

**WRITTEN TESTIMONY OF  
JOHN A. KOSKINEN  
COMMISSIONER  
INTERNAL REVENUE SERVICE  
BEFORE THE  
SENATE JUDICIARY COMMITTEE  
SUBCOMMITTEE ON OVERSIGHT, AGENCY ACTION, FEDERAL RIGHTS  
AND FEDERAL COURTS  
ON THE EXEMPT ORGANIZATIONS DETERMINATION PROCESS:  
PROGRESS OF AGENCY REFORMS AND CONGRESSIONAL OPTIONS  
JULY 29, 2015**

Chairman Cruz, Ranking Member Coons and Members of the Subcommittee, thank you for the opportunity to discuss actions taken by the IRS in response to the report two years ago by the Treasury Inspector General for Tax Administration (TIGTA) regarding the improper criteria used in processing applications for tax-exempt status under section 501(c)(4) of the Internal Revenue Code.

Let me begin by reiterating what I have said earlier in my tenure as IRS Commissioner. The situation described by the Inspector General in his report should never have happened, and we are doing everything possible to ensure that the mistakes referenced in the report do not happen again. Every taxpayer, whether an individual or an organization, needs to be confident that they will be treated fairly by the IRS no matter what their political affiliation, their position on contentious political issues, or whom they supported in the last election.

Even with our declining resources, we will still audit over 1 million taxpayers this year. And when someone hears from us regarding their tax return – by letter, I should add, in light of the recent proliferation of IRS impersonation telephone scams – they need to understand that it is only because of something in their tax return, and not other factors. And, if someone else has the same issue on their return, they will hear from us as well, within the limits of our budget resources.

A shared belief in the fairness of our tax system and its administration is fundamental to the voluntary compliance by our citizens with the requirements of our tax laws. This compliance provides the vast majority of the over \$3 trillion in revenue that we collect for the nation every year. We are the stewards of this system and take our responsibility seriously.

As part of our work to move forward, we have implemented all of the recommendations made by the Inspector General in his May 2013 report. The Inspector General reviewed our actions and issued a follow-up report in March of

this year, noting that the IRS has taken “significant actions” to address his recommendations.

These are important steps. We have eliminated the use of inappropriate criteria; we have expedited the processing of section 501(c)(4) applications; and we have instituted a quality review process to assure that unnecessary or improper information requests are not sent to applicants. In addition, the Department of the Treasury and the IRS have begun the process of drafting guidance on how to measure social welfare and non-social welfare activities of section 501(c)(4) organizations.

Our efforts to develop this guidance have been greatly informed by the more than 160,000 public comments received in response to the 2013 proposed regulations. We asked for, and received, comments on several issues, including three major issues: the proposed definition of political campaign activity; to which organizations that definition should apply; and the amount of political activity an organization can engage in consistent with a particular tax-exempt status. Our goal is to provide guidance that is clear, fair to everyone, and easy to administer.

The changes we have made in response to the Inspector General’s recommendations on exempt organizations also include:

- Establishing a new process for documenting the reasons why applications are chosen for further review;
- Developing new training and workshops for employees on a number of critical issues, including the difference between issue advocacy and political campaign intervention, and the proper way, under current law, to identify applications that require review of potentially significant political campaign intervention;
- Establishing guidelines for specialists in the IRS’s Exempt Organizations (EO) division on how to process requests for tax-exempt status involving organizations engaging in potentially significant political campaign intervention; and
- Creating a formal, documented process for EO determinations personnel to request assistance from technical experts.

In addition to these actions, the entire leadership chain – from the top down to the Exempt Organizations Division – is new since 2013, starting with the Commissioner of the IRS, the Deputy Commissioner for Services and Enforcement, the Commissioner of the Tax Exempt/Government Entities Division (TE/GE), the Deputy Commissioner of TE/GE, and the Director of Exempt Organizations. All of us are committed to providing taxpayers with the fair, unbiased actions and responses to their inquiries that they have a right to expect.

Importantly, the work of this new leadership team has included reducing the inventory of section 501(c)(4) applications, including the group of 145 cases in

the “priority backlog” – those that were pending for 120 days or more as of May 2013. By July 2, 2015, 140 of those cases, or 97 percent, were closed. Of the closed cases, 107 of them were approved, including 43 organizations that took advantage of a temporary self-certification procedure we offered in the summer of 2013. Of the remaining 33 closed cases, most were closed without a determination, either because the organization withdrew the application or it failed to respond to our questions. To date, five applications have been denied. The remaining five cases are still open.

Beyond the scope of the Inspector General’s recommendations, we have also established an agency-wide enterprise risk management program, creating risk management liaisons in each area of our operations and providing for the regular identification and analysis of risks to be eliminated or managed across the agency. We are working to create a culture where employees are encouraged to think of themselves as risk managers and to report any issues or problems that occur. My goal is to have employees understand that the only problems we can’t solve are the ones we don’t know about. As a corollary to that effort, we are encouraging the further flow of information from front line employees up through the organization as well as out to the front line from senior managers.

The investigations into the determination process for tax-exempt status also raised another issue that we have been working to address, and that is the need to improve the IRS’ records retention practices. This issue was brought into focus recently with the Inspector General’s release of a report on the IRS’ production of emails relevant to the investigations. The report described difficulties in searching for emails and retrieving them from the IRS’ outdated system for electronic records retention.

It is important to note that even with our antiquated system, the IRS was able to produce more than one million pages of documents to the investigating Committees, although at a cost of approximately \$20 million. This included a total of 78,000 emails sent or received by former Director of Exempt Organizations Lois Lerner. The Inspector General’s review found just 1,330 additional emails that had not already been produced. The Inspector General also observed that a review of those emails did not provide additional information for purposes of his investigation. The Inspector General also found that the erasure by IRS employees of a set of disaster recovery tapes in 2014 was not intentional and that there was no evidence that those employees had been directed to conceal information from investigators. Nonetheless, this situation should not have happened, and we are reviewing the IG’s report and taking steps to ensure that future document preservation instructions are understood and followed throughout the agency.

In addition, efforts are now underway to develop a more modern email retention system at the IRS, which will greatly improve the management and storage of emails that are Federal records. In particular, as detailed below, we are taking

measures going forward to ensure that our archival data is no longer stored in a manner that is vulnerable to loss through equipment failures – such as hard drive crashes. This will enhance our ability to fully and efficiently comply with information and document requests, without having to resort to the uncertain, costly, and difficult process of retrieving data either from individual employee hard drives or, as a backup, disaster recovery systems.

Even though the IRS has a long history of complying with the standards for retention of federal records set by the National Archives and Records Administration (NARA), the unprecedented volume and scope of the document requests made by Congress and the public since 2013 in regard to the processing of applications for tax-exempt status highlighted the need for the IRS to continue improving its maintenance of federal records that are in electronic form, consistent with the constraints on our budget. In this effort, we have been in close consultation with NARA to ensure the best approach.

As a first step, in October 2014, we implemented an interim email retention policy for all senior IRS executives. This interim policy, which follows NARA's recommendations for email records retention, was extended to all IRS executives in December 2014. This policy is to be followed by a more fully developed enterprise solution to allow us to securely store, search and retrieve emails that are federal records. We are working to complete the development and implementation of the enterprise solution, though success will depend on funding, staffing, and prioritization with other business requirements.

While the interim policy is an important step toward a consistent policy of electronic federal records retention, the IRS ultimately intends to develop and implement more automated enterprise solutions, consistent with government-wide guidance and standards. Given the importance of this issue, we have already begun to take action using the resources available to us.

The IRS considered putting a more modern system in place three years ago, but was unable to do so because of budget constraints. Now, however, we have made the decision to move forward with the new system, even if that means reducing resources to other areas of agency operations already hampered by continually diminished resources provided in the IRS budget each year. Once a more modern system is established, the IRS should be able to respond to even complex Congressional inquiries much more efficiently and effectively than in the past. Our goal is to ensure that we have the ability to obtain official records of the agency in a reliable and consistent manner.

Chairman Cruz, Ranking Member Coons and members of the Subcommittee, this concludes my testimony. I would be happy to take your questions.