the subgroup:

A. **NATIONAL RESEARCH PROGRAM** – The National Research Program ("NRP") is a much needed, top priority program that will begin this fall. Designed to measure compliance and help effectively identify compliance issues, this program is vital for ensuring that the IRS has accurate, up-to-date information with which to detect trends in noncompliance and select the returns appropriate for examination. Data gathered by the NRP will enable the IRS to update existing screening techniques used to select tax returns for examination. With updated information, the NRP effort will prevent thousands of "no change" audits each year.

B. **THE UNREPORTED INCOME DISCRIMINANT INDEX FORMULA -** (hereinafter "UIDIF") - is a vital compliance tool that the IRS has developed, along with the NRP, that will greatly increase the effectiveness of auditors and taxpayer compliance. Unreported income represents the largest component of the tax gap. This tool was developed to identify returns with a high probability of unreported income.

C. **HIGH-INCOME TAXPAYERS AND NON-FILERS** are being targeted as potential noncompliance problems as they aggressively seek to reduce their tax burden or simply drop out of the system.

D. **OFFSHORE CREDIT CARDS AND OTHER ABUSIVE TAX SCHEMES** are important areas to target. Early intervention by the IRS is important to prevent the abusive shelters currently

marketed to taxpayers. Abusive schemes that are openly marketed decrease the public's perception of a fair tax system.

E. **SPECIAL RESEARCH PROJECTS SUCH AS THE CALIFORNIA RESTAURANT PROJECT** - spearheaded by Taxpayer Education and Communication (hereinafter "TEC"), Southern California restaurant owners who potentially had underreported gross income in recent years received letters educating them about the need to accurately and properly report business income. Called the California Restaurant Industry Compliance Project (hereinafter "CRICP"), recipients of the letters were encouraged to review their federal tax returns for accuracy and contact their tax practitioner should changes have been required. Educational letters were also sent to preparers of discrepant returns. Taxpayer Education and Communication met with the California Restaurant Association and a number of tax professional organizations to introduce this project and outline the educational efforts made through workshops, online access, and trade and practitioner newsletters. The project will soon expand nationwide.

The SBSE Subgroup commends everyone involved in setting the current divisional compliance priorities. It is also encouraging to hear that auditor training will begin to focus not only on code and number issues but also on improved investigation skills. Beyond the numbers, examiners will have an expanded view of the audit to ensure that everything "feels right". While this approach may lengthen the amount of time certain cases are open; the results should justify the time invested.

ISSUE TWO: RECOMMENDATION

The SBSE Subgroup agrees with and endorses all of these priorities as well as expanding investigation skills training for examiners. There is a vast amount of data, both internal and external, available to the IRS that could be utilized in the matching or case building process. The Small Business/Self-Employed

Operating Division should maximize use of internal and external data to create compliance matching and audit initiatives for purposes of detecting and targeting noncompliance and non-filers. The California Restaurant Industry Compliance Project was a particularly well designed initiative to increase compliance. Similarly designed/managed projects should be implemented. Efforts should also be made to increase early intervention with respect to non-filing and non-payment of taxes.

The NRP and UIDIF are programs that should facilitate a more efficient audit selection process, improve selection of non-compliant returns for audit while minimizing resources, i.e., audit time, to secure maximum results. Further, when a case reaches an auditor, it is important that the auditor be able to secure data from sources he or she deems important. It is likewise important that the audit rate increases. Voluntary compliance and compliance enforcement has decreased in recent years. Only an increase in the number of audits, greater efficiency in audits performed, and a change in the public's perception that significant risk does *not* attach to the "audit lottery" can reverse this trend.

The Small Business/Self-Employed Operating Division recognizes the importance of education and educational tools for improving compliance. It is likewise important to understand the significance attaching to the education of future as well as present taxpayers. For this reason we believe that programs aimed at educating high school students should be aggressively undertaken.

ISSUE THREE: THE OFFER-IN-COMPROMISE PROGRAM

The Offer-in-Compromise Program (hereinafter "OIC") has given rise to many problematic issues. This is particularly true from a cost/benefit perspective, i.e., the cost of collection versus the amount collected. However, in fiscal year 2002, several improvements took place. The centralized offer process has reduced the amount of time required to process an offer. In the past, OIC settlements could take years to settle. New procedures are clearing fifteen to twenty percent of the offers submitted by screening non-qualifying cases based on information supplied by the taxpayer.

The offer of a "reasonable collection potential amount", as computed on Form 433B, is the first step in a processable offer. Case building activities take place later in the process. A pre-screening process has been implemented that prevents cases the IRS determines can be paid in full from entering the OIC process. These cases are subsequently turned over to Account Collection Services. Accordingly, this simple screening process has resulted in reclaiming and redirecting valuable resources to internal processes for purposes of addressing the OIC backlog. Further, where an offer has been allowed to remain on someone's desk too long, thus rendering the offer/package outdated, taxpayers are no longer required to begin the entire OIC process again, eliminating re-computations of financial statements and valuations.

Notwithstanding improvements, much work remains. The entire process is too long and offers continue to consume inordinate amounts of resources to collect relatively insignificant amounts of tax dollars. Collection rates of twelve- to fourteen- cents on the dollar remain, second and third requests for additional or updated information persist, and general frustration with the program thrives. Taxpayers deserve faster answers, fewer requests for less redundant information, and a higher rate of return on the resources dedicated to the program.

The staggering volume of submissions is part of the challenge. Offers submitted by taxpayers that are aware that collection efforts are suspended during pendency of an offer comprise one component of the increased volume in OIC submissions. Others result from advertising that touts a taxpayer's right to settle cases for pennies on the dollar.

Currently, installment agreements outside of the OIC Program must be full pay, as it was decided that partial pay Installment Agreements required legal clarification. Prior to that decision, fewer offers and more partial pay Installment Agreements existed. Better tracking and annual refund capture procedures are in effect for Installment Agreements. The Government Accounting Office and Taxpayer Advocate Service have recommended that partial pay Installment Agreements may be a more efficient method of collection.

Beyond the problematic time and dollar issues, an improved follow-up program is needed. Accepted offers require that a taxpayer remain compliant for five years. A formal monitoring program is needed to enforce this provision.

Lastly, a program is needed to track the underlying reasons for the substantial increase in the number of taxpayers utilizing this program in the first place. What factors are giving rise to the large numbers of offers submitted and what changes can be made to reduce such demand?

ISSUE THREE: RECOMMENDATIONS

Addressing the conditions that source a taxpayer's need to enter the OIC Program should be a condition precedent to any compliance agreement. For example, a taxpayer entering the program due to nonpayment of employment taxes should be required to make employment tax deposits subject to strict enforcement and should be tracked to ensure compliance.

Attention must also be given to the taxpayer. If actions can be undertaken to prevent future problems, such actions should become a condition precedent of the five-year agreement. Entry into the program may be sourced in conditions created by regulations or result from taxpayer ignorance or inattention.

Further, we recommend the following:

- Track taxpayers whose offers were rejected to determine the amount of tax, if any, ultimately collected;
- Automate the five year post-offer tracking;
- Compare the centralized offer programs for management best practices, such as progress tracking, and standardize across Service Centers;
- Provide taxpayers with an information number to the site working his or her case;
- Develop a process by which to resubmit claims that are processable but which were returned unprocessable;

- Compare current and previous two years agreed offers with the offshore credit card database (and review anomalies);
- Provide education program requirements as a condition precedent to settlement agreements;
- Continue working to reduce cycle time;
- Evaluate the penalty structure to determine a proper balance between incentives to file and timely pay versus unreasonable build-up of debt that overwhelms the taxpayer.
- Determine if taxpayers offering unrealistically low amounts received professional advice to do so, and from whom.

The SBSE Subgroup further supports the following initiatives:

- The proposed user fee;
- Identification of paid Form 656 preparers through a signature line on the application;
- The ability of the taxpayer to enter into partial payment installment agreements; and
- Modify the OIC application such that the filing of full pay returns is less likely.

ISSUE FOUR: THE K-1 MATCHING PROGRAM

The SBSE Subgroup is in full support of a K-1 Matching Program. We commend the Service for recognizing the need for such a project. Substantial income is sourced in Forms K-1, $800 billion was reported on 20 million K-1 returns. The K-1 Matching Program is a key compliance program that began in earnest during fiscal year 2002. The IRS has begun the process of matching K-1 information to taxpayer returns, matching Form K-1 amounts with the corresponding amount entered on a taxpayer's income tax return. What was initially conceived as a simple program has evolved into an income verifying and difference reconciliation program.

Much time and money is expended entering Form K-1 data. When the Form K-1 amount and the corresponding Form 1040 amount do not match, creating a mismatch, a CP notice is generated. The Form K-1 information is then compared to the return - by hand. Over half of the mismatches generated by this

process are "screened out" as correctly filed by humans who review the return in toto and identify items found elsewhere in the return that plausibly explain the mismatch. Of the mismatches remaining, perhaps half ultimately result in no change. Each of the steps identified herein requires highly trained personnel generating significant costs. Accordingly, this program should be automated as soon and as much as possible.

For a K-1 Matching Program to be successful, the goal of the Program must be clearly delineated. Is it a matching program, or is it an income verification and reconciliation program? The type identified is extremely important. At the time this report was written, tabulation of the first notice results was underway. These results should indicate if the income gap is sourced in omissions or inaccurate reporting. Also problematic is the fact that varieties of due dates cause many taxpayers to estimate or omit K-1 income that is not received by the filing date.

ISSUE FOUR: RECOMMENDATIONS

Prior to implementing a verification/reconciliation program we recommend:

- Developing an appropriate program based on the results of notices sent this year;
- Examining the effect that changing due dates to March 15 would have on compliance for returns on which K-1's are includable;
- Enter amended Form K-1 data when received;
- Utilize automated function as much as possible and minimize human resources that could be utilized elsewhere;
- Move forward with the matching of K-1s on returns where K-1's have been omitted, and track the tax collected on underreported and unfiled returns;
- Rewrite Form K-1 generating instructions to provide for uniform handling of issues such as basis, partner expenses, elections, and other complicating factors;
- Redesign K-1 and Schedules E and SE to facilitate ease of computer verification with complete *e-file* compatibility.

Absent implementation of the above recommendations, we recommend the K-1 Matching Program be limited to verifying the inclusion/omission of Form[s] K-1 on a taxpayer's income tax return.

ISSUE FIVE: IRS/PRACTITIONER FOCUS GROUPS

We commend the IRS on the recent series of Focus Group Sessions conducted as part of the Nationwide Tax Forum Program. Approximately forty practitioners were asked to provide input on issues of their choosing as well as issues the Council was considering. The issues covered included:

- *e~file;*
- K1 Matching;
- Offer-in-Compromise;
- IRS successes, such as the improved phone services;
- Overall opinion of the IRS since reorganization.

The practitioners who participated in the Focus Group Sessions opined that the IRS is headed in the right direction albeit expressing support for a higher audit rate. At the same time however, they expressed frustration with confusing mailing addresses and mailing address changes, and communication problems resulting from routing phone calls across the country.

The members of the SBSE Subgroup wish to thank the Commissioner for allowing them to participate in and facilitate these sessions.

ISSUE FIVE: RECOMMENDATIONS

The SBSE Subgroup believes that the Focus Groups could be improved by:

- Increasing the number of practitioners involved in each session;
- Including the Focus Group Sessions in the Forum Schedule/Agenda;
- Not requiring attendance to be the responsibility of IRS staff; and
- Conducting sessions in central meeting locations contiguous to Forum seminars and visible to attendees.

These recommendations are meant to increase the ability of practitioners to be heard. We strongly support continuing these Focus Groups in the future.

INTERNAL REVENUE SERVICE
ADVISORY COUNCIL

LARGE & MID-SIZE BUSINESS
SUBGROUP REPORT

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OCTOBER 18, 2002

LARGE & MID-SIZE BUSINESS
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I. INTRODUCTION

The LMSB Subgroup, consisting of professionals who represent large and mid-sized businesses and in-house tax counsel at large multinational corporations and an association, has been busy since April, 2002 participating in three separate multi-day meetings in Washington D.C. and several conference calls with Large & Mid Size Business (hereinafter "LMSB") Operating Division executives and personnel. In addition, as discussed in the General Report, many subgroup members have participated in Nationwide Tax Forum focus groups across the country. The members are most grateful for the time devoted by the executives and personnel of LMSB and the staff of the Office of National Public Liaison. Without their time and assistance, the subgroup would not have had as meaningful a year. While not exhaustive, the following identifies the primary issues reviewed and associated recommendations made by the LMSB Subgroup this past year.

II. Issues and Recommendations

A. LMSB Operations

1. Workload Realignment/Compliance Risk Assessment

ISSUE: During fiscal year 2001, the Large & Mid-Size Business Operating Division conducted a strategic assessment of its taxpayers to determine how best to deploy its workforce, prioritize its resources, track issues, and measure compliance. This initial assessment utilized a compliance risk scoring method to establish the "top tier" taxpayers that present the largest compliance risks. Among other things, the assessment validated anecdotal evidence of a large increase in pass-through entities. Using the information gained from the assessment, LMSB has been re-deploying its workforce in accordance with the "top tier" determination. Pursuant to the 2001 study, LMSB doubled partnership entity audit coverage during fiscal year 2002 and has projected an increase in audit coverage for fiscal year 2003 of two and three-tenths percent. LMSB's audit

coverage of non-large cases, including corporations, Form 1120S corporations, and non-coordinated Industry cases, improved to fourteen and six-tenths percent.

RECOMMENDATION: The LMSB Subgroup continues to be concerned with the low audit coverage of non-large case taxpayers, which we believe encourages non-compliance among mid-size businesses. However, we are highly encouraged by LMSB's use of the strategic assessment to assist in determining for the first time in years its actual audit coverage. We are also encouraged that LMSB appears initially to have used the results of the assessment to determine personnel needs and audit issues, provide immediate pass-through entity training, and shift newly trained auditors from large-case to pass-through entities. This should help LMSB improve its audit coverage of mid-sized businesses. The LMSB Subgroup believes that this type of assessment should be ongoing, and encourages LMSB to continue to utilize such assessments in the future. Moreover, we encourage LMSB's involvement and participation in future National Research Program iterations as applicable to businesses and to utilize NRP results for purposes of refining its assessments.

2. Post-Filing Processes

LMSB has initiated a number of processes to facilitate efficiency in the post-filing process. These processes include Limited Issue Focus Exam (hereinafter "LIFE"), a redesigned claims process, and a myriad of items that previously were tested in pilot programs, including Pre-filing Agreements, LMSB Fast Track Resolution (hereinafter "Fast Track"), Industry Issue Resolution, and Comprehensive Case Resolution (hereinafter the "Tested Processes"). In addition, until earlier this fiscal year, LMSB engaged teams to discuss and redesign the entire post-filing process.

A. LIFE

ISSUE: LIFE, currently under design in LMSB, is a new process, centered around the concept and issues of materiality, which would be available to certain taxpayers that have been

cooperative with the IRS in the past and whose tax returns reflect only a limited number of material and potential issues. Using guidelines established by LMSB regarding issues and materiality, a Team Manager, with respect to each taxpayer participating, would: (i) agree to an audit plan in which the IRS would audit only certain material issues based on a materiality threshold; (ii) with the taxpayer, agree not to file any claim below the threshold; and (iii) complete the audit within a shortened and specified time-frame. However, as part of implementing a LIFE audit plan, we understand that the Team Manager may require exceptions to the agreed upon materiality threshold.

RECOMMENDATION: The LMSB Subgroup strongly favors LIFE because: (i) the program acknowledges the past cooperation of certain taxpayers and their resulting lower audit risk; (ii) enables (and we recommend) the "freed-up" resources to be allocated to non-cooperative taxpayers and to groups of taxpayers for which the IRS has not had traditionally high audit coverage (e.g., mid-size taxpayers); and (iii) focuses exams on material issues. The subgroup strongly encourages LMSB to make no exceptions to the agreed upon materiality standard in a LIFE audit because such exceptions would dilute the program's above-described benefits and accordingly, reduce a taxpayer's willingness to participate. Moreover, similar to our recommendation below, we recommend that a Team Manager engaged in a LIFE audit be empowered to resolve and settle cases.

B. CLAIMS REDESIGN

ISSUE: Although LMSB's redesign of the claims process is in the early stages, the Operating Division's initial reaction is to create "two paths" for claims, while continuing to permit taxpayers informally to make claims with the audit team, rather than formally on an amended return. The first path would be for those claims raised within six months of the beginning of the audit, and the second path for claims made after expiration of the time period applicable to the first path. Claims under the first path would be audited and resolved by the audit team. Claims under the second path would be handled on a parallel track and reviewed outside the audit plan time frames on a resource available basis.

RECOMMENDATION: The LMSB Subgroup agrees with LMSB's early stage design. However, as LMSB continues the redesign process, care should be taken not to allow final design requirements to be an excuse for an audit team to audit claims only on a resource available basis. Such a practice would potentially defer, even preclude resolution, or negatively impact the beginning of the next exam cycle. In addition, the subgroup believes it is important for LMSB and the IRS to institutionalize the claims of non-large case taxpayers under audit so that such claims: (i) also are subject to the "two path" process; (ii) must be submitted to the auditor; and (iii) are prevented from being processed - or a refund granted - at a Service Center without the approval of the Team Manager.

C. THE TESTED PROCESSES

ISSUE: As discussed above, LMSB has instituted a myriad of Tested Processes. In the Industry Issue Resolution pilot program, LMSB selected seven issues for consideration, and the IRS published guidance on six of the seven issues selected. By all accounts, the program has been very successful and was made permanent in Notice 2000-20. For the year 2001-2002, LMSB has selected seven issues for Industry Issue Resolution.

The Pre-filing Agreement Program is designed to permit taxpayers, before filing a return, to resolve the treatment of an issue that would otherwise be likely to give rise to dispute in a post-filing examination. The Pre-Filing Agreement Program is intended to produce agreement on factual issues and apply settled legal principles to those facts. A Pre-filing Agreement is a specific matter closing agreement and, as such, resolves the subject of the Pre-filing Agreement for a tax period or periods. Execution of a Pre-filing Agreement is intended to resolve issues prior to filing, thus permitting taxpayers to avoid a portion of the costs, burdens, and delays that are frequently incident to post-filing examination disputes. In its Pre-filing Agreement pilot, LMSB accepted twelve applications of nineteen received, and entered into ten Pre-filing Agreements. LMSB spent thirty-seven and two-tenths days, on average, reviewing

the six Pre-filing Agreements entered into the first year of the pilot and an average of 166-1/10 days to complete each of the six agreements. An average of forty-four and one-half days was spent reviewing the four Pre-Filing Agreements entered into the second year of the pilot and an average of 482-3/4 days to complete each Pre-filing Agreement. The above statistics do not include time spent reviewing unaccepted or withdrawn applications. The process has required a great deal more time than anticipated, has resulted in redirecting resources away from basic audits, and has produced relatively few agreements. However, both taxpayers who entered into Pre-filing Agreements and LMSB generally believe the program is promising and provides benefits. The Pre-filing Agreement Program has now been made permanent.

To date, after two years, the Comprehensive Case Resolution pilot has resulted in but one case having been addressed and resolved. Lastly, the Fast Track Program has an Appeals option and a mediation option. The Appeals option has been praised highly and has resulted resolution of cases in seventy-one days on average. To date, no taxpayer has applied to use the mediation option, although the IRS and taxpayers have used mediation processes in the past successfully. The Fast Track Program is in the process of being made permanent by the IRS.

RECOMMENDATION: We believe that Industry Issue Resolution has been the most successful of the Tested Processes and strongly encourage LMSB and the IRS to continue using this useful program. Further, the subgroup believes that the Pre-filing Agreement Program has not been successful, largely because the program requires an intensive use of resources by the IRS and the taxpayer. We also have concerns regarding the program's applicability to non-large case taxpayers, and the potential costs to both taxpayers and the IRS associated with revisiting issues already addressed in a Pre-filing Agreement due to a closing agreement procedure that is applicable only to a particular tax period or periods. However, we encourage LMSB to review whether the Pre-filing Agreement Program can be redesigned to address these issues. The Fast Track Appeals Program should be emphasized and continued. For the time being, we encourage LMSB to continue marketing the Fast Track Mediation Program. However, if this

mediation program is not utilized soon, the subgroup encourages LMSB to end the program. The Comprehensive Case Resolution Program should be dropped due to its lack of success. Lastly, as we indicated last year, we believe that existing processes, such as Delegation Orders 236 and 246 and the Accelerated Issue Resolution, should be given new life, stressed to the same extent as the new processes, and measured to determine their effectiveness. The results of these measurements should be publicly reported.

D. REDESIGN OF ENTIRE POST-FILING PROCESS

ISSUE: Until earlier this fiscal year, LSMB had engaged a team and an outside facilitator to review and redesign the entire post-filing process. However, due to funding shortfalls, LMSB is no longer engaging the facilitator and the team has been disbanded.

RECOMMENDATION: The subgroup strongly encourages LMSB to recommence its post-filing process redesign efforts notwithstanding current budget constraints, and urges LMSB to seek assistance from its stakeholder groups and the IRSAC in redesigning the process. As part of this redesign, we encourage LMSB to consider formulating the redesigned process around "issues" and the "concept of materiality" (i.e., concepts that LMSB is addressing in LIFE) to streamline the post-filing process and "free-up" additional resources. A redesigned post-filing process is critical to assisting the IRS with limited resource allocations. With respect to non-large case taxpayers, the subgroup strongly encourages LMSB to institute procedures mandating that the agent establish a written audit plan with an estimated completion date prior to commencement of an audit.

3. LMSB BUDGET

ISSUE: Based on actuarial data, LMSB estimates that it will lose between 150 and 200 agents, and a total of 250 in fiscal year 2003. LMSB also estimates that it will continue to lose a substantial number of agents and employees across the next nine years. However, LMSB has the funding to replace less than thirty percent of those agents in fiscal year 2003, and its current budgetary situation makes it unlikely the Operating Division will be able to replace the substantial number of departing agents and

employees in future years. The subgroup believes that a compliance crisis will arise without these agents, particularly with respect to mid-size taxpayers.

RECOMMENDATION: LMSB has developed a multitude of processes to reduce the personnel needed for audits. (*See* II.B. above). However, given the significant number of projected agent and employee losses, these processes will provide a mere band-aid for the problem. Congress should fund LMSB adequately for personnel needs and the development of training programs for new and existing employees.

4. TRAINING AND PROFESSIONAL DEVELOPMENT

ISSUE: LMSB's goal is to become "a World Class Organization by promoting a culture of continuous learning." As part of the program in support of this goal for fiscal year 2002, LMSB has offered many training and educational programs on pass-through entities and tax shelters. We note that as part of this training, LMSB conducted forty-five Centra sessions (a web based software that runs on the Internet), twenty interactive video sessions, and many traditional classes around the country.

RECOMMENDATION: The LMSB Subgroup is gratified that the LMSB Operating Division adopted the recommendation made by the IRSAC in its 2001 Public Report that more technology be utilized in training, including the use of Centra. While LMSB has made progress in its training and development programs, we believe that it should continue to stress education, including training through technologies that will enhance distance learning. Further, the LMSB Subgroup recommends that LMSB establish educational programs that are mission-focused, customer-driven, and future-oriented (i.e., utilize the Compliance Risk Assessment to determine what and where to train). Lastly, the LMSB Subgroup encourages the LMSB Operating Division to provide achievement-based incentives for training and development programs.

5. SERVICE CENTER TRANSITION

ISSUE: Last year, the IRS transitioned LMSB taxpayers to Service Centers located in Ogden, Utah and Cincinnati, Ohio. Specifically, taxpayers will file Forms 1120, 1120S, and Forms 1065 at

the Ogden Service Center while Forms 941 will be filed at Ogden and Cincinnati Service Centers according to geographical location. Excise Tax returns, Forms 720, will continue to be filed at the Cincinnati Service Center regardless of geographical location.

RECOMMENDATION: While the transition by all accounts has been successful, the subgroup encourages LMSB to continue to monitor for issues that may arise.

B. Tax Shelters

1. WHAT IS A LISTED TRANSACTION?

ISSUE: LMSB's strategy with respect to tax shelters has centered on disclosure and transparency, particularly with respect to transactions that the IRS has specifically identified as "abusive." In a series of notices and rulings, LMSB has identified certain transactions with respect to which disclosure is mandatory by including them on a list (i.e., a "Listed Transaction"). Moreover, taxpayers and promoters have certain disclosure obligations with respect to a transaction which the taxpayer participated in or the promoter promoted if such transaction is "substantially similar" to a Listed Transaction. We note that the disclosure initiatives have allowed the IRS to identify "promoters" of tax shelter transactions and to take steps to compel disclosure.

RECOMMENDATION: The subgroup supports LMSB's efforts to stop abusive transactions, alert taxpayers to transactions about which there are concerns, and foster transparency. We also commend LMSB for the voluntary tax shelter disclosure initiative that ended April 23 of this year. However, the subgroup is concerned that not all Listed Transactions reflect "settled law" and that disclosure rules imposed with respect to "substantially similar" transactions may act as a trap for the unwary. Thus, we recommend that the IRS proceed with caution in imposing harsh penalties on taxpayers engaged in a transaction that was not in conflict with "settled law" at the time the transaction was entered into or reported on the federal income tax return.

2. TAX ACCRUAL WORKPAPERS

ISSUE: Earlier this year, the IRS issued guidance regarding the circumstances under which the IRS can request a taxpayer's tax accrual workpapers when a listed transaction is involved. In summary, for tax returns filed after June 30, 2002, if a taxpayer fails to disclose a listed or "substantially similar" transaction, the IRS can request the taxpayer's tax accrual workpapers, subject to certain safeguard procedures. However, if the taxpayer has disclosed the listed or "substantially similar" transaction, the IRS should request the taxpayer's tax accrual workpapers only with respect to a listed or "substantially similar" transaction. For tax returns filed prior to July 1, 2002, if a taxpayer was obliged to disclose the transaction and failed to do so, the IRS would limit its request to workpapers pertaining solely to the Listed Transaction. The IRS and LMSB have been developing a question and answer Revenue Procedure to address certain outstanding issues regarding this guidance.

RECOMMENDATION: The subgroup strongly believes that additional guidance is needed with respect to acquired entities. If an acquired entity fails to disclose prior to an acquisition, we believe it inappropriate for the IRS and/or LMSB to require the Acquiror to disclose its tax accrual workpapers, unless the Acquiror is given sufficient time following the acquisition to disclose and does not do so. Further, the disclosure obligation also applies to transactions that are "substantially similar" to Listed Transactions. The subgroup believes strongly that the definition of "substantially similar" should be refined such that the rules do not operate as a trap for the unwary or as grounds for delaying resolution of audit issues.

3. RESOLUTION STRATEGY PROCESS FOR LISTED TRANSACTIONS

ISSUE: LMSB is discussing various strategies for resolving cases that involve Listed Transactions.

RECOMMENDATION: The subgroup feels strongly that any resolution should not reward taxpayers that participated in abusive transactions or failed to disclose their participation early. Further, any resolution strategy should not *de facto* penalize taxpayers that did not participate in abusive transactions (i.e., result in a favorable settlement to non-disclosing or late disclosing taxpayers). Lastly, we encourage the IRS and/or LMSB to utilize all means available to penalize promoters, including the possibility that practice before the IRS be restricted.

C. Authority Issues within LMSB/Rules of Engagement vis-a-vis Counsel/Measurement of Audit Team/Team Manager Effectiveness

ISSUE: The subgroup believes strongly that many audits are not resolved in a timely manner because it is unclear when the Team Manager has ultimate authority vis-a-vis Technical Advisors, Specialists, Chief Counsel, and others. The absence of clear management guidelines (including the guidelines outlined in the Internal Revenue Manual) has contributed to the length and uncertainty of the post-filing process. Moreover, the subgroup believes that it is critical for LMSB to establish measures regarding the effectiveness of Team Managers and auditors. To date, we are unsure whether the measures established by LMSB are effective because such measures have not yet been disclosed.

RECOMMENDATION: The subgroup believes strongly that the Internal Revenue Manual and the Regulations should be redrafted to clarify that the Team Manager has the authority to resolve and settle a case, subject to a short, written list of discrete exceptions. These exceptions should include Coordinated Issues, but only when designated and disclosed in writing to taxpayers. Further, the subgroup recommends that LMSB's measures require that a Team Manager and his/her team be evaluated regarding how he or she exercises authority and resolves cases. Moreover, the subgroup believes strongly that an empowered Team Manager is the key to a successful LMSB and the key to LIFE and any redesigned post-filing process.

D. INTERNET WEB SITE

ISSUE: LMSB is finally part of the main IRS Web site, irs.gov. The subgroup believes it important that LMSB's site be user-friendly and interactive.

RECOMMENDATION: The subgroup recommends that LMSB's portion of the IRS Web site be more user-friendly, which should include improving the "search" function and providing easier access to specific regulations and other guidance. To provide a more interactive Web site, we believe the site should be a portal: (i) for filing, including: Coordinated Issue Papers, pre-filing agreement procedures, Forms S-4, Forms 966, S status elections, check-the-box elections, pre-filing agreement forms, and ruling requests; and (ii) for checking taxpayer accounts and filing status.

E. GLOBALIZATION/INTERNATIONAL

1. COMPETENT AUTHORITY

ISSUE: The bottleneck that exists in resolving Competent Authority Process issues remains a problem. The average time required to process a competent authority case in fiscal year 2002, has been 642 days. While this continues a five-year trend reducing processing time from the high of 807 days in fiscal year 1997, the subgroup believes there is room for further improvement. Part of the challenge is that LMSB has only thirty-four people to resolve more than 500 extremely complex cases, involving numerous foreign governments.

RECOMMENDATION: To assist in resolving this bottleneck, LMSB should continue to increase its staff and utilize creative agreements, such as the November 2000 Agreement with the United Kingdom. Further, we applaud LMSB for attempting to streamline the process through the updated Competent Authority Procedure, Rev. Proc. 2002-52. Moreover, the subgroup encourages the IRS to leverage the thoughts of taxpayers contemporaneously during the process, rather than through intermittent consultation. For example, the IRS should develop a mechanism by which a taxpayer may provide factual assistance contemporaneous with IRS' discussions with another country's competent authority.

2. TRANSFER-PRICING DOCUMENTATION

ISSUE: In recent years, transfer-pricing documentation has become increasingly important under the laws of many jurisdictions. Under the laws of the United States and other countries, taxpayers may be subject to documentation-related penalties under section 6662(e) of the Internal Revenue Code. As a consequence, taxpayers often struggle to understand and satisfy differing transfer-pricing documentation requirements in each jurisdiction. To help reduce the complexity, the Pacific Association of Tax Administrators (hereinafter "PATA") has tentatively prepared a unified set of documentation requirements that meet the applicable transfer-pricing documentation requirements for each of its member countries (the U.S., Canada, Japan, and Australia), permitting taxpayers to avoid penalties in those jurisdictions.

RECOMMENDATION: While the subgroup applauds LMSB's efforts with regard to the tentative documentation package produced by PATA, we encourage LMSB to ensure that the final set of unified requirements eliminates any uneven requirements of the PATA members. Further, since the transfer-pricing regulations have been in existence for some time, LMSB should review the entire process and documentation requirements, and determine what is and what is not important. Moreover, the subgroup encourages LMSB to establish simple documentation requirements for small taxpayers, small transactions, and smaller units of larger taxpayers, based on a materiality standard.

INTERNAL REVENUE SERVICE ADVISORY COUNCIL

WAGE & INVESTMENT SUBGROUP REPORT

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OCTOBER 18, 2002

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INTRODUCTION

The mission of the Wage & Investment (hereinafter "W&I") Operating Division is to make compliance with the tax law easier for the approximately 122 million taxpayers served by the Division. We are pleased that the W&I leadership continues to recognize the IRS goal of providing top-quality service to taxpayers in its Strategic Plan and Assessment. A great deal of planning and energy continues to be focused on developing strategies and systems that meet the demands of an extremely diverse customer base for timely, accurate, efficient, and automated services.

Compliance is the current watchword. As long as more than twenty-five percent of the taxpaying community believe they can cheat the "tax man," the viability of our voluntary tax system will be at risk. While IRS modernization and staffing efforts continue, it is clear that until information systems are modernized and full staffing is achieved, the integrity of our tax system will continue to erode.

Issue One: Status of the Stakeholder Partnership Education and Communication Program

The Stakeholder Partnership Education and Communication Program (hereinafter "SPEC") that was established in October, 2000 reflects a significant restructuring of the previous IRS taxpayer education and electronic field functions. As described in the Concept of Operations (hereinafter "CONOPs") that set forth the blueprint for SPEC, the program is designed to achieve a model for delivering the majority of its taxpayer assistance and outreach initiatives through community-based partnerships.

As the IRSAC noted in its last Public Report, SPEC has encountered funding and staffing shortfalls that interfere with its ability to achieve the strategic initiatives set forth in its CONOPs. It is our understanding that, as of August 2002, SPEC was neither fully funded nor staffed, despite expectations that steady progress would yield full staffing by fiscal year 2004. In a July conference call, W&I Subgroup members learned that unforeseen budgetary expenditures, i.e., the rate reduction credit, accounted for a portion of SPEC's funding shortfall. These - and other off-budget costs - forced the IRS to shift needed resources away from and to certain under-funded SPEC initiatives.

Despite these difficulties, however, SPEC has made significant progress in establishing community-based partnerships. Since its inception, SPEC has initiated or supported community-based Earned Income Tax Credit (hereinafter "EITC") outreach and income tax assistance programs in more than twenty-one cities, numerous national affinity organizations, corporations, Indian tribal nations, and volunteer organizations. Current examples include the Welfare-to-Work Partnership, a coalition of 20,000 corporations committed to hiring persons moving off welfare, and partnerships with the National League of Cities, National Education Associations, Cherokee Nation, Kroger, Annie E. Casey Foundation, FDIC, and Community Action Agencies, to provide individuals with EITC education and assistance. We applaud SPEC for its efforts in these areas, as well as for its initiatives to partner with AARP, Military VITA, UPS and others during the past filing season for purposes of conducting Train-the-Trainer programs. These programs facilitate multiple levels of training for volunteer income tax return preparers.

Because SPEC needs additional resources to continue its progress in establishing and monitoring the work of community-based partners, as well as meeting other strategic objectives, we remain concerned about SPEC's lack of funding and staffing. Indeed, given its current operational status, we strongly question whether it is feasible for SPEC to achieve its many strategic objectives within established time frames.

Further, we are concerned that, to date, there has been insufficient focus on measuring program success. For example, it is unclear what effect increases in community-based partnerships have had on the quality and quantity of services provided by SPEC. The effect such increases have had on customer satisfaction is likewise unclear. It is also uncertain whether SPEC has evaluated the effectiveness of its partners and, if so, the results of such evaluations. Although SPEC is developing "balanced measures," i.e., customer satisfaction and partner effectiveness, measures it plans to utilize in making funding and resource-allocation decisions, as of the writing of this report, the subgroup did not have access to such measures. Further, we were unable to obtain sufficient information to otherwise evaluate SPEC's progress in achieving the objectives set forth in its CONOPs, and it is unclear whether SPEC itself has made such an evaluation to

date. The need for measuring program success is apparent. Not only will SPEC allocate resources based on the results of such evaluations, but Congressional-funding decisions likely will be based on the perceived success or failure of SPEC's various program objectives.

Finally, as we explained in the July conference call discussed above, we are concerned that funding allocation decisions ultimately could undermine certain other strategic IRS objectives. For example, if SPEC continues to reduce VITA sites and no longer provides computers to VITA volunteers, paper returns may increase and some individuals may not file returns at all, i.e., due to the loss of convenient VITA sites.

Issue One: Recommendations

We applaud SPEC for the significant progress it has made in establishing community-based partners, and we encourage continued focus on strengthening current and establishing new partnerships for providing taxpayer assistance and education. We are concerned, however, that SPEC's diminished funding and staffing inevitably will curtail its progress on program initiatives. We therefore urge W&I to make a concerted effort to obtain full funding and staffing for SPEC in fiscal year 2003.

Further, we strongly encourage SPEC to articulate the manner in which it measures program success. Once the success of SPEC's program initiatives has been evaluated, we urge the results be shared with the IRSAC so that the Council may better assist SPEC in achieving these initiatives. Further, given the status of SPEC's current funding and staffing, in confluence with the likelihood that such shortfalls will continue, we view the initiatives set out in SPEC's CONOPs as unrealistic. Therefore, we encourage SPEC to revise program initiatives to more accurately reflect its current and likely future operational status.

Finally, we urge SPEC and IRS Senior Management to work together for purposes of ensuring that implementation of SPEC's program initiatives does not harm other important agency-wide goals, i.e., consequential increase in the number of non-filers and paper returns. We believe that focusing on measuring program success may obviate this concern to some extent, and should enable W&I to better coordinate its

strategic objectives and thus avoid such conflict. We therefore strongly recommend that SPEC reconsider its program initiatives in light of IRS strategic initiatives, and take steps in advance to ensure that the measures it adopts do not undermine system-wide objectives.

Issue Two: Meeting the Congressionally Mandated Goal for Electronically Filed Returns

By Congressional mandate, eighty percent of all returns are to be filed electronically by tax year 2007. When electronic filing began, a special modem and certain software were required. As a result, only volume filers were able to comply with the requirements. Today, the IRS recognizes that while ninety percent of all tax data exists in some electronic format, not all such data can be transmitted electronically. Even as the Service expands *e-file* capability, and adds to the inventory of forms and schedules available for electronic filing, the corresponding number of electronically filed returns has not grown by leaps and bounds. The Service continues to expand electronic filing capability. For example, partnership returns (Form 1065) now can be filed electronically. The Form1120 family is expected to be on line for tax year ending 2004. However, unless the Service can develop a better understanding with respect to why more practitioners and individual taxpayers do not *e-file*, the Congressional mandate will not be met.

Issue Two: Recommendations

We encourage the Service to continue meeting with practitioner organizations. However, as with private business, the Service must reach out to the customer. In this application, practitioners and individual taxpayers are the customers at issue. However, as discussed in the General Report, particular attention should be focused on practitioner groups to accelerate electronic filing at rates that will reach the Congressionally mandated goal, as the IRSAC believes that efforts focused on practitioners and practitioner groups will yield greater benefits than efforts directed at motivating/incentivizing individual taxpayers. Accordingly, marketing materials aimed at individual taxpayers are not generating sufficient interest in electronic filing. We recommend that the Service assemble focus groups and meet with volume practitioners

who do not file electronically to discuss why such practitioners do not *e-file*, and, in partnership with practitioner groups, develop measures to mitigate such impediments and/or resistance.

Issue Three: Barriers to Electronically-Filed Returns

A known barrier to *e-filing* is the amount of data entry required to create an electronic return as opposed to preparing a paper return in which a preparer need only enter wage and withholding information. Upon completing preparation of a paper return, a preparer merely attaches a copy of Form W-2 or Form 1099R to the return. In the alternative, to file electronically, a preparer must enter data in all boxes of Form W-2 or Form 1099R, including the name, address, city, state, zip code, and employer identification number of the issuer. Further, after entering this data, an electronically filed return can be rejected merely on the basis of a bad zip code.

Issue Three: Recommendations

We recommend that the IRS reduce the amount of input required for electronically filed returns. Tele-filed returns require only an employer identification number, and we recommend this same standard be applied to electronically filed returns.

Issue Four: Under Utilization of Preparer Penalties

The W&I Operating Division may exercise discretion with respect to directing compliance resources; as between individual taxpayers, paid preparers, or both. Compliance efforts directed to individual taxpayers include the manual and/or electronic screening of returns. Screening may result in the issuance of math error notices or notices of correspondence or in-person exams. Criminal sanctions may also be imposed. Of the approximately nineteen million Earned Income Credit (hereinafter "EIC") returns filed annually, approximately one million math error notices or notices of examination are issued. Of 125 million individual returns filed each year, approximately 600,000 are subject to examination. During the past three years, 130 criminal investigations have been initiated, resulting in 116 convictions of EIC-related fraud schemes.

Sanctions, both civil and criminal, may also be imposed on paid preparers. Civil penalties range from fifty dollars for infractions such as failure to sign a return, failure to provide the taxpayer with a copy of his or her return, and failure to retain a copy of the return on file. *See* Internal Revenue Code section 6695(a)-(f). A $250 penalty may be assessed for negligence in completing a return, and $1,000 may be imposed on preparers who deliberately or willfully prepare erroneous returns. Further, in 1997, Congress enacted legislation that permits assessment of a $100 penalty for failure to document due diligence in preparing an EIC return. *See* Internal Revenue Code section 6695(g).

An EIC compliance study conducted in 1999 reported that sixty-eight percent of all EIC returns were prepared by paid preparers. Results from an earlier study indicated that non-enrolled preparers generated nearly twice the error rate of enrolled preparers on EIC returns; indeed, the error rate for paid preparers exceeded the error rate for self-prepared returns. Each year, more than one million individuals prepare tax returns for a fee. Moreover, at least two-thirds of this group is comprised of non-enrolled preparers; that is, these preparers have demonstrated no proficiency with respect to licensing, training or minimum skill requirements. In fact, there is no requirement that a paid income tax preparer be fluent in English.

Issue Four: Recommendations

Based on these facts, members of the W&I Subgroup are very concerned about the relative paucity of preparer penalties imposed by the IRS each year. For example, in fiscal year 2001, a mere 248 paid preparers were assessed the $100 penalty for violating due diligence requirements that attach to EIC returns. This number looks startling small relative to the one million EIC returns subjected to math error notices and/or examination procedures each year, as well as the historically high non-enrolled preparer error rates. Assessment of other preparer penalties also appears quite low, given that more than sixty-five million returns are prepared by paid preparers nationwide each year. Only 3,000 preparers were assessed a fifty dollar penalty under Internal Revenue Code section 6695(a)-(f). Slightly more than 4,000 preparers were assessed

the $250 penalty for negligent return preparation, and the $1,000 penalty for deliberate or willful return errors was imposed on slightly more than 3,000 preparers.

Criminal sanctions imposed on paid preparers also appear quite low compared to reported error rates on EIC returns. Over the past three years, ninety-six criminal investigations were initiated to look into preparer schemes. Investigators identified 6,854 questionable returns and fifty-three preparers were convicted of income tax fraud.

We understand that W&I has made careful assessments regarding the return on investment (e.g., recovery of tax dollars) with respect to allocating resources to individual taxpayer compliance as compared to investing these resources in preparer compliance. However, the return on current allocations, given the extremely low rate of sanctions for preparer malfeasance, creates the perception in the non-enrolled community that negligent or willful errors on returns carry very limited risk of sanctions. We urge that W&I review its current allocation of resources and its strategies for imposing sanctions against non-enrolled, paid preparers. We further recommend that W&I involve the IRSAC in this planning process during the coming year.

ISSUE FIVE: BALANCING UTILIZATION OF RESOURCES AMONG COMPLIANCE, EDUCATION, AND OUTREACH

Following the restructuring of the IRS, compliance with the tax law has been identified by both the IRS and the practitioner community as a key focal point. Ensuring that compliance is fair and consistent is an important strategy for enhancing voluntary compliance. However, the subgroup also believes that taxpayer education and outreach, especially to W&I taxpayers, is a key strategy to enhance voluntary compliance. Accordingly, the subgroup recommends that resource allocation, including employees as well as technology, should be balanced among compliance, education, and outreach.

Issue Five: Recommendations

We appreciate the time and effort that IRS personnel have committed to brief this subgroup on specific initiatives and programs, which impact W&I compliance, education, and outreach. While we support these programs and initiatives, we recommend certain changes that we believe will better achieve the IRS mission of providing America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all. More specifically, we recommend that W&I maintain the high priority status identified to the three projects below, subject to certain changes, as follows:

(1) Enhancement of Service-wide Electronic Research Project/Automated Customer Service Representative Research Tools;

(2) Translation of Notices, Returns and Letters into Languages, Spanish in Particular; and

(3) Redesign of Notices and Letters to Increase Readability and Comprehension by Earned Income Credit taxpayers.

(1) Enhancement of Service-wide Electronic Research Project/Automated Customer Service Representative Research Tools.

Currently, the W&I Operating Division has dedicated resources to enhancing service-wide electronic research projects and automated Customer Service Representative (hereinafter "CSR") research tools. For example, W&I and the Taxpayer Advocate's Office (hereinafter "TAS") identified the impact on customer service and taxpayer compliance that results from the lack of training and/or effective screening tools for customer representatives who screen EIC cases and inquiries. To address this, the IRS retained a consultant to create an electronic online program, Online Tax Examiner Decision Support Tool, to assist customer service representatives both in campuses and area walk-in offices for the purpose of facilitating more accurate decisions and providing more accurate advice for EIC-related questions. This is a comprehensive, automated, online research program that will be available to telephone and walk-in-service

CSRs for the purpose of answering tax law and procedure questions regarding the EIC, head of household filing status, and dependency exemptions. The subgroup believes that such a resource will result in more accurate and timely advice to taxpayers who claim any of these tax benefits. Accordingly, this subgroup recommends the continued identification of W&I tax issues for which similar tools can be developed. However, the subgroup believes that such tools should not be limited to CSRs. Rather, the IRS should make such resources available to practitioners and taxpayers, preferably through the IRS Web site. Doing so, we believe, will have additional positive impact on compliance with the W&I tax law.

(2) Translation of Notices, Returns and Letters into Languages, Spanish, in Particular.

Currently, the IRS has a multilingual project, the aim of which is to identify languages, other than English, that

are the first language of sizable numbers of taxpayers. Further, the project aims at identifying key notices, forms,

and letters with which W&I taxpayers, for whom English is a second language, are likely to have contact. We

believe this project wisely recognizes the increasing populations of taxpayers who speak Spanish and for whom

English is a second language. While there may be differing views on English as a Second Language (hereinafter

"ESL") programs, to the extent the absence of tax notices, forms, and letters in languages other than English

impacts compliance and the payment of taxes, we recommend continuing efforts to identify the need for notices,

forms, letters, and returns to be made available in other languages.

As a first priority, this project has identified the need to translate notices, forms, and letters into Spanish, recognizing the increased number of taxpayers in the United States for whom Spanish is a first language. To the extent that there exists a sizable population of EIC-eligible taxpayers for whom Spanish is a first language, we believe this will assist compliance. We recommend that this project continue on its

timetable. We also support the approach currently in place that includes low-income taxpayer clinics serving non-English speaking clients in the process of identifying and prioritizing translations. However, we also recommend that the project place all translated forms on the IRS Web site, determine which notices and letters can be produced in double-sided format, with one side in English and the other in Spanish, and that notices, forms, and letters which cannot be so produced contain a line referencing a toll-free telephone number manned by Spanish speaking employees familiar with the notice, form, or letter.

We believe, however, that the project should adopt a faster timeline for translations of notices, forms, and letters into languages, other than English, which are first languages of sizable numbers of United States taxpayers. Recent census data indicates that other European languages, specifically French, German, Italian, and several Asian languages, specifically Chinese, Korean and Japanese, are the first languages of a sizable number of United States taxpayers. As with Spanish, we believe that translating notices, forms, and returns into these languages will prove cost-effective and have a positive impact on compliance by W&I taxpayers for whom English is a second language.

(3) <u>Redesign of Notices and Letters to Increase Readability and Comprehension by Earned Income Credit Taxpayers</u>.

The IRS has also undertaken a review of notices and letters affecting the W&I taxpayer population. We applaud IRS efforts to partner with and include segments of the professional and academic communities who work with W&I taxpayers, for assistance and advice regarding how to make notices and letters more understandable. We recommend that this review process continue.

We also make two specific recommendations that the subgroup believes will further compliance. First, the subgroup recommends that redesign of notices, forms, and letters utilize charts and flow charts to convey complicated ideas. Such techniques, we believe, will assist taxpayers with low-literacy skills or for whom English is a second language and should increase understanding of the tax law. Second,

the subgroup recommends that the IRS develop criteria with which to track changes in compliance that might be connected with redesign for purposes of determining which redesigns are more effective.

Issue Six: Modify the Focus of Compliance, Education, and Outreach for Earned Income Credit Taxpayers

The EIC is a wage-supplement program that has been administered through the IRS since the mid-1970s. Studies have documented how millions of wage earners and their families have been lifted out of poverty by the EIC program. However, Congress was concerned with perceived abuses of the EIC and directed the IRS to address both compliance and education. Last fiscal year, Congress specifically appropriated $146 million for the IRS to perform this task.

Issue Six: Recommendations

The W&I Subgroup believes that during an economic downturn, the IRS must be more proactive in educating and engaging in outreach activities to EIC-eligible taxpayers who do not claim the EIC. Likewise, the IRS should set as a high priority the monitoring of paid preparers who negligently or willfully misadvise taxpayers to claim the EIC when in fact they are ineligible. The subgroup is concerned about the current imbalance between efforts directed at compliance and those targeted to education and outreach, as well as the absence of meaningful tracking of paid preparers who negligently or willfully misadvise taxpayers regarding claims of EIC. The subgroup strongly believes that TAS' current involvement in the examination of EIC taxpayers is a positive step in striking a balance between compliance and education and outreach and should be continued. However, in general, the subgroup believes that the current IRS approach to compliance and education and outreach in the EIC area should be modified so as to better achieve the IRS mission of applying the tax law with integrity and fairness to all.

More specifically, the subgroup recommends the IRS:

(1) Use Earned Income Credit Appropriated Funds to Commission a Broad and Comprehensive Study to Identify Reasons for Under- as well as Over-claims of the Earned Income Credit;

(2) Study the Effectiveness of Imposing the Two- and Ten-Year Penalties for Incorrect Earned Income Credit Claims;

(3) Develop a Program That Measures the Correlation Between Categories of Paid Tax Return Preparers and Incorrect Claims of the Earned Income Credit; and

(4) Develop a Program That Measures Changes in Compliance with the Earned Income Credit with Simplification of the Earned Income Credit, Specifically Changes to the Tie-Breaker Rule.

(1) Use Earned Income Credit Appropriated Funds to Commission a Broad and Comprehensive Study to Identify Reasons for Under- as well as Over-claims of the Earned Income Credit.

The Government Account Office (hereinafter "GAO"), as well as other organizations and scholars, have identified a potentially high rate of EIC-eligible taxpayers who do not claim the credit. However, there has been no well-constructed study performed that would assist the IRS in targeting this population with an effective education and outreach campaign. Similarly, there has been no well-constructed study conducted to accurately identify the reasons for perceived EIC fraud or noncompliance. The IRS has recognized that generally, to increase compliance and more fairly enforce the tax law, there is a need for accurate and relevant data. The National Research Program (hereinafter "NRP") initiative reflects this. However, as currently designed, it does not appear the NRP will be able to capture information to assist the IRS in targeting rates for underclaims of EIC. Thus, this subgroup recommends that the IRS use a portion of the funds specifically appropriated to the EIC program to commission a national study to identify: (i) under-claiming EIC taxpayers; (ii) how to reach such taxpayers; (iii) more precisely the reasons taxpayers incorrectly or fraudulently claim the EIC; and (iv) how to reduce the error and fraud rate. While we recognize that increased examination of EIC returns has resulted in the interception or freezing of substantial refund dollars, there has been no similar effort made to identify taxpayers who are otherwise eligible for the EIC but who do not claim it. This, we believe, hinders the fair application of the EIC rules.

(2) Study the Effectiveness of Imposing the Two- and Ten-Year Penalties for Incorrect Earned Income Credit Claims.

Congress has imposed two penalties for mis-claims of the EIC. If the IRS denies a taxpayer's EIC claim for recklessness or intentional disregard of the law and rules, the taxpayer cannot claim the credit for the next two tax years. If the IRS denies an EIC claim because of fraud, the taxpayer cannot claim the credit for the next ten years. It is not clear to this subgroup how these penalties are tracked and whether tracking of the imposition of penalties provides sufficient information to allow the IRS to construct meaningful education or incentive programs for W&I taxpayers to reduce reckless, intentional, or fraudulent behavior with respect to the EIC. Thus the subgroup recommends that the IRS develop a study that tracks the imposition of these penalties and the criteria upon which penalties are assessed, to measure the impact of imposing these penalties on taxpayer behavior vis-à-vis the EIC.

(3) Develop a Program That Measures the Correlation Between Categories of Paid Tax Return Preparers and Incorrect Claims of the Earned Income Credit.

Popular press as well as research suggests that over-claim rates of the EIC may be correlated to advice by paid return preparers. Further, anecdotal information from low-income taxpayer clinics suggests a further correlation to unregulated paid tax return preparers. Based on briefings to this subgroup, it is the subgroup's understanding that no program currently exists for measuring whether a correlation exists between categories of paid tax return preparers and over-claim rates. The subgroup believes that if a correlation can be identified between over-claim rates and categories of paid tax return preparers, it will assist the IRS in targeting audiences that need EIC education and have a powerful and positive impact on reducing over-claim rates. Thus, the subgroup recommends that W&I

develop a program to measure the correlation between categories of paid tax return preparers and over-claim rates for EIC.

(4) Develop a Program That Measures Changes in Compliance with the Earned Income Credit with Simplification of the Earned Income Credit, Specifically Changes to the Tie-breaker Rule.

We recognize that the complexity of the EIC rules directly correlates to levels of noncompliance. We also recognize that simplification is not something the IRS can achieve on its own. However, Congress' interest continues in simplification of the tax law, generally, and the EIC specifically. Most recently, Congress simplified the so-called tie-breaker rule. Whether simplification in the EIC area specifically, or in the tax law generally, impacts compliance and the allocation of resources cannot be determined without developing a program that measures the correlation between tax law changes targeted at simplification and compliance with those laws. We recommend that the IRS immediately fashion a method for measuring the impact of the simplification of the EIC tie-breaker rules on EIC compliance and that any future changes aimed at simplification be tracked in terms of impact on compliance.

Conclusion

Members of the W&I Subgroup appreciate the time, commitment, and cooperation of W&I representatives and management with whom we have met. We continue to be amazed at the leadership shown by the W&I management team given their limited financial resources and staffing to meet the goals set by the Commissioner. We look forward to assisting the management team next year and await future initiatives toward achieving the W&I mission.

EXHIBIT A

INTERNAL REVENUE SERVICE ADVISORY COUNCIL

K-1 MATCHING TASK FORCE REPORT

ROGER N. HARRIS
MICHAEL E. MARES, TASK FORCE CHAIR
GREGORY H. STEINBIS

SEPTEMBER 21, 2001

INTRODUCTION

The K-1 Matching Task force met in person and by conference call to identify and discuss issues we believe should be considered in the design of the matching program. Overall, the Task Force commends the IRS for tackling this extremely complex and difficult task. We also believe that the successful design and implementation of a K-1 Matching Program will enhance voluntary compliance.

DISCUSSION

We cannot over-emphasize the need to develop a matching program that will operate successfully from the time it is launched. To avoid a host of potential problems caused by a poorly designed program, the IRS must ensure the success of the program from its earliest beginnings. The Task Force members unanimously agree that serious damage will be done to IRS' credibility should a substantial number of erroneous notices be distributed; with the majority of taxpayer recipients comprised of Small Business & Self-Employed customers.

ISSUE

Thus, the Task Force is quite concerned that the matching program be carefully designed to minimize the chance for error. We believe this will require more extensive investigation than a review and analysis of currently transcribed K-1 data. Given the significant differences that currently exist in the preparation of K-1s, and the confluence of complex partnership, trust, and S corporation tax law, given the overlay of and interplay with various other tax provisions, i.e., the passive loss rules described in Internal Revenue Code section 469, and the at-risk rules contemplated in section 465 of the Internal Revenue Code, the Task Force believes that a rigorous review of the entire reporting process may be a necessary prerequisite to the successful implementation of an effective matching program.

RECOMMENDATIONS

Accordingly, we recommend:

(1) No matching be undertaken unless or until the IRS conducts a thorough feasibility study/analysis of such program, given the existing K-1 structure. However, we do recommend the IRS match listed K-1 partners, shareholders, and beneficiaries with individual tax return data for purposes of determining whether entities having partners, shareholders and/or beneficiaries have filed returns. We understand from our meetings with IRS representatives that this will, in fact, be implemented and are fully supportive of the process.

(2) The IRS should determine whether certain amounts lend themselves to ready matching where no additional calculations are required. For example, interest and dividends should be readily transferable to Form 1040, Schedule B. If so, tests should be conducted to determine whether such matches can easily and accurately be made.

(3) We urge the IRS to correlate data from line 1, Form 1965 (trade or business income) with self-employment tax data. However, many partners adjust K-1, line 1 for non-reimbursed expenses when such expenses are incurred by a partner in his or her capacity as a partner. Thus, there may be no match frequently between K-1, line 1 (trade or business income) and the self-employment tax. Likewise, limited partners incur no self-employment tax liability, giving rise to the need for cross-reference to the type of partner identified on page 1. This may provide information with respect to the existence of an employment tax problem and/or issue.

(4) We recommend that the IRS analyze the income amount reported as "other income or deductions" on lines 7 and 11, and determine the components comprising such amount. Based on the experience of the Task Force, we believe a substantial number of K-1s report basis adjustments pursuant to election under section 754 of the Internal Revenue Code on these lines, which can operate to

complicate income reconciliation.

(5) We recommend the IRS consider whether information provided by Schedule J serves any material purpose given the significant reporting differences resulting therefrom. However, the IRS should seek stakeholder input prior to concluding, since many practitioners and third parties use this information for a variety of non-tax purposes.

(6) We recommend the IRS determine whether losses are deducted where no basis exists (information provided by the K-1 itself, i.e., negative capital account with liabilities less than the negative capital account). Again, whether the entity is reporting capital accounts on a tax basis makes a significant difference. Additional information is needed with respect to how capital accounts are maintained for tax return purposes. It is our belief that consistency does not exist, often making it impossible for a partner to determine his or her basis from the return.

(7) We recommend the IRS determine whether limitations contemplated in section 179 of the Internal Revenue Code are properly applied at the entity level.

(8) We recommend the IRS determine the extent to which each existing line of the tax return is utilized.

(9) We recommend the IRS calculate the number of returns that meet the small partnership exception (Form 1065, Schedule B (Question 5)) and the K-1 issues presented by such returns. This information may be used to devise a simplified small entity K-1.

(10) We recommend the IRS determine the number of returns that report rental income or loss amounts only and the potential revenue issues arising from such reported amounts.

(11) We recommend the IRS analyze the significance of Alternative Minimum Tax adjustments and/or preferences reported, and whether a line should be added to Form 6251 specifically to facilitate pass-through entity adjustments.

We believe the IRS should consider modifications to K-1s for purposes of ease in matching data. This will require careful analysis, since any K-1 change will require extensive communication including improved instructions regarding Form 1065 preparation (practitioner training will also be very important). We also recommend that the IRS consider redesign of Form 1065 to simplify information reporting, and a simplified K-1 design - a "K-1 - EZ" as it were - for small partnerships with limited transactions.

CONCLUSION

The Task Force will continue to monitor this matter and seek ongoing status reports regarding the matching program and data correlation.

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OCTOBER 18, 2002

Internal Revenue Service Advisory Council
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Eugene R. Braam, EA, PA Mr. Braam owns and manages a large tax practice in Mankato, MN. His firm has prepared over 25,000 tax returns to date, and will prepare approximately 100 business returns and 1,000 individual returns this coming tax season. He is licensed as a public accountant, investment advisor and insurance agent and is enrolled to practice before the IRS. Mr. Braam has been active in several professional associations including the National Society of Accountants, the National Association of Enrolled Agents, the National Association of Tax Practitioners, the Minnesota Association of Public Accountants, and the Institute of Certified Practitioners, where he held leadership positions in each organization. He was also the first Enrolled Agent to serve as Board Chairman of the Minnesota State Board of Accountancy. Mr. Braam has also held leadership positions in numerous civic organizations such as the United Way, regional library associations, Minnesota Historical Society, to name a few. He is an ardent public speaker, having spoken at numerous civic, business and professional organizations. (**W&I Subgroup**)

Timothy B. Clay Mr. Clay owns and manages Accounting & Business Consultants, Inc., a financial management company that serves small businesses and individuals. His firm assists businesses in QuickBooks set-up, organizational structure configuration, tax issues, preparation of SBA applications, IRS representation, payroll, and loan packages. Mr. Clay is also the Executive Director of the Birmingham Minority Business Development Center, where he organized weekly meetings for potential start-up businesses. Timothy provided a mechanism for information exchange among partners such as, the SBA, the IRS, and state and local governments. Mr. Clay holds a BS in Business Administration, with a minor in Accounting, from Oakwood College, and an MBA from the University of Alabama at Birmingham with a concentration in Accounting/Data Processing. **(SBSE Subgroup)**

Richard D'Avino Richard D'Avino is Senior Vice President, Taxes, for General Electric Capital Services in Stamford, CT, where he is responsible for leading global tax compliance, policy and planning for 25 separate financial services businesses, operating in over 45 countries, comprising over $400 billion of asset exposure. Mr. D'Avino also worked as Vice President and Senior Tax Counsel for General Electric Capital Services. Richard holds a BS in Accounting from the Wharton School of Business, University of Pennsylvania, and a JD from the University of Pennsylvania. **(LMSB Subgroup)**

Felecia G. Dixson Felecia Dixson is an Enrolled Agent and sole proprietor of Accounting Technologies, in Salem, MO. She is currently the Committee Chair of the Special Enrollment Examination Advisory Committee for the Internal Revenue Service, and an editor and writer of the Illinois Farm Tax School Manual, University of Illinois. A member of the National Association of Tax Practitioners, National Society of Accountants, and Accreditation Council for

Accountancy and Tax, Inc. Ms. Dixson has more than nineteen years experience in the tax business, working with clients, both for profit and nonprofit organizations. **(SBSE Subgroup)**

Jolet L. Dusenbery, EA Ms. Dusenbery is an instructor for the National Association of Tax Practitioners ("NATP") and an adjunct instructor at Johnson State College. She formerly owned and operated a tax and accounting firm that specialized in tax preparation, representation and electronic filing issues. Prior to owning her business, Ms. Dusenbery held industry various positions. Ms. Dusenbery is enrolled to practice before the IRS, holds a BS in Environmental Science and a MS in Education. She is an active member in the National Association of Tax Practitioners, the National Association of Enrolled Agents and other professional associations. She has published tax articles for local newspapers and other association publications, spoken on live radio programs, and presented entrepreneurial workshops on small business issues. (**SBSE Subgroup**)

Michael W. Evanish, EA Mr. Evanish manages MSC Business Services, a $3.5 million accounting, payroll, business analysis, and tax preparation business providing services primarily to farmers in a four-state area. Mr. Evanish formed alliances with a law firm, CPA firm, and lending, leasing and appraisal firm to provide advice/assistance to farmers his firm did not offer. Prior to holding his present position, Mr. Evanish served as Director of Training at MSC for several years. Prior to his employment with MSC, Mr. Evanish held positions in sales and accounting with other organizations. Mr. Evanish is enrolled to practice before the IRS, and has a BS in accounting and marketing from Clarion University. Mr. Evanish is active in community affairs, having served on the Hampden Township Planning Commission, and the Kingwood Homeowners' Association. He is also a member of the National Society of Accountants. **(SBSE Subgroup Chair**)

Lester D. Ezrati, Esq. Lester Ezrati is Vice President of Hewlett-Packard Corporation in Palo Alto, CA, where he is responsible for Domestic & International Taxation, Licensing, Customs and Audit. Prior to holding his current position, Mr. Ezrati worked in both International and Domestic Tax Counsel also at Hewlett-Packard. He is a past International President of the Tax Executives Institute where he led the establishment of a strategic plan to guide the organization over a subsequent five-year period. He is active in other professional associations such as the California and Utah State Bars and the American Bar Association. He has a BA in Economics from the University of Rochester, a JD from Boston College and an LL.M. in Taxation from the New York University School of Law. (**LMSB Subgroup**)

Roger N. Harris, EA Mr. Harris is President of Padgett Business Services in Athens, GA and has been with Padgett for more than twenty years. Mr. Harris is a member of the National Society of Accountants, where he has served as Chair of the Federal Taxation Committee. In that capacity, Mr. Harris has testified extensively

before congressional committees on issues such as EFTPS, IRS restructuring and reform, and small business issues. Mr. Harris is also affiliated with the National Association of Enrolled Agents, and is an accredited tax advisor and preparer of the Council for Accountancy and Taxation. He has a degree in accounting from the University of Georgia. **(IRSAC Chair & SBSE Subgroup member)**

Timothy B. Heavner

Timothy Heavner is Executive Director, The Community Tax Law Project, in Richmond, VA. Mr. Heavner develops program initiatives for 501 (c) (3) organizations providing *pro bono* legal services to low-income individuals in tax controversies. Prior to holding his current position, Mr. Heavner was Associate Area Counsel for the IRS, in which position he represented the IRS in both tax and general litigation matters with primary emphasis in tax litigation, including specialized knowledge of EITC and Innocent Spouse provisions. He is active in the American Bar Association and the West Virginia and Virginia State Bars. He holds a BA in Government from Georgetown University, a JD from Washington and Lee University, Lexington, VA, and an LLM in Taxation from Georgetown University Law Center. **(W&I Subgroup)**

Tracy Hollingsworth

Tracy Hollingsworth is a Senior Attorney and Director of Tax Affairs with Manufacturers Alliance/MAPI in Arlington, VA. She has been with Manufacturers Alliance for the last twenty-plus years, providing technical, networking and meeting services to the corporate tax directors of their member companies. She has published numerous articles, i.e., Treasury Suspends Overarching Final Research Tax Credit Regulations; Asks for Comments, LAR-447 (February 2001), and Corporate Tax Shelters: Finding a Measured Response, LAR-433, (April 2000). Ms. Hollingsworth is active in the American Bar Association, District of Columbia and the Massachusetts Bar Associations, and holds a BA from Scripps College, Claremont, CA, and a JD from Boston University, Boston, MA. **(LMSB Subgroup)**

Ann Kathryn Hubbard

Kathryn Hubbard is an Enrolled Agent and the owner of Hubbard Financial Services, Inc. She is currently President of the Texas Society of Enrolled Agents, a member of the National Society of Enrolled Agents and an active member of NAEA's Leadership Committee. Ms. Hubbard is also a Fellow of the National Tax Practice Institute, and a well-known tax seminar speaker in the Houston area. Ann was the Treasurer for the Annise Parker Houston City Council Campaign and volunteered for the Houston Chronicle Tax Hotline. **(SBSE Subgroup)**

Eliot L. Kaplan

Eliot Kaplan is a member of the law firm, Squire, Sanders & Dempsey L.L.P., in Phoenix, AZ, practicing in the areas of federal, state, and local tax law, and general business law. He has extensive experience in organizing joint ventures and other partnerships and has represented a wide variety of small, medium, and large businesses. Prior to entering private practice, Mr. Kaplan was an

attorney-advisor with the Office of Chief Counsel at the Internal Revenue Service, drafting rulings and regulations. He is active in many civic and bar activities, including the American Bar Association Section of Taxation. Mr. Kaplan holds a BS degree from the University of Arizona, a JD from Arizona State University, and an LLM, with distinction, from Georgetown University. **(IRSAC Vice-Chair & LMSB Subgroup Chair)**

Pamela P. Kulish

Pamela Kulish is the President and Chief Operating Officer of Computer Accounting Service, Inc. Through her company, Ms. Kulish provides tax preparation services, financial analysis and planning relative to taxes and investment strategies, to nearly 300 individual clients. Corporate clients include approximately 50 retail and service organizations with gross revenues ranging up to $7 million. Services directed to corporate clients include: live payroll; monthly financial reporting; analysis and recommendations of cafeteria employee benefit plans; business plans; development of budgets and projects; and local, state, and federal tax preparation. Ms. Kulish is a member of the Maryland Society of Accountants, the National Association of Enrolled Agents, and the National Association of Accountants. (**SBSE Subgroup**)

Diana L. Leyden

Diana Leyden is an Assistant Clinical Professor and the Director of the Tax Clinic at the University of Connecticut, School of Law. Ms. Leyden teaches and supervises law students representing low-income taxpayers in federal and state tax controversies, and trains law students in conducting conferences and hearings before the IRS and the Connecticut Department of Revenue Services. Prior to her current position, Ms. Leyden was a Tax Attorney with the Connecticut Department of Revenue Services. She is a member of the American and Connecticut Bar Associations and Chairs the Communication and Program Developments Subcommittee and the Low-Income Taxpayer Committee for the American Bar Association. Ms. Leyden holds a BA degree from Union College, Schenectady, NY, a JD from the University of Connecticut, and an LLM from Georgetown University. **(W&I Subgroup)**

Susan W. Martin

Susan Martin is currently interim Assistant Vice-President for Academic Affairs and a Professor of Accounting and Taxation at Seidman School of Business at Grand Valley State University. Prior to her current position, Ms. Martin was the Commissioner of Revenue for the State of Michigan. She co-authored a textbook titled, *Today's Essentials of Government* and *Not-for Profit Accounting and Reporting*, and has published numerous articles. Ms. Martin holds a BS in public speaking from Central Michigan University, an MBA in Accounting from Michigan State University, and a Ph.D. in Accounting from Michigan State University. **(SBSE Subgroup)**

Marjorie L. Miller

Ms. Miller is a principal at The Miller Group in Portland, OR., where she provides informational presentations and analyses of business activities for tax credit potential for industries and accounting firms in the Northwest. Prior to her current position, Ms. Miller was a Tax Associate at Coopers & Lybrand, a law clerk for a Portland, OR law firm, an Adjunct Professor at

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Michael A. O'Connor Mr. O'Connor is an attorney in private practice who has worked as a litigator, lobbyist, program administrator, and more recently as a consultant providing management assistance, policy analysis and technical assistance to public and private human service agencies and private businesses. Mr. O'Connor has designed and implemented outreach campaigns that promote greater participation by eligible families in Earned Income Credit and other tax benefit programs available to lower income families. Mr. O'Connor also established the Tax Counseling Project as a multi-site VITA program in Chicago, and while managing this project for several years, developed a total of fourteen sites across Illinois. In 1991, Mr. O'Connor developed the nation's first training and technical assistance resource guide regarding tax benefits available to foster and adoptive parents. In 1997, Mr. O'Connor developed a handbook and delivered a seminar on unique tax benefits available to families providing adult residential care to developmentally disabled persons. Mr. O'Connor has a BA in Political Science from the University of Illinois and a JD from DePaul University. He has published numerous tax articles for various law journals and other publications. (**W&I Subgroup**)

Michelle B. O'Connor Michelle O'Connor is an Assistant Clinical Professor and Director of the Quinnipiac University School of Law Tax Clinic. In her current position she developed an intake system, a new filing protocol, and a case tracking system, that ensures better, continuous representation of clients. Prior to her current position, Ms. O'Connor practiced law with Arnold and Porter, where her work included tax planning, compliance, transactional, and litigation matters in the employee benefits tax and federal income tax areas. Michelle also worked at the Department of Justice, Tax Division, as an attorney, and clerked for the honorable Stephen J. Swift of the U.S. Tax Court. She is a member of the American, Virginia and District of Columbia Bar Associations. Ms. O'Connor holds a BA from the University of Connecticut and a JD from Washington and Lee University. **(W&I Subgroup)**

Albert C. O'Neill, Jr., Albert O'Neill is an attorney with the firm of Trenam, Kemker, Scharf, Barkin, Frye, O'Neill & Mullis. He is currently President of the American Bar Retirement Association, having served as Director for the previous five years. He also served as Chair of the American Bar Association's Section of Taxation and numerous other positions in both the American and Florida Bar

Associations over a twenty-year period. Mr. O'Neill has an LLB, magna cum laude, from Harvard University and has published several articles in the Harvard Law Review. (**LMSB Subgroup**)

Charles W. Shewbridge III Charles Shewbridge recently retired from Bell South Corporation in Atlanta, Georgia, where he was the Chief Tax Executive. Mr. Shewbridge is a past International President of the Tax Executives Institute where he also served as a Director and member of the Executive Committee. Prior to his employment with Bell South, Mr. Shewbridge held executive positions at Dominion Resources, Inc., Universal Leaf Tobacco, Inc., and Davenport and Company. Previously Mr. Shewbridge was associated with two CPA Firms and taught at the Virginia Commonwealth University. He has an MBA in accounting & management and is active in other professional associations such as the United States Telephone Association, Chairman of the Tax Committee, and the Edison Electric Institute where he served on the tax Committee. (**LMSB Subgroup**)

Gregory H. Steinbis Greg Steinbis practices as a Certified Public Accountant in Morgan Hill, CA., at the southern end of the Silicon Valley. Mr. Steinbis is also enrolled to practice before the IRS. He performs accounting, payroll, tax, and estate work and more recently, financial advisory services. He is active in the National Association of Enrolled Agents and is the organization's immediate Past President, also serving as Vice President, Treasurer and board member during the past seven years. During this period he was a member of the Governance Restructuring Task Force that was instrumental in reorganizing NAEA's internal governance. Mr. Steinbis has also been active in civic organizations in and around the Silicon Valley. **(W&I Subgroup Chair)**

Denise Strain Denise Strain is Vice President and General Tax Counsel for Citicorp/Citibank and has been with the corporation for over 24 years. Ms. Strain directs all aspects of the global tax function through the management of over 120 tax professionals in eight countries. Denise is Vice Chairman of the Tax Committee for the National Foreign Trade Council, an active member of the American Bankers Association, and the Business Round Table Tax Committee. Denise Chairs the New York Bankers Association Tax Committee, and holds a BA in Psychology from Fairfield University, a JD from St. John's University, and an LLM in Taxation from New York University. **(LMSB Subgroup)**

Carol Tremble For more than 13 years, Carol has owned her own practice, Carol B. Tremble, Certified Public Accountant, serving 450 clients; 200 of whom are small business owners. Ms. Tremble prepares taxes and provides general business consulting. Carol is a Selectman in her town, having been elected to this position consistently every three years since 1988, and is a member of the American Institute of Certified Public Accountants, the New England Peer Review Board, and the Vermont Society of CPA's. Ms. Tremble holds a BA in Mathematics from the University of Vermont. (**SBSE Subgroup**)

Betty M. Wilson

Betty Wilson is Vice President of Taxes, MGM Mirage Corporation. In this role, Betty developed the Corporate Tax Department for MGM Mirage, and was named one of the 20 Most Influential Women in Southern Nevada for 2001 by "INBUSINESS LAS VEGAS". As the International President of Tax Executives Institute from 2000-2001, Ms. Wilson continued and enhanced the partnership among Tax Executives Institute, the Section of Taxation of the American Bar Association, and the Tax Division of the American Institute of Certified Public Accountants for the promotion of the joint tax simplification project. Ms. Wilson holds a BS degree in Accounting from Colorado State University. (**LMSB Subgroup**)