14 Recommendations for Congress and the IRS as They Attempt to Narrow the Tax Gap

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BY: ANDREW LAUTZ AND PETE SEPP

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President Biden's American Families Plan proposes spending $1.8 trillion over 10 years on initiatives like universal pre-school and access to tuition-free community college, new subsidies for child care and paid leave, and a permanent extension of expanded Affordable Care Act premium tax credits. Like Biden's $2 trillion American Jobs Plan and the already-passed $1.8 trillion American Rescue Plan, the American Families Plan is ambitious in scale and scope. President Biden has proposed paying for the latter plan in part by narrowing the so-called "tax gap," the difference between federal taxes owed and paid by individuals, families, and businesses across the country. The White House estimates that with an $80 billion increase to the Internal Revenue Service (IRS) budget over 10 years and increased third-party reporting requirements from financial institutions, they can raise $700 billion in revenue to cover a significant portion (around 39 percent) of the $1.8 trillion American Families Plan cost.

There are reasons to believe this estimate is wishful thinking at best and tremendously irresponsible budgeting at worst. As NTU Foundation's Andrew Wilford, Andrew Moylan, and Pete Sepp wrote in a recent policy paper:

> Now, there is reason to believe that the latest IRS estimate of the tax gap at $381 billion may be inaccurate. For example, the official IRS estimate of the tax gap does not factor in the growth of cryptocurrency and new research into offshore holdings.
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> ...no one can truly claim to know the exact size of the tax gap — if the exact amounts and sources of uncollected revenue were known, it would be far easier than it is for the IRS to collect it. Nevertheless, the picture becomes rather clear: the tax gap is almost certainly not $1 trillion and no bona fide research in existence today adequately supports the notion that it is.

The reference to $1 trillion is relevant because IRS Commissioner Chuck Rettig recently made headlines by *suggesting* the tax gap *could be* $1 trillion per year, much higher than the most recent estimate from the IRS (published in 2019 and based on tax years 2011 through 2013) of $381 billion per year. Unfortunately, as NTU Foundation pointed out, media took Rettig's "off-the-cuff statement" as "gospel truth," which is likely out of step with reality.

Unfortunately, perceptions that the tax gap is $1 trillion per year may feed into a belief that the IRS can *easily* claw back $700 billion over the next decade by increasing the IRS budget and increasing third-party reporting requirements. The administration estimates it can raise a third of the $700 billion ($240 billion net) from that increased IRS budget and the remaining two-thirds ($460 billion) from enhanced reporting requirements. However, as NTU Foundation has pointed out, this estimate of a return on investment (ROI) is likely a significant overstep. And if the Biden administration's efforts fall significantly short of $700 billion over 10 years -- and nonpartisan, expert analysis suggests they might -- American taxpayers could be left responsible for tens of billions or even hundreds of billions of dollars in additional deficit spending to pay for new programs, at a time of already-record debt and deficits in the federal government.

Therefore, NTU believes that it is not only prudent but *necessary* for Congress and the IRS to take several precautions before assuming a tax gap windfall can be spent on expensive new federal programs and initiatives. Our 14 recommendations for Congress and the agency can be separated into four broad buckets:

1. **Protecting taxpayer rights**: Congress must ensure that individuals and businesses are treated fairly by a beefed-up IRS. Lawmakers must also ask the agency to be straightforward and transparent about what kind of additional costs honest actors in the private sector may bear as the federal government seeks to aggressively narrow the gap.
2. **Spending IRS money correctly**: The $80 billion pot of money that the Biden administration

wants Congress to give the IRS will be wasted if additional appropriations do not come with strict Congressional direction and oversight for how the agency spends the money.

3. **Improving the agency**: Congress must also ensure that the agency does not use additional funds to simply double down on its past and present mistakes, and lawmakers should play an active role in ensuring the IRS makes progress on outstanding recommendations for improvement from both government and non-government watchdogs.
4. **Figuring out the real tax gap**: Before Congress allows the Biden administration to go on a spending spree with theoretical tax gap windfalls, the IRS should be forced to provide an updated estimate of the current tax gap and to demonstrate to Congress it can collect the kind of revenues the Biden administration is projecting for its plan. Without these safeguards, deficits and the debt may grow.

More on those recommendations below. First though, a brief overview of the tax gap, and why figuring out the true tax gap is such a confounding challenge for policymakers and experts alike.

The Tax Gap: $381 Billion? $1 Trillion? Or Somewhere In Between?

When the IRS discusses the tax gap, there are actually two separate numbers to keep in mind: 1) the *gross* tax gap, or the difference between federal taxes owed and federal taxes paid in a timely manner, and 2) the *net* tax gap, or the gross tax gap reduced by late tax payments or by IRS enforcement efforts that claw back revenue owed to the federal government. The oft-cited $381 billion figure is the agency's most recent (2019) estimate of the *net* tax gap, averaged across three tax years (2011-2013).

An IRS official recently told the Senate Finance Subcommittee on Taxation and IRS Oversight that, using a "new methodology" that the agency hopes will produce "more timely estimates and projections of the tax gap" in the future, the IRS estimates the *gross* tax

Key Facts:

President Biden's ambitious spending plans will only be deficit-neutral to the extent his proposed $80 billion IRS budget increase can raise $700 billion over 10 years.

Non-partisan analysis suggests that the Biden administration's projections are optimistic, and Congress should receive additional opinions before relying on those estimates.

Congress must also treat enhanced taxpayer rights as a prerequisite to additional IRS funding, rather than just window dressing for a bigger and bolder agency.

Lawmakers also need to ensure the IRS spends its new money in the right ways and addresses long-term deficiencies before spending tens of billions of dollars.

NTU's recommendations are intended to inform Congress as it exercises rigorous oversight of the Biden administration's IRS plans.

gap in 2019 was approximately $600 billion (or 36 percent higher than the 2011-2013 estimate of a $441 billion gross tax gap). The same official also told the Subcommittee that the IRS hopes to release a study on the 2014-2016 tax gap *next* year, which is the same six- to eight-year lag reflected in the 2019 study of the 2011-2013 gap.

The $600 billion estimate is, of course, 40 percent lower than the $1 trillion "off-the-cuff" guess from Commissioner Rettig earlier this year. Figuring out a true estimate of the current tax gap is critical to lawmakers' efforts to narrow the gap, as is getting a second opinion beyond just IRS estimates of the tax gap.

The IRS points to three components of the overall tax gap:

1. The *non-filing* gap: individuals, families, or businesses that owe taxes but do not file a tax return;
2. The *underreporting* gap: individuals, families, or businesses that underestimate or underreport their taxable income, and as a result do not pay as much in taxes as they owe; or
3. The *underpayment* gap: individuals, families, or businesses that properly report their income but do not pay their entire tax bill in a timely manner.

The IRS estimates that the non-filing and underpayment gaps *combined* make up only 21 percent of the gross tax gap. The other 79 percent, or $352 billion in tax years 2011-2013, is the underreporting gap. The plurality of that slice of the pie is the underreporting of business income, $110 billion or 25 percent of the overall gross tax gap. Understanding why and how the tax gap occurs is necessary for Congress and the IRS to determine where to focus their tax gap efforts.

Also important is an understanding of what type of untaxed income *makes up* the tax gap. The vast majority (71 percent of the gross gap) is individual income tax, which includes so-called "pass through" business income earned by S corporations, partnerships, and sole proprietorships. Another 18 percent is payroll taxes that fund Social Security and Medicare. Untaxed corporate income makes up another 9.5 percent. These estimates are also important to helping Congress and the IRS focus their efforts (and/or inform policymakers where *not* to waste dollars and efforts).

Senate Finance Committee Ranking Member Mike Crapo (R-ID) is seeking answers to some of these important questions about the tax gap, especially as it pertains to Commissioner Rettig's recent $1 trillion speculation. Specifically, Ranking Member Crapo wants to know:

- How much of the possible $1 trillion gap is attributable to growth in the dollar value and asset value of the $381 billion net gap from eight to 10 years ago;
- How much of the gap is attributable to cryptocurrency holdings which, the Ranking Member notes, are subject to significant and rapid changes in valuation; and
- How much of the gap is attributable to "unreported or concealed income offshore and in pass-through entities."

Understanding the answers to these questions is crucial to determining the accuracy of Commissioner Rettig's $1 trillion guess, and to future estimations of the tax gap.

Recommendations for Congress

The Biden proposal -- $80 billion in increased IRS funding over a decade and increased third-party reporting requirements for a projected $700 billion in recovered "tax gap" revenue -- is the talk of Washington, D.C. and reportedly has "some bipartisan appeal" among lawmakers in Congress. As experts and advocates on tax policy and IRS reform, NTU has more than a dozen recommendations for Congress and the IRS as it considers narrowing the gap. Lawmakers must proceed with caution, or else this proposed pot of money to the IRS could 1) violate taxpayer rights and due process, 2) be spent on the wrong investments, 3) cause the IRS to double down on current and past failures, 4) fail to narrow the tax gap as much as promised, or 5) some combination thereof. What follows are 14 recommendations, mostly for Congress as it considers Biden's American Families Plan. These recommendations are drawn not only from NTU's legislative experience and participation with the National Commission on Restructuring the IRS, but also our ongoing consultation with tax practitioners and former IRS senior managers.

Protecting Taxpayers' Rights

For decades, NTU has stood at the forefront of efforts to improve and expand taxpayers' rights and protections under the law -- and to guard against an overzealous or abusive IRS. Though a modest increase to the IRS budget for particular activities aimed at narrowing the gap *may* be in order, Congress must continue to rigorously conduct oversight of IRS activities and must first build upon work from legislation like the Taxpayer First Act (TFA), which became law thanks in part to the hard work of the late Rep. John Lewis (D-GA). The Biden administration plan calls for hiring over 86,000 new IRS employees over the next 10 years. Congress should ensure that those new employees understand and vigorously protect taxpayer rights, notwithstanding the significant challenges the agency faces in closing the tax gap.

1. **Pass additional taxpayer protections before making significant increases to the IRS budget**: Just last month, NTU reiterated its endorsement of legislation from Sen. John Cornyn (R-TX) to pass a Small Business Taxpayer Bill of Rights, which would create an alternative dispute resolution program for audits, give the IRS greater latitude to release levies that cause financial hardship, and strengthen safeguards against taxpayer abuses by IRS officers and agents, among other commendable provisions. Taxpayers' experience with the IRS's contradictory administrative behavior and its "courtroom crusades" against conservation easement deductions prove that Congress has plenty of work to do bolstering taxpayer rights before it gives the IRS $80 billion for more enforcement. The TFA was another major step forward for Congress. It created an Independent Office of Appeals to better protect taxpayers' rights, attempted to address poor IRS customer service performance, and required the IRS to deliver a restructuring plan to Congress (more on that below). However, as we noted to the Senate Finance Committee earlier this year, "important work lies ahead." Congress can improve upon TFA by developing new best practices. Lawmakers also need to rigorously monitor the implementation of the IRS Independent Office of Appeals. In other words, before Congress green-lights a significant increase to the IRS budget it should 1) ensure TFA implementation is proceeding on time and in a manner consistent with Congressional intent, and 2) build on the work of TFA by further improving taxpayer rights and due process. These could, with due deliberation, include:
    - A new mechanism for receiving, cataloging, and resolving taxpayer complaints over IRS employees, modeled after citizen review boards that currently monitor such complaints concerning big city police departments. Samuel Walker, a Professor of Criminal Justice at the University of Nebraska-Omaha, developed such a proposal that would apply to the IRS more than 20 years ago. It remains highly relevant today.

- Greatly expanded provisions allowing taxpayers to recover full attorney fees and damages if they prevail in court over IRS actions that were unjustified.
- Potential liability expansions or disciplinary measures for reckless behavior on the part of IRS agents, along with greater managerial incentives for conscientious employees who focus on taxpayer service and rights. Decades ago, Congressman Andy Jacobs (D-IN) proposed a legislative amendment that would have given judges some discretion to hold IRS employees liable for taxpayers' court costs when such employees acted arbitrarily and capriciously. Some may consider this step too drastic, but it is no longer completely out of place in what has become a national discussion over law enforcement liability reforms.
- Provide statutory reform of the Anti-Injunction Act, Declaratory Relief Act, and Federal Tort Claims Act, all of which combine to effectively prevent most taxpayers from enforcing their rights in court until after they have suffered harm. Recently the U.S. Supreme Court ruled unanimously to curtail somewhat the reach of the Anti-Injunction Act, but much more clarity is needed.
- Put legislative teeth into how Executive Orders 13891 and 13892, as well as the Administrative Procedure Act, apply to IRS rulemakings and guidance. This area of law has, as well, been a topic of litigation in the nation's highest court.

These and other steps in the direction of more robust taxpayer rights and remedies should be *prerequisites* for additional funding, rather than window dressing for the agency's new pot of cash.

2. **Ensure integration between a) the IRS reorganization plan under TFA and b) any new and significant appropriations to the IRS budget**: In January of this year, the IRS submitted a lengthy and detailed reorganization plan based on TFA requirements. The reorganization plan would make significant changes to the IRS organizational chart, create a new Chief Taxpayer Experience Officer, create a new Enterprise Change and Innovation Division, create a new Relationships and Services Division, and (concerningly) merge compliance functions by IRS employee expertise rather than type of taxpayer. This plan -- along with an IRS Modernization Plan submitted by the agency -- would require $4.1 billion in additional funds from fiscal years 2021 through 2025, according to the agency. Yet, it has not received even a modicum of scrutiny from Congress as to whether the plan is advisable or practical. The reviews so far from the private sector tax community have been mixed. As one of the less positive reviewers, longtime practitioner Stuart Bassin, noted:

> The taxpayer experience can only improve if the agency can make it easier for taxpayers to obtain answers to their questions from IRS employees, who have better access to the information required to accurately respond to the taxpayers' inquiries. ... [T]he report represents an initial collection of ideas, which require substantial further development, refinement, and even radical revision before the proposed reorganization strategy, customer service strategy, and training strategy can be implemented.

While President Biden is proposing giving the IRS a lot more than $4 billion over five years, Congress needs to ensure that the reorganization and modernization plans just recently submitted by the agency are fully integrated with the proposed new funding aimed at narrowing the tax gap. If the IRS does not have time to reorganize and modernize its operations, for example, Congress could be sending a hamstrung and behind-the-times agency a massive pile of money that it cannot spend efficiently and properly. In other words, more time and care is required to allow the IRS to catch up on its significant mandates under TFA.

3. **Require the IRS and/or Congress to quantify the potential costs of a beefed-up IRS budget to the private sector**: President Biden's American Families Plan would 1) provide the IRS with an additional $80 billion over 10 years, 2) "require financial institutions to report information on account flows so that earnings from investments and business activity are subject to reporting more like wages already are," and 3) give the IRS the authority to oversee paid tax preparers. Each of these planks could require additional time, manpower, or money from private sector entities, even those that are paying their taxes in full and on time. Indeed, a coalition of organizations representing the financial services sector recently wrote to Congress to warn them that the third-party reporting proposal "would impose cost and complexity that are not justified by the potential, and highly uncertain, benefits." Any significant increase in IRS audits could also put scores of honest taxpayers through the burdens of an audit, while financial institutions could have to hire additional personnel and devote significant additional resources to handing more cash-flow information over to the agency. While some of these initiatives may help narrow the tax gap, the agency should be required to furnish Congress with a good-faith estimate of how much these new proposals could cost the private sector.

4. **Require ongoing and robust reporting for the newly-designed Child Tax Credit before relying on tax gap recovery projections as a pay-for**: In 2014 the IRS estimated that 25 percent to 30 percent of Child Tax Credit (CTC) payments were improperly made, adding up to billions of dollars per year. Now, the CTC is going through a significant change -- as passed in the American Rescue Plan Act -- that, for 2021 only, increases both the size of the CTC and expands eligibility to millions more families. Biden's American Families Plans would extend this expanded CTC through 2025. While NTU has written favorably of some CTC expansion plans, such as the Family Security Act from Sen. Mitt Romney (R-UT), we are concerned about the potential for increased improper or fraudulent payments in this new version of the CTC. Recent reports have indicated that the expanded monthly benefit will be difficult for the IRS to implement. Verifying current and continuous eligibility for some families may be challenging, and as with the pre-American Rescue Plan version of CTC there is the potential for high rates of fraud. Congress should require the IRS to report regularly on its progress in a) implementing the new CTC and b) monitoring the program for fraud or improper payments.

Spending IRS Money Correctly

5. **Require the IRS to provide Congress (and the public) with a detailed plan for how it would spend an additional $80 billion over 10 years**: The public-facing version of the Biden administration's plan for additional IRS funding currently amounts to just a few dozen pages in an outline recently released by the Treasury Department. While we understand that all lengthy plans take time to develop, Congress should *not* green-light a significant increase to the IRS budget without a clear, line-item plan from the Biden administration and IRS Commissioner Rettig detailing how the agency would spend the money. From there, Congress should hold hearings where they can question IRS and White House officials about their spending plan. Congress should also revise the plan where they see fit, given the legislative branch ultimately controls when and how federal funds are spent (and, indeed, how much money is spent). This process should also be as public as possible, so that non-government stakeholders like NTU have the chance to weigh in with their expertise and advocacy.

6. **Require the IRS to participate in a budget consultation process that will consist of planning, formulation, and execution not only with senior IRS managers but also frontline staff and stakeholders**: The IRS Restructuring and Reform Act (RRA) of 1998 established an IRS Oversight Board (consisting of non-government and government members) to "oversee the IRS in its administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws and tax conventions." Part of the Board's duties were to "review and approve the IRS budget request" every year. Unfortunately, the Board currently does not have a quorum, rendering it useless, and -- as Sen. Rob Portman (R-OH) pointed out in a hearing last year -- "has not [been] supported" by any "administration since [its passage into law]." Sen. Portman has some thoughtful ideas to re-establish and re-invigorate the Board, with oversight of -- among other things -- "customer service, IT modernization, budgeting," and more. Re-establishing the Board could be a key step to ensuring the IRS avoids waste or abuse of its new funding, whether at the level of $80 billion over 10 years or some other number. If Congress would rather consider another structure, so be it, but the importance of such an entity harnessing private sector talent to focus on managerial concerns at the IRS cannot be overstated. As NTU testimony from September 2017 put it:

    > Congress could pursue several alternatives to the current Oversight Board. One is to work with the Administration to identify more full-time nominees and staff who can devote additional hours to the Oversight Board's mission. That mission could be further clarified so as to distinguish it from Treasury and IRS Advisory Groups as well as the National Taxpayer Advocate and Treasury Inspector General for Tax Administration. The Board could focus on providing practical private-sector guidance to the IRS on meeting the goals of its strategic plan and embracing innovation (such as ADR techniques). Further, the Board could analyze data and feedback from other bodies such as the Taxpayer Advocacy Panels to provide direct, ongoing input to Congress on legislative responses to some of the most pressing tax administration issues.

7. **Require the IRS to furnish Congress (and the public) with an action plan for reducing the tax gap for nonfarm proprietor income (that nonetheless protects small business taxpayers' rights)**: According to the most recent IRS study of the tax gap, the single largest component of the gap is underreporting of non-farm proprietor income -- a total of $68 billion, or more than 15 percent of the estimated gross tax gap. This is a larger gap than the entire non-filing gap or the entire underpayment gap. It's a larger gap than the underreporting of corporate income tax, and it's larger than the gap for underreporting on non-business individual income. Given this is the largest slice of the tax gap pie, the IRS should have a detailed plan for reducing this gap in particular. That action plan should include steps to protect the due process rights of small businesses who report income on individual returns (so-called "pass-through income"). Another useful element of such a plan would be to compare the cost-effectiveness of alternative strategies for closing this gap. For example, would creation of an administrative quadrennial simplification process for tax law affecting small business, along with more resources to promulgate advance guidance, yield better compliance (and revenue) than relying more heavily on examinations and investigations? Such research is not, and should never be, beyond the capabilities of IRS technical experts.

8. **Ensure that funding is not earmarked for enforcement alone, and does not come with mandatory minimum audit requirements**: As NTU Foundation wrote in its recent policy paper: "enforcement efforts have succeeded in raising the compliance rate by an average of 2.2 percent. It's not at all clear that an agency with this kind of history is capable of efficiently

spending billions in new funding." NTU Foundation has encouraged a more holistic approach to narrowing the tax gap, which must include efforts to improve outdated and ineffective IRS technology and to reduce improper or fraudulent payments coming from the agency. This recommendation, is of course, tied to numerous other recommendations in this paper, such as requiring a report from the IRS on how it plans to spend $80 billion over 10 years. However, it is worth reiterating that an additional dollar to enforcement alone *may or may not* narrow the tax gap, depending on which part of the gap the agency plans to pursue or how the agency plans to spend its money. Investing in agency improvements may provide a greater return on investment than simply beefing up the enforcement division alone, as a recent NTU Foundation paper explains.

Improving the Agency

9. **Require that the IRS fulfill -- or make significant progress on -- numerous Government Accountability Office (GAO) and Treasury Inspector General for Tax Administration (TIGTA) recommendations before increasing their budget**: As of May 2021, the IRS has 243 open and unfulfilled recommendations from the non-partisan GAO. The oldest open recommendation dates to 2009, and the most recent dates to earlier in May 2021. The recommendations cover topics like quality assurance in delivering expanded CTC payments, better tracking of refund processing, security risks at the agency, and improvements to third-party information reporting. Fifteen recommendations, dating back to 2014, are deemed "priority recommendations" that GAO says "can save large amounts of money, help Congress make decisions on major issues, and substantially improve or transform major government programs or agencies." Some priority recommendations concern efforts to prevent and monitor business identity theft, coordinate cybersecurity efforts to protect taxpayer information, and improve timely transfer of taxpayer appeals requests to the IRS Independent Office of Appeals. While it is impractical for Congress to require that the IRS complete action on all 243 open GAO recommendations before the legislature green-lights a budget increase, Congress could require progress on priority recommendations and/or some more recent and time-sensitive recommendations before sending $80 billion to the agency. Meanwhile, the latest semiannual report to Congress from TIGTA identified 155 "significant unimplemented corrective actions" recommended by TIGTA to the IRS since May 2007. With hundreds of recommendations outstanding from GAO and TIGTA, it seems irresponsible to give the IRS such a significant increase in funds without some meaningful progress on the most important of the above, outstanding recommendations.

10. **Require an action plan from the IRS on reducing the tax return backlog before significantly increasing the IRS budget**: According to recent reports, the IRS has a backlog of "1.7 million returns still in process that were filed before 2021." Since putting tax return dollars in the hands of millions of Americans can and should be a higher and more immediate priority than narrowing the tax gap (which will be a multi-year or even multi-decade effort), Congress should require the IRS to furnish an action plan for reducing this backlog as much as possible before green-lighting an $80 billion budget increase.

11. **Require an action plan from the IRS on phasing in universal electronic returns before significantly increasing the IRS budget**: As NTU Foundation's Demian Brady has pointed out before, "[p]rivate sector tax preparation software had long allowed users to complete [tax] forms electronically, but the government took years to catch up with the times." Brady notes that the IRS finally allowed taxpayers to file amended returns electronically in May of 2020 amidst a global pandemic that challenged taxpayers across the country. In the 21st century, taxpayers should be able to file all returns electronically, though the IRS can and should

continue to provide mail-in options for taxpayers who may not have ready or easy access to the internet. Given the importance of reducing taxpayer time and compliance burdens with the agency, Congress could require an action plan from the IRS on universal electronic returns before it approves an $80 billion budget increase over the next decade. If the tax agency's leadership is sufficiently motivated to commit to this goal, they will have plenty of private-sector expertise that can guide them. The Free File Alliance is just one example of the technology that exists to expand e-filing Service-wide.

Figuring Out the Real Tax Gap

12. **Demand an updated study from the IRS on the present tax gap, and sources of uncertainty in the estimates, before allowing tax gap projections to be included as a pay-for**: Of course, a major mystery in Congressional and administrative efforts to narrow the tax gap is, as noted above, figuring out just exactly how large the tax gap is. The last estimate from the IRS, completed nearly two years ago, covers tax years 2011-2013 -- eight to ten years ago. Though the IRS is reportedly working on a 2022 study for tax years 2014 through 2016, and though data lag continues to be an issue in providing up-to-date estimates of the tax gap, Congress should require a more robust analysis from the IRS of the present-day tax-gap estimated using new IRS methodologies referenced by an official in recent testimony to the Senate Finance Committee. Congress could then have an idea of how close or far off Commissioner Rettig is with his recent $1 trillion guess, or how close or far off Treasury Secretary Janet Yellen is with her $700 billion estimate. The IRS should also be clear with Congress and the public where there are uncertainties in the tax gap estimate. Though the agency has done just that in recent tax gap estimates, Congress could require additional measures of uncertainty such as a confidence interval.

13. **Require a 'second opinion' from the Congressional Budget Office (CBO) and/or additional nonpartisan experts on potential tax gap returns from an $80 billion increase to the IRS budget and increased third-party reporting requirements**: As NTU Foundation pointed out in its recent policy paper on the tax gap, CBO estimated just last year that a $20 billion increase to the IRS budget would yield a $61 billion increase in revenues and a $40 billion budget increase would yield a $103 billion increase in revenues (all over 10 years). These estimates of return-on-investment, $3.05 to $1 and $2.575 to $1, respectively, are lower than the Biden Treasury Department's recent estimate of $4 to $1. Subject to even more uncertainty is the Biden administration's prediction that it can raise an additional $460 billion from enhanced third-party reporting requirements. Given the explanation for this estimate currently amounts to a few paragraphs, this reads as little more than a half-trillion-dollar bet at the moment. In other words, Congress should not be satisfied with an IRS and/or Biden administration estimate alone, and should ask CBO to study what revenue the Biden administration's tax gap plan could yield.

14. **Require a 'proof of concept' from the IRS on narrowing the tax gap before tax gap revenues are 'spent' on new programs and priorities**: All of the uncertainty mentioned above means it would be irresponsible for lawmakers to rely on projected, theoretical revenues from narrowing the tax gap to pay for new, expensive programs and initiatives. Congress should require the IRS to demonstrate it can reach certain revenue targets with its new funding -- a 'proof of concept,' for lack of a better term -- before it uses the additional revenues for anything other than contributions to the Department of Treasury's General Fund. This 'proof of concept' should also take place over several years, given -- if IRS prioritization is correct -- initial revenues from narrowing the tax gap will largely reflect low-hanging

fruit. If Congress proceeds with this recommendation, though, it must take care to avoid incentivizing overzealous or abusive behavior at the IRS as it seeks to meet tax gap revenue targets. This is but one reason why a taxpayer bill of rights is critical to any tax gap push.

Conclusion

Narrowing the tax gap will be a significantly challenging initiative for both Congress and the IRS. The tax gap will never be zero -- and, indeed, at some point additional IRS funding for purposes of narrowing the tax gap will reach a point of diminishing returns that actually waste taxpayer money rather than benefiting taxpayers. Of course, an important principle throughout our recommendations to Congress and the agency is that protecting taxpayer rights and due process -- for taxpayers large and small, rich and poor alike -- is a *prerequisite* for additional spending, not a mere verbal commitment we expect from the agency.

If the IRS can demonstrate progress on protecting taxpayer rights, solving current agency deficiencies, and improving taxpayers' experience with the agency, then some additional funding for purposes of narrowing the gap may be a worthwhile investment for Congress and taxpayers. If the IRS can then demonstrate that the tax gap is as large as the agency says it is, and that the agency can collect on the portion of the tax gap the administration says it can, then -- and only then -- can Congress consider counting additional tax gap revenues as a way to pay for new spending. Of course, as an organization deeply concerned with fiscal responsibility in the federal budget, we would insist that any new revenues be devoted to paying down the nation's $28 trillion debt.

While narrowing the tax gap can and should remain an important goal for policymakers, we hope the above recommendations make clear that Congress and the IRS have a lot of more basic work in front of them first.

About the Authors

Andrew Lautz is the Director of Federal Policy with National Taxpayers Union.

Pete Sepp is the President of National Taxpayers Union.

NATIONAL TAXPAYERS UNION

2021 National Taxpayers Union
122 C Street NW, Suite 650, Washington, DC 20001
ntu@ntu.org