Highlights of GAO-24-105281, a report to congressional requesters

Why GAO Did This Study

IRS attributes approximately \$80 billion in unpaid taxes to sole proprietors underreporting income each year. This comprises 16 percent of the estimated annual \$496 billion tax gap. In tax year 2019, roughly 27.8 million sole proprietors filed tax returns, which accounted for about 18 percent of all individual taxpayers.

GAO was asked to review the tax compliance of sole proprietors. This report (1) reviews options for IRS to close the tax gap by increasing sole proprietor compliance, (2) evaluates IRS efforts to assess the risk of sole proprietor noncompliance, and (3) assesses IRS efforts to conduct outreach to improve voluntary compliance among sole proprietors.

GAO reviewed literature and conducted a nongeneralizable survey of 25 experts and stakeholders on options to improve sole proprietor compliance. GAO also analyzed IRS tax gap and statistical data, reviewed agency documentation, and interviewed agency officials.

What GAO Recommends

GAO is recommending that Congress consider requiring (1) Treasury to develop a tax gap strategy that includes efforts to improve sole proprietor compliance, and (2) IRS to implement voluntary withholding when both companies and sole proprietors would like to participate. GAO is also making three recommendations to IRS related to policies and practices that could improve sole proprietor compliance. IRS agreed with one recommendation and disagreed with two. GAO maintains that all the recommendations are valid, as discussed in the report.

View GAO-24-105281. For more information, contact James R. McTigue, Jr. at (202) 512-6806 or mctiguej@gao.gov.

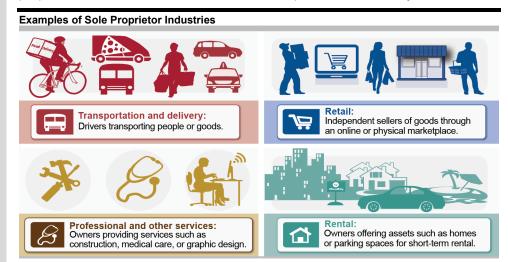
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SOLE PROPRIETOR COMPLIANCE

Treasury and IRS Have Opportunities to Reduce the Tax Gap

What GAO Found

The Department of the Treasury and the Internal Revenue Service (IRS) have not developed an overall tax gap strategy that includes specific approaches to address sole proprietor noncompliance, as GAO recommended in July 2007. Sole proprietor underreporting is one of the largest segments of the tax gap (the difference between federal income taxes owed and the amount paid). Sole proprietors are individuals who own an unincorporated business by themselves.



Sources: GAO adaptation of graphics from the JPMorgan & Co. Institute report, "The Online Platform Economy in 2018: Drivers, Workers, Sellers, and Lessons," Anna/umar/tinica10/Adrian Hillman/Flatman vector 24/Ljupco Smokovski/stock.adobe.com and from analysis of literature and stakeholder interviews. | GAO-24-105281

GAO identifies 17 options to improve sole proprietor tax compliance. The options involve tradeoffs and would best be considered as part of an overall tax gap strategy. However, Treasury officials said they have no plans to develop a strategy. Also, IRS has not taken steps to allow for voluntary withholding on payments to independent contractors, including sole proprietors, as GAO recommended in May 2020. Without voluntary withholding, these workers may find making quarterly tax payments burdensome, which may reduce compliance.

IRS's strategic operating plan outlines its priorities for the coming years, but neither this plan nor other IRS documents provide an approach specifically to improve sole proprietor compliance. While IRS has some methods to assess noncompliance risk, they are not complete or specific to sole proprietors. A risk assessment would allow IRS to make strategic decisions related to enforcement and outreach priorities to help it reduce sole proprietors' share of the tax gap.

IRS has a communications plan for platform workers, who are one type of sole proprietor. However, it does not have a coordinated communications plan focused on informing the wide variety of sole proprietors about their tax and reporting responsibilities. Such a plan would help sole proprietors meet their tax obligations and navigate tax law changes. According to stakeholders GAO spoke with, some sole proprietors are unaware of their tax obligations on income earned through online platforms. Additionally, stakeholders told GAO that they found the existing guidance overly technical and difficult to understand.

United States Government Accountability Office