



Testimony
Before the Committee on Ways and
Means, House of Representatives

For Release on Delivery
Expected at 10:00 a.m.
Thursday, May 9, 2019

TAX GAP

Multiple Strategies Are Needed to Reduce Noncompliance

Statement of James R. McTigue, Jr., Director,
Strategic Issues

Accessible Version

GAO Highlights

Highlights of [GAO-19-558T](#), a testimony before the Committee on Ways and Means, House of Representatives

Why GAO Did This Study

The tax gap—the difference between tax amounts that taxpayers should have paid and what they actually paid voluntarily and on time—has been a persistent problem for decades. The tax gap estimate is an aggregate estimate of the five types of taxes that IRS administers—individual income, corporation income, employment, estate, and excise taxes. For each tax type, IRS attempts to estimate the tax gap based on three types of noncompliance: (1) underreporting of tax liabilities on timely filed tax returns; (2) underpayment of taxes due from timely filed returns; and (3) nonfiling, when a taxpayer fails to file a required tax return on time or altogether.

This testimony discusses factors contributing to the tax gap and strategies to reduce it. This testimony is based on prior GAO reports on the tax gap and enforcement of tax laws, including those with open recommendations or matters for congressional consideration that could help reduce the tax gap.

Enforcement of tax laws has been on GAO's High Risk List since its inception in 1990, and GAO has made various recommendations to IRS and suggestions to Congress to reduce the tax gap that have resulted in improvements. For example, GAO recommended that IRS consider comparing individuals' tax returns with the information educational institutions report to verify taxpayers' education tax benefits claims and suggested that Congress require brokers to report to both taxpayers and IRS the adjusted cost of the securities sold by taxpayers. These actions resulted in billions of dollars in additional revenue.

View [GAO-19-558T](#). For more information, contact James R. McTigue, Jr. at (202) 512-9110 or McTigueJ@gao.gov.

May 9, 2019

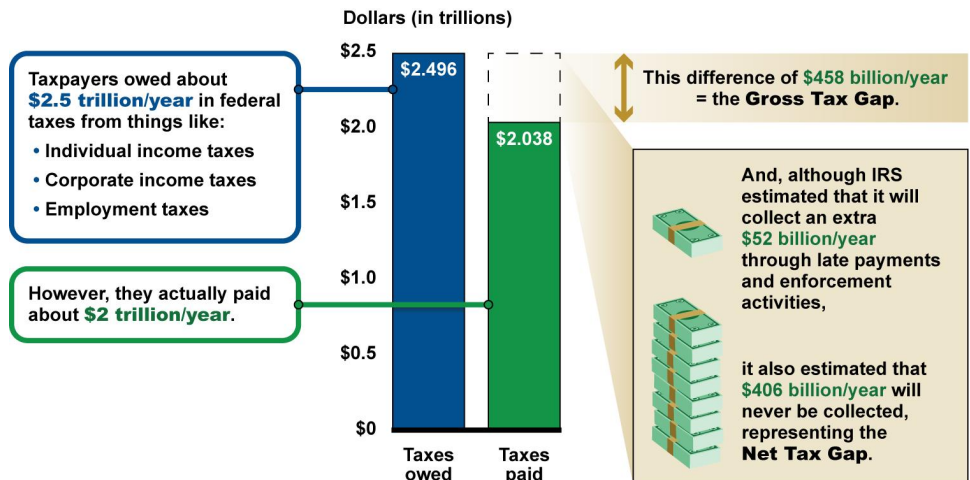
TAX GAP

Multiple Strategies Are Needed to Reduce Noncompliance

What GAO Found

The Internal Revenue Service's (IRS) latest tax gap estimate (2016) found that taxpayers voluntarily and timely paid about 81.7 percent of owed taxes for tax years 2008-2010, leaving an annual gross tax gap of \$458 billion. IRS estimated a net tax gap—after late payments and enforcement actions—of \$406 billion.

IRS's Annual Average Tax Gap Estimate for Tax Years 2008-2010



Data of highlights figure IRS's Annual Average Tax Gap Estimate for Tax Years 2008-2010

	Dollars (in trillions)
Taxes owed	\$2,496 Taxpayers owed about \$2.5 trillion/year in federal taxes from things like: <ul style="list-style-type: none"> Individual income taxes Corporate income taxes Employment taxes
Taxes paid	\$2,038 However, they actually paid only about \$2 trillion/year. This difference of \$458 billion/year = the Gross Tax Gap. And, although IRS estimated that it will collect an extra \$52 billion/year through late payments and enforcement activities, it also estimated that 406 billion/year will never be collected, representing the Net Tax Gap.

GAO's work has found that three important factors contribute to the tax gap.

- **Limited third party information reporting.** The extent to which individual taxpayers accurately report their income is closely aligned with whether third parties (e.g., employers) report income (e.g., wages) to them and to IRS.
- **IRS resource tradeoffs.** IRS's budget and staffing levels have fallen over the past decade, and IRS faces increasing responsibilities, such as implementing Public Law 115-97—commonly known as the Tax Cuts and Jobs Act—which involved significant changes to tax law.
- **Tax code complexity.** The federal tax system contains complex rules that may be necessary to appropriately target tax policy goals; however, this can engender errors and lead to underpaid taxes.

GAO's work has demonstrated that no single approach will fully and cost-effectively address noncompliance since the problem has multiple causes and spans different types of taxes and taxpayers. In light of these challenges, GAO has made numerous recommendations to IRS—some of which have not yet been implemented—such as developing and documenting a strategy that outlines how IRS will use data to update compliance approaches to help address the tax gap. Reducing the tax gap will also require targeted legislative actions. For example, expanding third-party information reporting could increase voluntary compliance and providing IRS with the authority to regulate paid tax return preparers could improve the accuracy of the tax returns they prepare.

Chairman Neal, Ranking Member Brady, and Members of the Committee:

I am pleased to be here today to discuss the tax gap—the difference between tax amounts that taxpayers should pay and what they actually pay voluntarily and on time. The most recent data available show that, in 2016, the Internal Revenue Service (IRS) estimated an average annual gross tax gap of \$458 billion for tax years 2008 to 2010. IRS estimated that through late payments and enforcement actions, it will collect an additional \$52 billion annually for tax years 2008 to 2010, resulting in an average annual net tax gap of \$406 billion.

The tax gap has been a persistent problem for decades, and enforcement of tax laws has been on our High Risk List since its inception in 1990.¹ We have previously reported that there are no easy fixes to this problem, and given persistent levels of noncompliance, reducing the tax gap will not likely be achieved through a single solution. Rather, the tax gap must be attacked on multiple fronts with multiple strategies over a sustained period of time.

Even modest reductions to the tax gap would yield significant financial benefits and help improve the government's fiscal position. For example, just a 1 percent reduction of the 2008-2010 average annual net tax gap would have resulted in about \$4 billion more in annual revenue for those years. For illustrative purposes, for fiscal year 2019, this amount of revenue could fund about 82 percent of IRS's enforcement budget; the entire operation of the U.S. Census Bureau; or the combined federal budgets of the national park system Operations account, Smithsonian Institution, and the National Archives and Records Administration.²

My testimony today discusses (1) factors contributing to the tax gap and (2) strategies for reducing the tax gap. My comments are based on prior

¹Every 2 years, we issue a list of programs and operations that are "high risk" due to their vulnerabilities to fraud, waste, abuse, and mismanagement, or that need transformation. Progress in addressing areas on this list has led to more than \$350 billion in financial benefits to the federal government in the past 13 years. For the most recent update, from March 2019, see GAO, *High-Risk Series: Substantial Efforts Needed to Achieve Greater Progress on High-Risk Areas*, [GAO-19-157SP](#) (Washington, D.C.: Mar. 6, 2019).

²For fiscal year 2019, IRS's enforcement budget was \$4.86 billion; the entire operation of the U.S. Census Bureau was \$3.8 billion; and the combined budgets of the national park system Operations account (\$2.5 billion), Smithsonian Institution (\$1.0 billion), and the National Archives and Records Administration (\$0.4 billion) was about \$4 billion.

reports on the tax gap and enforcement of tax laws, including those with open recommendations or matters for congressional consideration that could help reduce the tax gap.³ The products cited throughout this statement include detailed explanations of the methods used to conduct our work. We conducted the work on which this statement is based in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

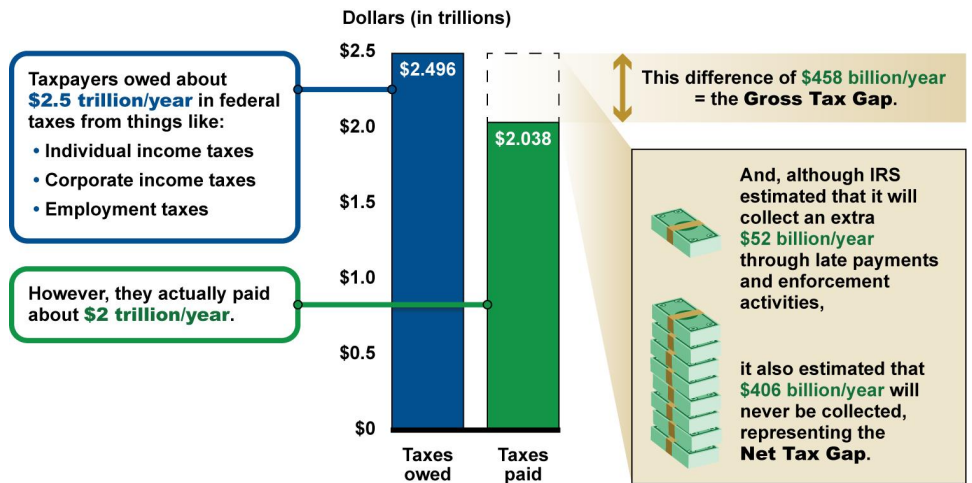
Background

In April 2016, IRS released its most recent tax gap estimate, stating that taxpayers should have paid an average of about \$2.5 trillion dollars per year in federal taxes for tax years 2008 to 2010. Of this amount, IRS estimated that taxpayers voluntarily and timely paid about 81.7 percent, or \$2.04 trillion, leaving \$458 billion in unpaid taxes per year, as shown in figure 1.⁴

³For example, see GAO, *Internal Revenue Service: Strategic Human Capital Management is Needed to Address Serious Risks to IRS's Mission*, [GAO-19-176](#) (Washington, D.C.: Mar. 26, 2019); *Tax Gap: IRS Needs Specific Goals and Strategies for Improving Compliance*, [GAO-18-39](#) (Washington, D.C.: Oct 31, 2017); *Fiscal Outlook: Addressing Improper Payments and the Tax Gap Would Improve the Government's Fiscal Position*, [GAO-16-92T](#) (Washington, D.C.: Oct 1, 2015); *Tax Gap: IRS Could Do More to Promote Compliance by Third Parties with Miscellaneous Income Reporting Requirements*, [GAO-09-238](#) (Washington, D.C.: Jan. 28, 2009); and *Tax Gap: Actions That Could Improve Rental Real Estate Reporting Compliance*, [GAO-08-956](#) (Washington, D.C.: Aug. 28, 2008).

⁴In its financial statements, IRS reported that taxpayers paid an average of \$2.5 trillion per year for 2008–2010. However, this figure represents gross collections, which includes amounts to be refunded to taxpayers, as well as penalties, interest, and enforcement revenue, which are not paid voluntarily. Additionally, the financial statement amounts are calculated on a fiscal year basis, while the tax gap is calculated on a tax year basis.

Figure 1: IRS's Annual Average Tax Gap Estimate for Tax Years 2008 to 2010



Source: Internal Revenue Service (IRS). | GAO-19-558T

Data from Figure 1: IRS's Annual Average Tax Gap Estimate for Tax Years 2008 to 2010

	Dollars (in trillions)
Taxes owed	<p>\$2,496</p> <p>Taxpayers owed about \$2.5 trillion/year in federal taxes from things like:</p> <ul style="list-style-type: none"> • Individual income taxes • Corporate income taxes • Employment taxes
Taxes paid	<p>\$2,038</p> <p>However, they actually paid only about \$2 trillion/year.</p> <p>This difference of \$458 billion/year = the Gross Tax Gap.</p> <p>And, although IRS estimated that it will collect an extra \$52 billion/year through late payments and enforcement activities, it also estimated that \$406 billion/year will never be collected, representing the Net Tax Gap.</p>

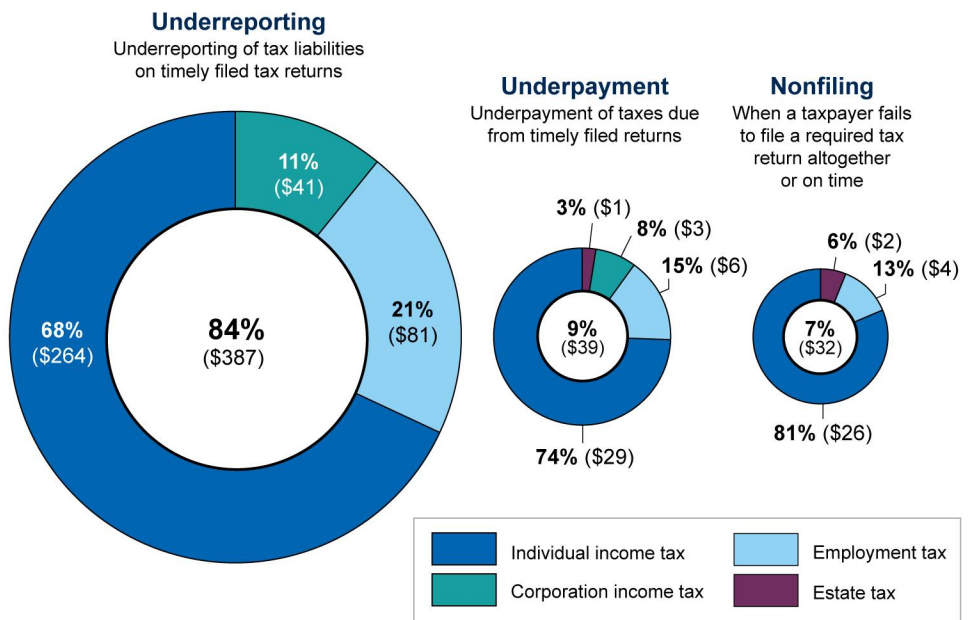
The tax gap estimate is an aggregate estimate of the five types of taxes that IRS administers—individual income, corporation income,

employment, estate, and excise taxes.⁵ For each tax type, IRS attempts to estimate the tax gap based on three types of noncompliance: (1) underreporting of tax liabilities on timely-filed tax returns; (2) underpayment of taxes due from timely-filed returns; and (3) nonfiling, when a taxpayer fails to file a required tax return altogether or on time.

Underreporting of tax liabilities accounted for most of the tax gap estimate for tax years 2008 to 2010, making up 84 percent of the entire estimated gross tax gap, as shown in figure 2.

Figure 2: Estimated Average Annual Gross Tax Gap by Type of Noncompliance and Tax, Tax Years 2008 to 2010

Dollars (in billions)



Source: GAO analysis of Internal Revenue Service (IRS) information. | GAO-19-558T

Data table for Figure 2: Estimated Average Annual Gross Tax Gap by Type of Noncompliance and Tax, Tax Years 2008 to 2010

Dollars (in billions)

⁵Employment taxes include both employer-withheld employment taxes and self-employment taxes.

Pie chart 1: Underreporting

- Total of all three types: 84% (\$387)
- Individual income tax: 68% (\$264)
- Corporation income tax: 11% (\$41)
- Employment tax: 21% (\$81)
- Estate tax: none

Pie chart 2: Underpayment

- Total of all three types: 9% (\$39)
- Individual income tax: 74% (\$29)
- Corporation income tax: 8% (\$3)
- Employment tax: 15% (\$6)
- Estate tax: 3% (\$1)

Pie chart 3: Nonfiling

- Total of all three types: 7% (\$32)
- Individual income tax: 81% (\$26)
- Corporation income tax: none
- Employment tax: 13% (\$4)
- Estate tax: 6% (\$2)

Note: Data may not sum to totals because of rounding. Individual income tax includes individual business income tax. Estate tax underreporting noncompliance is not shown in this graphic because it represents less than one-half percent of total underreporting noncompliance. Excise tax is not shown in this graphic because IRS does not have excise tax underreporting noncompliance or nonfiling noncompliance estimates, and its estimate for excise tax underpayment noncompliance represents less than one-half percent of total underpayment noncompliance. In addition, IRS does not have a corporation income tax estimate for nonfiling noncompliance.

Individual income taxes made up the largest portion (\$264 billion) of underreporting. Underreporting of business income accounted for nearly half (\$125 billion) of that amount, as shown in table 1. Business income

underreporting includes income from sole proprietors, which accounted for the largest share (\$78 billion) of individual income tax underreporting.⁶

Table 1: Estimated Average Annual Individual Income Underreporting Tax Gap by Tax Return Item or Category, Tax Years 2008 to 2010

Dollars in billions

Tax return items or category	Tax gap estimate
Business income	125
Sole proprietor income	78
Income from partnerships, S corporations, estates/trusts	22
Rents and royalties	20
Farming income/loss	5
Non-business income	64
Other income ^a	29
Capital gains	11
Taxable Social Security benefits	7
Pensions and annuities	5
Wages	5
Business sale/Form 4797 income	4
Dividends	1
Interest	1
State income tax refunds	1
Unemployment compensation	1
Credits	40
Earned income tax credit	27
Child tax credit	7
Education credits	4
Other credits	2
Deductions	18
Unallocated marginal effects ^b	12
Exemptions	6
Filing status	5

⁶Sole proprietors are self-employed individuals who should file a Schedule C with their individual tax return to report profits and losses from their business. Sole proprietors include those who provide services, such as doctors or accountants; produce goods, such as manufacturers; and sell goods, such as car dealers and grocers.

Tax return items or category	Tax gap estimate
Other taxes	1
Adjustments ^c	-5
Total individual income underreporting	264

Source: Internal Revenue Service data. | GAO-19-558T

Note: Data may not sum to total because of rounding.

^aOther income includes any taxable income not reported elsewhere on the tax return or other schedules—such as gambling winnings, rental of personal property, and canceled debts—as well as deductions for net operating losses.

^bUnallocated marginal effects represent the difference between the total estimated tax gap for individual income tax underreporting and the sum of tax gap estimates of individual income tax underreporting by tax return line item. This discrepancy occurs whenever more than one line item has been underreported on the same tax return, leading to an understatement of the true tax gap.

^cAdjustments are the line items that are subtracted from the total income line to arrive at adjusted gross income. For the 2008–2010 estimate, the majority of the adjustments can be attributed to understated individual income tax deductions for self-employment tax. Underreported self-employment income can lead to an underreported self-employment tax liability, which, in turn, can lead to understated income tax deductions for self-employment tax.

IRS uses various approaches to estimate the different components of the tax gap. A primary source of information IRS uses is its National Research Program (NRP) study of individual tax returns. Through NRP, IRS examines a stratified, random sample of tax returns, and uses statistical modeling to produce estimates of noncompliance for the population of individual income tax return filers. Other areas of the tax gap are estimated using payment data or other statistical models. In 2016, IRS completed examinations for an NRP study on employment tax returns filed from tax years 2008 to 2010. IRS employees reported that they plan to start analyzing the results by June 2019. However, IRS has not provided plans for how it will use the results to update the current state of the employment tax gap estimate, as we previously recommended.⁷ The tax gap includes unintentional errors as well as intentional evasion, such as intentionally underreporting income, intentionally overreporting expenses, and engaging in abusive tax shelters or frivolous tax schemes.⁸

⁷GAO, *Employment Taxes: Timely Use of National Research Program Results Would Help IRS Improve Compliance and Tax Gap Estimates*, [GAO-17-371](#) (Washington, D.C.: Apr. 18, 2017).

⁸By definition, legal tax avoidance (i.e., legally lowering tax liability) is not included in the tax gap. IRS has not developed specific estimates for the tax gap related to income earned from illegal activities or certain forms of fraud. However, if IRS discovers these types of income over the course of an audit, it could be included in the tax gap estimates. In general, refund fraud related to identity theft would not be included in the tax gap estimate because it does not involve evading a tax liability.

As we have previously reported, completely closing the tax gap is not feasible, as it would entail more intrusive enforcement and more burdensome recordkeeping or reporting than the public is willing to accept, and more resources than IRS is able to commit.⁹ However, even modest reductions would yield significant financial benefits and help improve the government's fiscal position.

Tax noncompliance, even when unintentional, could discourage compliant taxpayers and undermines the integrity of the tax system and the public's confidence in it. For example, consider two groups of taxpayers with similar tax situations—those who pay the full amount of tax due and those who do not. Those who do not pay taxes are not meeting their obligation to fund government services, which, in effect, shifts the fiscal burden to those who do pay. Further, IRS devotes resources to attempt to collect taxes due from noncompliant taxpayers—resources that could be used for other purposes.

In addition, noncompliance can create an unfair competitive advantage among businesses because those that do not pay tax debts are avoiding costs that tax-compliant businesses are incurring. For example, our past investigations identified instances in which federal contractors with tax debts won awards based on price differentials over tax compliant contractors.¹⁰

⁹GAO, *Tax Gap: Sources of Noncompliance and Strategies to Reduce It*, [GAO-12-651T](#) (Washington, D.C.: Apr 19, 2012).

¹⁰We made recommendations to IRS, the Department of Defense (DOD), the Financial Management Service, and the Office of Management and Budget to address issues with delinquent federal contractors. See GAO, *Financial Management: Thousands of Civilian Agency Contractors Abuse the Federal Tax System with Little Consequence*, [GAO-05-637](#) (Washington, D.C.: June 16, 2005), and *Financial Management: Some DOD Contractors Abuse the Federal Tax System with Little Consequence*, [GAO-04-95](#) (Washington, D.C.: Feb. 12, 2004).

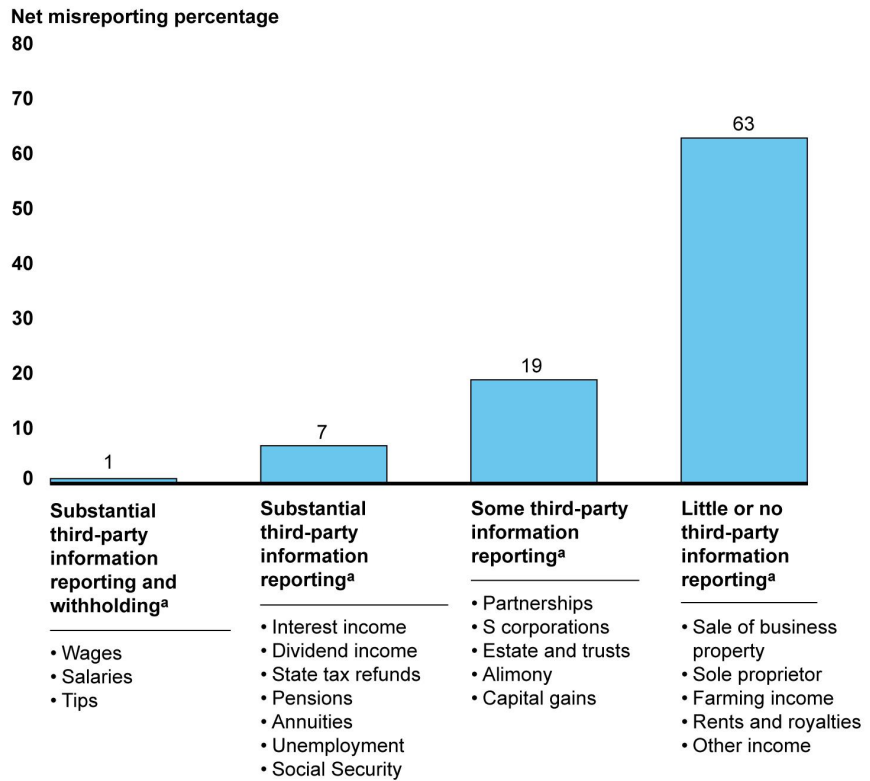
Key Factors Contributing to the Tax Gap Include Limited Third-party Information Reporting, Resource Trade-offs, and Complexities in the Tax Code

Our past work has found that three important factors contributing to the tax gap are the extent to which income is reported to IRS by third parties, IRS's resource trade-offs, and tax code complexity.

Limited Third-Party Information Reporting

As we have previously reported, the extent to which individual income tax taxpayers accurately report their income is closely aligned with the amount of income that third parties report to them and to IRS. For example, according to 2008–2010 IRS data, taxpayers misreported more than half of the types of income for which there is little or no third-party information reporting, such as business income (see figure 3). In contrast, when employers both withheld taxes from, and reported information on, wages and salaries to employees and IRS (through Form W-2, Wage and Tax Statement), taxpayers misreported on only 1 percent of such income. Similarly, taxpayers misreported less than 10 percent of investment income that banks and other financial institutions reported to account holders and IRS (through Forms 1099).

Figure 3: Effect of Third-Party Information Reporting on Individual Income Tax Compliance, Tax Years 2008 to 2010



Source: GAO analysis of Internal Revenue Service (IRS) information. | GAO-19-558T

Data table for Figure 3: Effect of Third-Party Information Reporting on Individual Income Tax Compliance, Tax Years 2008 to 2010

Category	Net
Substantial information reporting and withholding	1
Substantial information reporting	7
Some information reporting	19
Little or no information reporting	63

Note: Net misreporting percentage is the sum of the net misreported amount divided by the absolute values (over or underreported) of the amounts that should have been reported, expressed as a percentage.

^aIRS receives information from third parties that it uses to verify income or deduction amounts that taxpayers report on their tax returns. IRS categorized various line items on the individual income tax return into four different groupings of third-party reporting in IRS Publication 5161, *Estimation of the Underreporting Tax Gap for Tax Years 2008–2010: Methodology Research, Analysis and Statistics*

Technical Paper, September 2016. However, IRS did not provide a scale to define the differences between substantial, some, and little or no third-party information reporting.

For items subject to substantial third-party information reporting, IRS is able to use automated processes to address noncompliance. The automated underreporter program, through which IRS matches amounts reported on tax returns with amounts reported on information returns submitted by third parties, is one such process. This computer matching program allows IRS to identify discrepancies between tax returns and information returns, and propose automatic changes to taxpayers.¹¹ For items with little to no third-party information reporting, IRS must rely on more resource-intensive methods, such as correspondence or face-to-face examinations, to address noncompliance. While these examinations may be started by reviewing specific tax return line items, they may also be expanded to cover other areas of the tax returns if there are indications of misreporting in areas of the return not previously identified. However, it is harder for IRS to detect noncompliance in areas with little third-party information reporting.

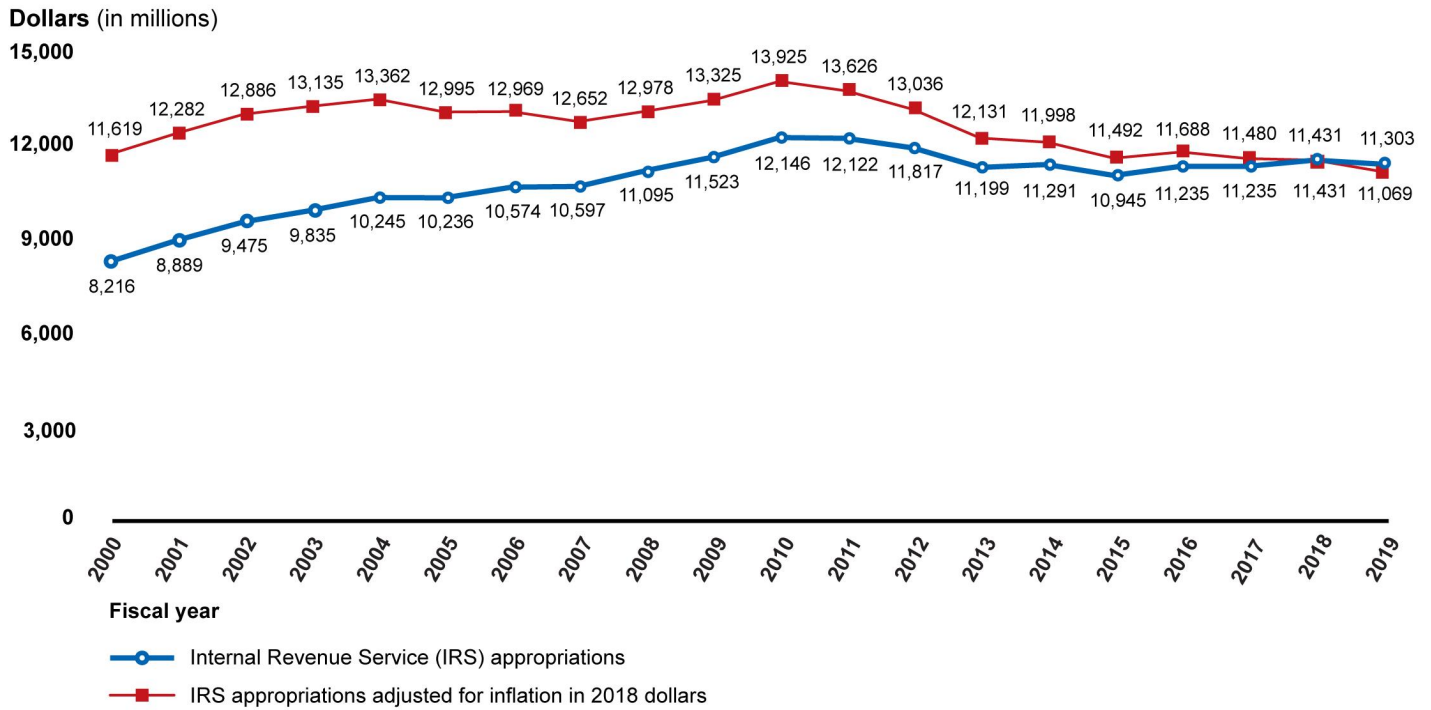
IRS Resource Trade-offs

IRS's budget declined by about \$2.6 billion (18.8 percent) from fiscal years 2011 through 2019, and IRS's budget for fiscal year 2019 is less than its fiscal year 2000 budget, after adjusting for inflation (see figure 4).¹²

¹¹Sometimes, if the discrepancy exceeds a certain tax threshold, an automated underreporter reviewer will contact a taxpayer asking for an explanation of the discrepancy or payment if additional taxes are assessed.

¹²In 2018 dollars.

Figure 4: IRS Appropriations Nominal and Inflation Adjusted (2018 Dollars, in Millions), from Fiscal Years 2000 through 2019



Sources: GAO analysis of Congressional Research Service reports for fiscal years 2000 through 2004, Internal Revenue Service Congressional Justifications for fiscal years 2005 through 2020. GAO-19-558T

Data Table for Figure 4: IRS Appropriations Nominal and Inflation Adjusted (2018 Dollars, in Millions), from Fiscal Years 2000 through 2019

Fiscal Year	IRS Appropriations	Appropriations in 2017 Dollars
2000	8,216	11,619
2001	8,889	12,282
2002	9,475	12,886
2003	9,835	13,135
2004	10,245	13,362
2005	10,236	12,995
2006	10,574	12,969
2007	10,597	12,652
2008	11,095	12,978
2009	11,523	13,325
2010	12,146	13,925
2011	12,122	13,626

Fiscal Year	IRS Appropriations	Appropriations in 2017 Dollars
2012	11,817	13,036
2013	11,199	12,131
2014	11,291	11,998
2015	10,945	11,492
2016	11,235	11,688
2017	11,235	11,480
2018	11,431	11,431
2019	11,303	11,069

Note: Inflation adjustments were made using Bureau of Economic Analysis data and Congressional Budget Office projections of the fiscal year chain weighted gross domestic product price index. The fiscal year 2008 enacted budget includes supplemental funding for Economic Stimulus payment of \$202.1M.

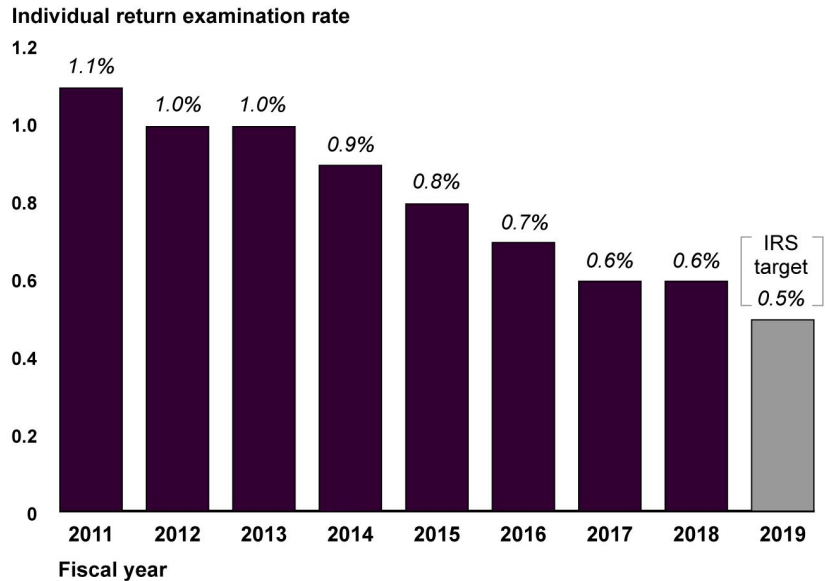
Since fiscal year 2011, IRS staffing has fallen from 95,544 full-time equivalent employees to an estimated 75,676 in fiscal year 2019, a 20.8 percent reduction. At the same time, IRS faces increasing responsibilities, such as implementing relevant aspects of Public Law 115-97, which included significant changes to corporate and individual tax law.¹³ IRS also faces ever-evolving and significant challenges protecting taxpayer information, preventing identity theft and fraud, and modernizing an aging technology infrastructure.

We previously reported that available staff has been a key factor in IRS decisions to scale back a number of program activities, such as examining tax returns, according to IRS officials.¹⁴ Our analysis of IRS data shows the rate of individual returns audited has declined between fiscal years 2011 and 2018 (see figure 5). Reducing examinations can reduce revenues collected through such enforcement action, and may indirectly reduce voluntary compliance.

¹³To provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018, Pub. L. No. 115-97, 131 Stat. 2054 (Dec. 22, 2017) (commonly referred to as the Tax Cuts and Jobs Act).

¹⁴[GAO-19-176](#).

Figure 5: Rates of Internal Revenue Service (IRS) Individual Income Tax Return Examinations, Fiscal Years 2011 through 2019



Source: GAO analysis of IRS Data Book data and the Congressional Budget Justification for IRS, fiscal year 2020. | GAO-19-558T

Data Table for Figure 5: Rates of Internal Revenue Service (IRS) Individual Income Tax Return Examinations, Fiscal Years 2011 through 2019

Fiscal Year	2011	2012	2013	2014	2015	2016	2017	2018	2019
Individual Return Examination Rate	1.1%	1.0%	1.0%	0.9%	0.8%	0.7%	0.6%	0.6%	0.5%

Tax Code Complexity

The federal tax system contains complex rules that may be necessary to appropriately target tax policy goals, such as providing benefits to specific groups of taxpayers. However, this complexity imposes a wide range of recordkeeping, planning, computing, and filing requirements upon taxpayers. For example, taxpayers who receive income from rents, self-employment, and other sources may be required to make complicated calculations and keep detailed records. This complexity can lead to errors and underpaid or overpaid taxes. Complexity, and the lack of transparency that it can create, can also exacerbate doubts about the tax system’s integrity.

Tax expenditures—tax credits, deductions, exclusions, exemptions, deferrals, and preferential tax rates estimated by the Department of the Treasury to reduce tax revenue by about \$1.38 trillion in fiscal year 2018—can add to tax code complexity. In part, this is because taxpayers must learn about, determine their eligibility for, and choose between tax expenditures that may have similar purposes. For example, as we reported in 2012, about 14 percent of filers in 2009 (1.5 million of almost 11 million eligible returns) did not claim an education credit or deduction for which they appeared eligible.¹⁵

The complexity involved with tax expenditures may be acceptable if they achieve their intended purposes.¹⁶ However, in many cases, their effectiveness is questionable or unknown. With some exceptions, tax expenditures generally are not subject to reauthorization and the annual congressional budget processes. We have recommended greater scrutiny of tax expenditures since 1994, as periodic reviews could help determine how well specific tax expenditures achieve their goals, and how their benefits and costs (including complexity) compare to those of other programs with similar goals.¹⁷ Such actions would help facilitate oversight and accountability of tax expenditures more in line with the performance management and reporting requirements of other federal programs.

Paid tax return preparers and tax software developers help taxpayers navigate the complexities of the tax code. However, some paid preparers may introduce their own mistakes. For example, in a limited study in 2014, we found that seven of 19 preparers who completed returns for our undercover investigators made errors with substantial tax consequences while, only two preparers calculated the correct refund amount.¹⁸

¹⁵GAO, *Higher Education: Improved Tax Information Could Help Families Pay for College*, [GAO-12-560](#) (Washington, D.C.: May 18, 2012).

¹⁶GAO, *Tax Expenditures: IRS Data Available for Evaluations Are Limited*, [GAO-13-479](#) (Washington, D.C.: Apr. 30, 2013).

¹⁷GAO, *Tax Expenditures: Opportunities Exist to Use Budgeting and Agency Performance Processes to Increase Oversight*, [GAO-16-622](#) (Washington, D.C.: July 7, 2016); *Tax Expenditures: Background and Evaluation Criteria and Questions*, [GAO-13-167SP](#) (Washington, D.C.: Nov. 29, 2012); *Government Performance and Accountability: Tax Expenditures Represent a Substantial Federal Commitment and Need to Be Reexamined*, [GAO-05-690](#) (Washington, D.C.: Sept. 23, 2005); and *Tax Policy: Tax Expenditures Deserve More Scrutiny*, [GAO/GGD/AIMD-94-122](#) (Washington, D.C.: June 3, 1994).

¹⁸GAO, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors*, [GAO-14-467T](#) (Washington, D.C.: Apr. 8, 2014).

Likewise, using NRP data, which are statistically representative, we estimated that 60 percent of returns prepared by preparers contained errors.

Multiple Strategies Are Needed to Reduce the Tax Gap

IRS's overall approach to reducing the tax gap consists of improving services to taxpayers, and enhancing enforcement of the tax laws. In spite of these efforts, the percentage at which taxpayers pay their taxes voluntarily and on time has remained relatively constant over the past three decades. Our past work has demonstrated that no single approach will fully and cost effectively address noncompliance since the problem has multiple causes and spans different types of taxes and taxpayers. In light of these challenges, we have made numerous recommendations to IRS that have not yet been implemented, as well as matters for congressional consideration. For example, in our most recent high-risk update, we highlighted various actions IRS should take to improve enforcement of tax laws and reduce the tax gap.¹⁹

- **Strategy for using compliance data.** Developing and documenting a strategy that outlines how IRS will use data to update compliance strategies could help address the tax gap. For example, a strategy that outlines how IRS plans to use NRP data to update compliance programs and approaches would help IRS determine resource trade-offs and more fully leverage the investment it makes in compliance research, while providing Congress with a better understanding of the merits of the research it is being asked to fund.²⁰

¹⁹[GAO-19-157SP](#). These recommendations represent only some of the recommendations we have made to IRS related to the enforcement of tax laws high-risk area. Among those recommendations are some we consider to be of highest priority—those that we believe warrant priority attention from heads of key departments or agencies. They are highlighted because, upon implementation, they may significantly improve government operation, for example, by realizing large dollar savings; eliminating mismanagement, fraud, and abuse; or making progress toward addressing a high-risk or duplication issue. For example, some priority recommendations address the need for IRS to improve taxpayer services, such as by developing strategies for providing web-based services to taxpayers and to improve telephone and correspondence services. For details of the 23 recommendations to IRS we believe should be given highest priority, see GAO, *Priority Open Recommendations: Internal Revenue Service*, [GAO-19-324SP](#) (Washington, D.C.: Apr. 4, 2019).

²⁰[GAO-18-39](#).

- **Voluntary compliance goal.** A long-term, quantitative goal for improving voluntary compliance may provide IRS with a concrete target the agency can use in fulfilling its mission. Without a quantitative goal, it will be more difficult for IRS to determine the success of its strategies, adjust its approach when necessary, and remain focused on results, especially since factors that affect compliance change over time.²¹
- **Analyzing employment tax NRP study results.** Developing and documenting plans to assess its NRP employment tax study results would help IRS (1) identify areas of noncompliance, (2) devise actions to address such noncompliance, and (3) update its employment tax gap estimate. Without completed analysis of the NRP employment tax study results, IRS risks using outdated data to make decisions about compliance and areas of the tax gap to pursue.²²
- **Leveraging the Return Review Program.** IRS's Return Review Program (RRP) is a tool to detect and select potentially fraudulent returns to prevent the issuance of invalid refunds. Evaluating the costs and benefits of expanding RRP to analyze individual returns not claiming refunds could support other enforcement activities by streamlining the detection and treatment of other types of noncompliance and fraud.²³

Given that the tax gap has been a persistent issue, reducing it will also require targeted legislative actions, such as those we highlighted in our 2019 high-risk update.²⁴

- **Additional third-party information reporting.** Expanding third-party information reporting to IRS could increase voluntary tax compliance. For example, reporting could be required for certain payments that rental real estate owners make to service providers, such as contractors who perform repairs on their rental properties, and for payments that businesses make to corporations for services.²⁵

²¹[GAO-18-39](#).

²²[GAO-17-371](#).

²³GAO, *Tax Fraud and Noncompliance: IRS Could Further Leverage the Return Review Program to Strengthen Tax Enforcement*, [GAO-18-544](#) (Washington, D.C.: July 24, 2018).

²⁴[GAO-19-157SP](#).

²⁵[GAO-09-238](#) and [GAO-08-956](#).

- **Enhanced electronic filing.** Requiring additional taxpayers to electronically file tax and information returns could help IRS improve compliance in a resource-efficient way. For example, expanding the mandate for corporations to electronically file their tax returns could help IRS reduce return processing costs, select the most productive tax returns to examine, and examine fewer compliant taxpayers.²⁶
- **Math error authority.** Providing IRS with authority—with appropriate safeguards—to correct math errors and to correct errors in cases where information provided by a taxpayer does not match information in government databases, among other things, could help IRS correct errors and avoid burdensome audits and taxpayer penalties.
- **Paid preparer regulation.** Providing IRS with the authority to regulate paid tax return preparers could improve the accuracy of the tax returns they prepare.²⁷

Chairman Neal, Ranking Member Brady, and Members of the Committee, this completes my prepared statement. I would be pleased to respond to any questions that you may have at this time.

GAO Contact and Staff Acknowledgements

If you or your staff have any questions about this testimony, please contact James R. McTigue, Jr. at (202) 512-9110 or mctiguej@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Key contributors to this testimony include Jeff Arkin, Assistant Director; Robyn Trotter, Analyst-in-Charge; A.J. Stephens; and Alicia White. Other staff who made key contributions to the reports cited in the testimony are identified in the source products.

²⁶GAO, *Partnerships and S Corporations: IRS Needs to Improve Information to Address Tax Noncompliance*, [GAO-14-453](#) (Washington, D.C.: May 14, 2014).

²⁷[GAO-14-467T](#). A previous study found similar results: see *Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors*, [GAO-06-563T](#) (Washington, D.C.: Apr. 4, 2006).

This is a work of the U.S. government and is not subject to copyright protection in the United States. The published product may be reproduced and distributed in its entirety without further permission from GAO. However, because this work may contain copyrighted images or other material, permission from the copyright holder may be necessary if you wish to reproduce this material separately.

GAO's Mission

The Government Accountability Office, the audit, evaluation, and investigative arm of Congress, exists to support Congress in meeting its constitutional responsibilities and to help improve the performance and accountability of the federal government for the American people. GAO examines the use of public funds; evaluates federal programs and policies; and provides analyses, recommendations, and other assistance to help Congress make informed oversight, policy, and funding decisions. GAO's commitment to good government is reflected in its core values of accountability, integrity, and reliability.

Obtaining Copies of GAO Reports and Testimony

The fastest and easiest way to obtain copies of GAO documents at no cost is through GAO's website (<https://www.gao.gov>). Each weekday afternoon, GAO posts on its website newly released reports, testimony, and correspondence. To have GAO e-mail you a list of newly posted products, go to <https://www.gao.gov> and select "E-mail Updates."

Order by Phone

The price of each GAO publication reflects GAO's actual cost of production and distribution and depends on the number of pages in the publication and whether the publication is printed in color or black and white. Pricing and ordering information is posted on GAO's website, <https://www.gao.gov/ordering.htm>.

Place orders by calling (202) 512-6000, toll free (866) 801-7077, or TDD (202) 512-2537.

Orders may be paid for using American Express, Discover Card, MasterCard, Visa, check, or money order. Call for additional information.

Connect with GAO

Connect with GAO on [Facebook](#), [Flickr](#), [Twitter](#), and [YouTube](#).
Subscribe to our [RSS Feeds](#) or [E-mail Updates](#). Listen to our [Podcasts](#).
Visit GAO on the web at <https://www.gao.gov>.

To Report Fraud, Waste, and Abuse in Federal Programs

Contact FraudNet:

Website: <https://www.gao.gov/fraudnet/fraudnet.htm>

Automated answering system: (800) 424-5454 or (202) 512-7700

Congressional Relations

Orice Williams Brown, Managing Director, WilliamsO@gao.gov, (202) 512-4400,
U.S. Government Accountability Office, 441 G Street NW, Room 7125,
Washington, DC 20548

Public Affairs

Chuck Young, Managing Director, youngc1@gao.gov, (202) 512-4800
U.S. Government Accountability Office, 441 G Street NW, Room 7149
Washington, DC 20548

Strategic Planning and External Liaison

James-Christian Blockwood, Managing Director, spel@gao.gov, (202) 512-4707
U.S. Government Accountability Office, 441 G Street NW, Room 7814,
Washington, DC 20548



Please Print on Recycled Paper.