**Tax Foundation's "Tax Policy Podcast"**
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**Scott Hodge**: Thank you for tuning in today. I'm Scott Hodge, president of the Tax Foundation. Joining me for our Tax Policy Podcast is Nina Olson, who is currently the National Taxpayer Advocate at the Internal Revenue Service, where she frequently writes, speaks, and testifies before Congress about issues affecting taxpayers. Nina, thanks for joining us today.

**Nina Olson**: It's my pleasure.

**Hodge**: Well, I'm sure that when you go to dinner parties and tell people that you're the Taxpayer Advocate at the IRS, they think it's probably like "military intelligence," sort of an oxymoron. What does the Taxpayer Advocate do, and why was the office created in the first place?

**Olson**: Well, the Taxpayer Advocate has been around since the 70s, in one form or another, first as the IRS Ombudsman, and then the Advocate, and now the National Taxpayer Advocate. It was created by Congress to be the voice of the taxpayer, an independent voice of the taxpayer inside the IRS. It is a little bit like an oxymoron, but that tension sort of helps us do our job. We help taxpayers solve their particular problems with the IRS, and then we learn from those particular problems to identify systemic problems that might affect groups of taxpayers, or where the law needs to be changed, or where IRS processes need to be changed.

**Hodge**: What are some of the most pressing issues of complexity? I was reading through some of the reports that have come out of your office recently, and you have some ten different areas of the tax code that are most problematic, like the Earned-Income Tax Credit and so forth. Can you identify some of those, and what you've identified as what Congress needs to focus on?

**Olson**: Well, they run the whole gamut from the law just being too complex, to the law being burdensome on taxpayers in a procedural way. The Earned Income Credit is an example of complexity. It's not just the Earned Income Credit; even though we've had some simplification, we do have a Child Credit, a Dependency Exemption, Head of Household Status, the Earned Income Credit and this is sort of silly to make people go through all of these different kind of provisions just to get some benefits that are geared to the family, and we have recommended some changes that would give a unified credit for a family that would be easier for people and not trip them up.

On the other hand, you have something like Capital Gains, where people have to compute the basis in their stock, and what the Government Accountability Office found was that when people are left with having to calculate what the cost or the basis of their stock was when they sell stock, that sometimes they over-report their basis and therefore under-report their gain. On the other hand, sometimes they just give up trying to figure out the basis and they actually low-ball it, and they end up paying more than their taxes that are due. We recommended that Congress require brokers to report the stock basis of transactions at the same time that they report the sales. That would both help taxpayers, certainly would raise some revenue, and would reduce burden all around.

**Hodge**: Well, of course, the complexity, as I think you've pointed out, is a major contributor to what is known as the "tax gap" and the difference between what the IRS thinks Americans owe in taxes and what's actually paid. And we actually interviewed Senator Max Baucus a few weeks ago, who was extremely concerned about this issue. You've written on this quite extensively, and your office has looked at it, but you've pointed out that enforcement and audits aren't the sole effort that ought to be needed to close the tax gap. That we need simpler tax laws, better services and so forth -- so you need a more holistic approach, I think is the term that you've used.

**Olson**: Yeah, I think that's right. One of my points is that with enforcement, you don't convert a taxpayer that is non-compliant into a compliant taxpayer -- in fact you may make them madder. Enforcement has a one-time effect, but it doesn't have the halo effect that actually helping someone become voluntarily compliant -- you're really changing behavior, you're changing the norm of behavior. And I encourage the IRS, I've been writing a lot about this to look at the types of non-compliance, because you could in fact have what I call "asocial non-compliance." You know, the person doesn't care about following any laws, and no matter what you do, you are not going to be able to convert that person into a compliant taxpayer, they view it more as a risk and a gamble, and that's the mentality. And enforcement's the appropriate response in those cases.

But on the other hand, where the complexity of law leads people to make mistakes, well then the response is not to go after them with a sledgehammer, the response is to go after Congress to say make the law simpler, or we need to explain the law better.

And sometimes what you have is "procedural non-compliance," where the law is OK, but the IRS has set up all these hurdles for people to prove that they are eligible for something, for claiming a deduction, or some kind of provision, and the taxpayer just gives up, either fudges it or doesn't even claim it.

And I guess another really important type is what I call "brokered non-compliance," namely, the role of preparers facilitating, encouraging or discouraging compliance or non-compliance. There's a different approach for each one of them, and just taking a broad stroke and saying audits are the only thing, that's just not the response, that's not going to get us to close the tax gap.

**Hodge**: Well, speaking of sledgehammers, in a way, the IRS has started looking at contracting out or using private debt collectors to collect those unpaid tax bills. The New York Times has been very critical of this effort; they think it'll actually be more expensive, and obviously one of the biggest issues is the concern about privacy or the sensitivity of all of this data. Can you help us sort through all this, is the New York Times off-base on this, and what's the perspective of your office?

**Olson**: I personally am opposed to using private debt collectors to actually collect the tax. I think that the IRS has the authority to do this, and although I think that the program as designed right now is legal, is constitutionally permissible because the private debt collectors aren't really doing anything that requires discretion and judgment, which is reserved to government employees.

That's the very problem with why this won't work. It's because it's premised on the concept that there are basic, simple tax cases, and I'm here to tell you, after having practiced outside the IRS for 27 years, and now being National Taxpayer Advocate for five years, that there is no such thing as a simple tax case. That even when you think that you've got somebody who has signed their tax return that shows a balance due, that they've agreed to the amount, when you actually go out to touch them, often they say, "Well, I can't afford to pay this right now, I'm uncollectible." That requires discretion. It requires a decision whether you're going to put a lien on that taxpayer's account while you hold off collecting. Or somebody will say, "Well, I don't mind paying the tax, but I don't think I should have to pay the penalty, I was in the hospital," you know. And all of those things, the private debt collectors can't, constitutionally, decide, and so the cases go back to the IRS.

So here we have this situation where we're paying 25% to the private debt collectors, then we're going to reserve 25% of whatever we collect to pay for the IRS unit that is going to have to work these cases, so the public fiscal only gets 50%, and my question is, what if we had just sent a letter to that taxpayer? I mean, these are cases that have just been lying fallow, you know? And so what if we had just shaken the tree ourselves with a letter? Which goes to my other point about, there might be a role for private debt collectors, in the fact of, they might be very helpful to us in doing skip tracing, trying to find the taxpayers, you know? Or trying to find assets. Not necessarily engaging in the conversation with the taxpayer, but assisting the IRS in doing some of its core responsibilities.

**Hodge**: Just to play devil's advocate for a minute, there are a lot of cases in the government where using private debt collectors has been pretty effective, such as the student loan programs, farm loan programs, the Small Business Association Administration loan programs, etc., where the government has proven to be pretty ineffective at maintaining the effectiveness of those collections, and moving to private collectors has proven to be very effective, and actually improved the servicing, in some cases, of those loans. Wouldn't that apply in this case?

**Olson**: I think there are two issues. One is that from the Secretary and the Commissioner on down, everyone acknowledges that the IRS collects the tax cheaper, better, and more effectively than the private debt collectors. The Commissioner has sworn before Congress, on sworn testimony, that that is his position. It's just that we're not getting additional funds from Congress to hire the employees to do that work. The second point is, the Constitution doesn't reserve the authority to issue a student loan to the government, but the Constitution does say that the power to lay and collect tax resides in the government. There's really a constitutional issue there. And my final point is, the government will not fall down if the student loans are not made, but the government will fail, and the social contract with the taxpayers will fail, if we do not protect taxpayer rights, and protect taxpayer privacy, and raise the funds that we need to. You know, we can argue that whether we need a smaller government, or a larger government and lower taxes, and things like that, but there is this understanding--and I view it as a social contract--between the tax administrator and the taxpayers, that we are going to absolutely protect their rights, and absolutely protect their privacy, and really honor the fact that they are coming in and paying the lifeblood of government with their hard-earned dollars; and I think that makes it very, very different from the other kind of areas where we have used private debt collectors quite effectively. And again, I view that there is a role for private debt collectors, it's just not the role that this test has, or this program has envisioned.

**Hodge**:  Well, I think when you survey most taxpayers, they feel that the Tax Code is just simply too complicated, and we all hear of the famous Money Magazine article every year, in which they send out 50 tax returns to 50 specialists and get 50 responses. And certainly tax reform has been on the lips of many here in Washington--the President, last year, had his Tax Reform Panel which, unfortunately, that report is now sitting on a dusty shelf, but you've presented some very, very interesting testimony to the Panel, and what you recommended, that tax reform needs a taxpayer-centric approach, which I thought was quite interesting. And you had laid out a set of core principles that tax reform should follow, and one of those should be that the Tax Code shouldn't entrap taxpayers, it should be as simple as possible, the Tax Code should be periodically reviewed by Congress for what you called a "sanity check"--boy, that sounds like welcome relief! Tell me more about some of these core principles, and how we can move that forward and get those introduced into the whole tax reform debate.

**Olson**:  Well, what I was trying to say to the Panel, and which I reiterated in my December Annual Report to Congress, was that we really need to understand the taxpayer, and make sure that we design rules that don't create burden for the taxpayer and aren't counterintuitive to the way the majority of taxpayers live their lives, and of course the dependency exemptions and all the credits are a good example of that. On the other hand, this entrapment--and the alternative minimum tax is a classic example of both that violation of that principle, as well as an example for why we need a sanity check periodically, because the alternative minimum tax is going to entrap so many taxpayers on a going-forward basis--it already does now--and it is so far away from achieving what its original purpose was that if we had, say, a periodic review of a different portion of the Code, once every year on a five-year cycle, you would find it more affordable to say, "Oops! This is creeping in an area that we don't want it to go. We need to revise it," the revenue cost wouldn't be so great. You would be able to make these revisions on an ongoing basis. And it would also reflect the way the world changes over time. Another example of just trying not to entrap taxpayers, and knowing your taxpayers, are [sic] the education credits. You know, we have a public policy to encourage secondary and higher education, and that's very laudatory, but we have all of these credits and taxpayers just clearly do not know whether they have chosen the right one. And in fact, GAO did a report that showed that when they actually went and looked at returns where taxpayers had tried to wade through these provisions and decide what was right, they often selected the thing that was not best for them, and that if they'd selected another education provision, they would have gotten more tax benefit; but it's just too complicated for them.

**Hodge**: And the solution, ultimately, will be, have to be, some fundamental tax reform.

**Olson**: I agree with that.

**Hodge**: It just appears that things have stalled, until we get somebody to light a fire under Congress and the White House, it doesn't appear that that's going to be the case any time too soon.

**Olson**: Well in 2001 we made the legislative recommendation to repeal the Alternative Minimum Tax, and we repeated that just about every single year; and I had sort of hoped that by raising the Alternative Minimum Tax, and the revenue impact of the Alternative Minimum Tax, by 2010 or 2012, depending on which numbers you look at, it will cost more to repeal the AMT than it will be to repeal the regular Income Tax and leave the AMT. And that doesn't mean that you get rid of having to go through the steps of calculating your regular income tax. You still have to do that to leave the AMT. I mean, that's a mess, and I had hoped that we would, by identifying that, and beating the drum about AMT--dealing with the AMT is going to drive the need for fundamental tax reform--that we would do it before we reached a crisis in 2010 or 2012 and 33 million taxpayers are pulled into this. But now I've just been feeling like, oh, they're going to wait until the very last minute, when we do have the crisis, and that will be the driver. You know, basically, people standing up like in the movie "Network" saying, "I'm mad as heck and I won't take it anymore!"

**Hodge**: Well, ultimately, members of Congress are followers and not leaders. I think that it is that sort of public outrage that will drive the process, and certainly having you at the National Taxpayers' Advocate office is a big help in that. I think that just far too few people appreciate the fact that there is an office, a taxpayer advocate, and thanks to the work that you're doing, and highlighting these issues, and bringing them to the attention of Congress, you're making a difference in that process, and hopefully will begin to drive the effort to fundamental reform.

**Olson**: Thank you.

**Hodge**: Thanks for spending some time with us--I really appreciate it--and taking time away from your efforts to be there on behalf of taxpayers.

**Olson**: Well, thank you for all your good work. This was very enjoyable.

**Hodge**: Thanks so much.

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