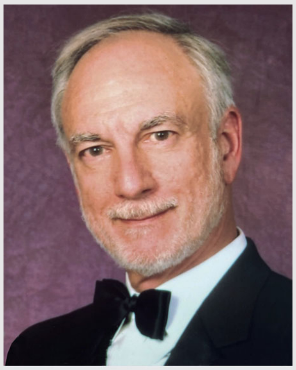
How to Evaluate the Biden Administration's Tax Compliance Plan

by Fred L. Forman, Fred T. Goldberg Jr., and Charles O. Rossotti


Fred L. Forman


Fred T. Goldberg Jr.


Charles O. Rossotti

Fred L. Forman was executive vice president and senior technology officer at American Management Systems from 1971 until 1997, when he became its general manager for Europe. In 2000 he joined the IRS as the associate commissioner for business systems modernization, serving until 2004, after which he did strategic technology consulting in the private and public sectors. Over the last several years, he has served as an officer and board member for several nonprofit organizations.
Fred T. Goldberg Jr. was appointed by President George H.W. Bush to serve as IRS commissioner from 1989 to 1991 and Treasury assistant secretary for tax policy in 1992. And he was appointed by President Reagan to serve as IRS chief counsel from 1984 to 1986. He is currently of counsel in the Washington office of Skadden, Arps, Slate, Meagher & Flom LLP. Charles O. Rossotti co-founded American Management Systems in 1970. He led the company for 27 years until he was appointed IRS commissioner in 1997 by President Clinton. He served five years as commissioner and was later appointed by President George W. Bush to a panel to recommend reform of the tax code. Since then, he has resumed his business activities.

In this article, Forman, Goldberg, and Rossotti examine the recently proposed comprehensive tax compliance plan under the Biden administration's American Families Plan and present a guide on how to evaluate the proposal.

Treasury recently proposed a comprehensive tax compliance plan under the administration's American Families Plan that would include third-party reporting on summary inflows and outflows of financial accounts and long-term funding to rebuild the IRS's technology and workforce. Treasury estimated that this proposal would produce a revenue gain of $778 billion over 10 years and an additional $1.3 trillion over the following 10 years.[1]

Some skepticism about the amount of revenue such a program would produce is understandable. And questions about how it would affect taxpayers, how it would be implemented, and how Congress could monitor its progress are reasonable and need to be answered. In due course, administration officials will undoubtedly be testifying before Congress about those issues.

The Treasury plan closely mirrors a plan that we have spent the last two years developing. Our "Shrink the Tax Gap" (STTG) plan[2] has been documented in published articles and numerous presentations, congressional testimony, and public commentary.[3] We believe this background provides a solid basis for explaining the reasoning that underlies the administration's proposal.

In this article, we present a guide on how to evaluate the administration's proposal, posing and suggesting answers to nine key questions people have about it.

[1] Treasury, "The American Families Plan Tax Compliance Agenda" (May 2021).

[2] Charles O. Rossotti, "Recover $1.6 Trillion, Modernize Tax Compliance and Assistance," *Tax Notes Federal*, Mar. 2, 2020, p. 1411; Rossotti and Fred L. Forman, "Recover $1.6 Trillion, Modernize Tax Compliance and Assistance: The How-To," *Tax Notes Federal*, Sept. 14, 2020, p. 1961; and Rossotti, Natasha Sarin, and Lawrence H. Summers, "Shrinking the Tax Gap: A Comprehensive Approach," *Tax Notes Federal*, Nov. 30, 2020, p. 1467.

[3] All of which are available at www.shrinkthetaxgap.com.

1. What's the problem, and is it real?

The tax gap is real, enormous, and getting worse by the year. The tax gap is the amount of tax that is legally owed under the tax code and is not paid each year. It is an actual cash loss to the fisc. That loss will have to be paid by others, either through higher taxes now or higher taxes later if the loss is made up by borrowing.

The tax gap has been measured carefully by the IRS in detailed published studies over the years. The most recent study, covering tax years 2011-2013, showed a gross gap of $441 billion.[4] Simply extrapolating that for the growth in the economy would have increased that gap to $574 billion in 2019. Other recent studies indicate that number may be even larger. Barry Johnson, acting chief of IRS research and analytics, testified on May 11 at a Senate Finance subcommittee public hearing that the number is likely now more than $600 billion.[5]

Although the estimates of the tax gap vary, all the estimates are enormous. By comparison, the tax gap is more than all the income taxes paid by the lower 90 percent of individual filers — about 135 million people.[6] Approximately 85 percent of that gap is attributable to the top 25 percent of taxpayers.[7]

Is that a problem worth trying to solve? Put another way, is doing nothing about it fair to people who already pay all their taxes? If the government needs revenue, would it be better to simply raise taxes on those already paying?

2. Can we really do something practical about the tax gap?

Old hands in Washington have heard about the tax gap for decades and, despite periodic studies, nothing effective has been done to reduce it. It just keeps growing as the economy grows. Some people may conclude that nothing can be done about it. In the past, there has been some reason for that sentiment of resignation because the causes of the tax gap have not been easy to address.

Most tax revenue comes in because the income of taxpayers is reported on documents like Forms W-2 for wages or 1099 for interest and dividends. When income is reported and easily checked by IRS computers, compliance is 95 to 99 percent. Even when the IRS has some but not all information, the compliance rate is 83 percent. But most of the tax gap is from more complex sources of income that are not reported and not easily checked. When the IRS has little or no third-party reporting, such as on much business income, compliance is as low as 50 percent.[8]

About 85 percent of this less visible income is earned by taxpayers in the top 25 percent of the income bracket.[9]

a. Just scaling up auditing is not a good solution, nor is it what the plan is all about.

When the IRS cannot use technology to check returns, it must use manual auditing, which is essential but inefficient for both taxpayers and the IRS. All the auditing the IRS does today recovers only 2.5 percent of the tax gap.[10] One of the reasons many old tax hands are skeptical about a program to substantially reduce the tax gap is that simply scaling up auditing will not produce the desired results.

Revenue gains from traditional auditing are low because the IRS does not use all available information to select returns for audit and to analyze data about the return before starting the audit. When the exam starts, the examiner has only slow and inefficient means to communicate with taxpayers and preparers during the exam. The result is that 20 to 40 percent of expensive exams produce nothing,[11] and even simple "correspondence exams" take more than six

[4] IRS, "Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2011-2013" (Sept. 2019).

[5] Subcommittee on Taxation and IRS Oversight, "Closing the Tax Gap: Lost Revenue From Noncompliance and the Role of Offshore Tax Evasion," May 11, 2021.

[6] Forman, "Exhibit 1: Projections of Gains From TCAM," STTG (Apr. 9, 2021).

[7] Shrinkthetaxgap.com, "Exhibit 12: Backup for Information Reporting" (Nov. 24, 2020). Exhibit 12 shows that approximately 62 percent of underreported income is from returns in the top 25 percent of adjusted gross income. Applying estimated tax rates to this income, STTG estimates that 86 percent of the underreported tax is from the top 25 percent of returns.

[8] IRS, "Federal Tax Compliance Research," *supra* note 4.

[9] "Exhibit 12," *supra* note 7.

[10] IRS, "Congressional Budget Justification and Annual Performance Report and Plan, FY 2021," at 113 (undated). Revenue of $15.71 million is 2.7 percent of the tax gap and is 0.4 percent of $3.5 trillion in collections.

[11] IRS Data Books for 2010, 2015, and 2019, "Audit No Change Rates" (Table 9a for 2010 and 2015, and Table 17b for 2019).

months to complete.[12] Starting an audit by gathering information from a taxpayer, only to find out months later that there was no problem in the first place, is not good for anyone.

But scaling up that traditional process is not what the administration's proposal is about.

b. What is different now?

What is different today is that technology can do more of the work to find likely deficiencies in returns and increase the efficiency of the follow-up process. When the IRS has applied technology to analyzing its information to find and resolve deficiencies, the results have been far greater than from traditional auditing, as shown in Table 1:

Table 1. Return on Investment (ROI) for Major IRS Enforcement Programs

Enforcement Program 2018 (dollars in millions)	Cost	Revenue	ROI
Examination[a]	$3,716	$15,017	**4.0**
Automated Underreporter (AUR)[a]	$208	$5,364	**25.8**
Return Review Program (Refund Screenings)[b]	$419	$6,510	**15.5**

[a]*Source*: IRS FY2020 Budget and Performance Plan.

[b]GAO "Tax Fraud and Noncompliance: IRS Could Further Leverage the Return Review Program to Strengthen Tax Enforcement," GAO-18-544 (July 2018), covers three-year period.

The IRS already has a lot of information that it cannot effectively use to identify deficiencies. For example, the IRS cannot efficiently evaluate information on 40 million Schedules K-1, on the Form 1099-K reports from payers, or on submissions required by the Foreign Account Tax Compliance Act.

But the IRS also lacks information on some sources of income, such as much business income earned by individuals and passthrough businesses such as partnerships. This is like a hole in a large bucket — the water will find the hole.

The solution that we and the administration proposed will leverage information and technology to increase voluntary compliance and make the enforcement process more efficient.

By adding third-party reporting that can help identify underreported income, more income will move from the low-visibility category to higher visibility. That is what the additional report proposed by the administration on financial accounts will do. Just like plugging the existing hole in the bucket, this additional information will increase voluntary compliance and help pinpoint deficiencies.

Upgrading IRS technology will also allow the agency to make full use of all its information to increase the effectiveness and efficiency of all IRS enforcement activities when deficiencies are found.

The combination of these elements builds on what works today — providing taxpayers and the IRS the same information for more accuracy in tax return preparation, and providing the IRS the technology to check returns efficiently and to resolve cases promptly and fairly.

Would any large business that was owed billions in uncollected amounts fail to upgrade its technology to find out as soon and precisely as possible which customers are not paying what they owe? Would they just let the losses continue if they could be more effective in collecting by investing in technology?

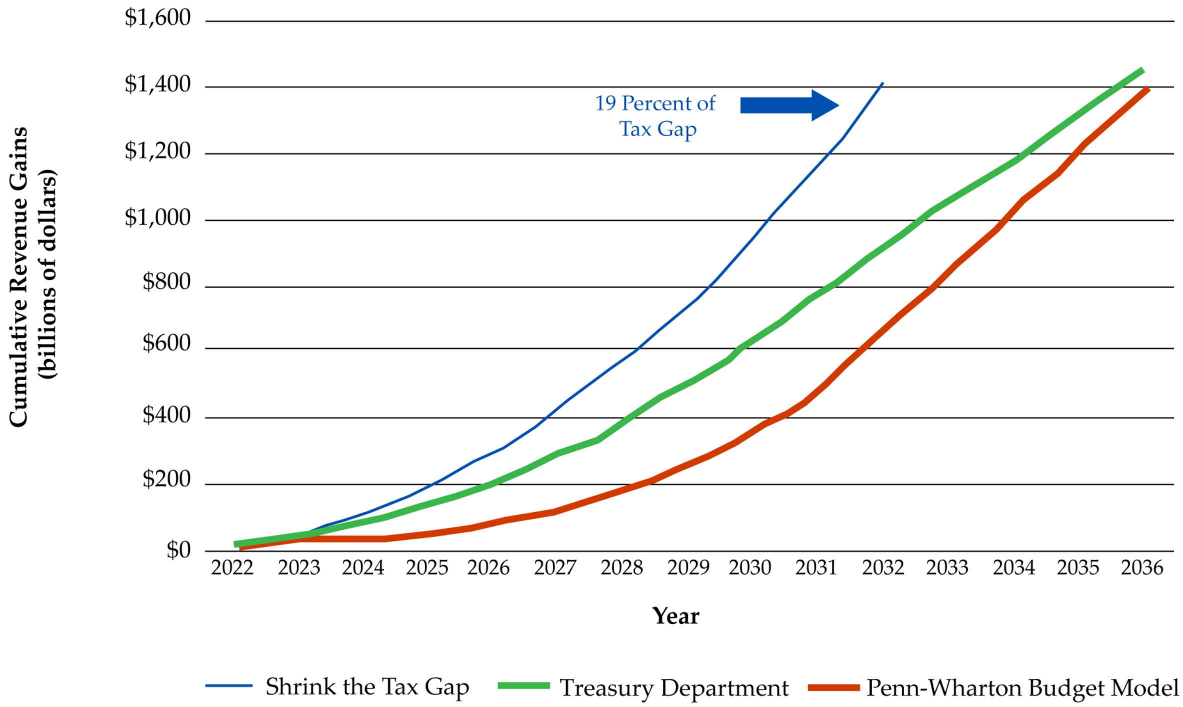
Is there any successful business that is not investing in new technology and skilled employees to change the way it deals with its customers?

3. How much revenue can this program really produce?

We understand the skepticism about revenue estimates. And there is always a range of uncertainty about any future revenue. In this case, three independent estimates have been made of the revenue that can be gained from a comprehensive program that includes enhanced

[12]Government Accountability Office, "IRS Correspondence Audits: Better Management Could Improve Tax Compliance and Reduce Taxpayer Burden," GAO-14-479, at Appendix II, "Profile of IRS Correspondence Audits" (June 2014).

Figure 1. Tax Gap Revenue Gain From Different Models



information reporting and consistent 10-year funding for technology and workforce:

- Treasury estimated a gain of $778 billion over 10 years and an additional $1.6 trillion over the next 10 years;[13]
- the Penn Wharton Budget Model (PWBM) projects a gain of $480 billion in 10 years and $1.4 trillion in 15 years;[14] and
- our STTG plan estimates a gain of $1.4 trillion over the first 11 years.[15]

All three estimates project meaningful increases in revenue, differing mainly in timing, but none assume recovery of a big fraction of the enormous tax gap. Our STTG estimate would recover only 19 percent of the tax gap over 11 years, and the Treasury estimate would recover less than 10 percent of the tax gap in 10 years.

The Congressional Budget Office is another important estimator, and it has not yet provided an estimate of the administration's plan. In 2020 the CBO conducted an analysis,[16] limited to traditional auditing, but simply scaling up traditional auditing is not what the administration proposed, and that alone would not produce a major reduction in the tax gap.

Does it seem reasonable that a serious effort over 10 years, using modern technology, could recover at least 10 percent of the taxes that are legally owed but not paid?

Each of these independent estimates used different methods, and it is understandable that timing of revenue gains would differ. But the magnitude of the gains over time are similar, as shown in Figure 1.

[13] Treasury, *supra* note 1.

[14] PWBM, "President Biden's American Families Plan: Budgetary and Macroeconomic Effects" (May 5, 2021). PWBM's tax module is a microsimulation model with detailed tax calculators for individual income taxes, payroll taxes, corporate taxes, and estate taxes. It simulates behavioral responses to tax policy changes and calculates effective tax rates used in the PWBM dynamic OLG model. It begins with representative samples of individual income tax and business tax returns, which provide more than 100 variables on income sources, deductions, credits, and other taxpayer characteristics. These returns are statistically matched with records from the current population survey and are projected forward in accordance with forecasts from PWBM's microsimulation model. This process informs how the population of tax units evolves over time, accounting for changes in demographics and incomes.

[15] Forman, "Appendix A: Shrink the Tax Gap (STTG) Plan: Calculating the Revenue Impact, Revision 4," STTG (May 24, 2021).

[16] CBO, "Trends in Internal Revenue Service's Funding and Enforcement" (July 2020).

According to Figure 1, the following is how long it would take to recover approximately $1.4 trillion using each estimate:

Table 2. Estimated Time to Recover Cumulative Total of $1.4 Trillion

Treasury tax compliance plan	14 years
PWBM	15 years
STTG plan	11 years

A closer look at the revenue estimates.

Each of these estimates used different methods to arrive at similar conclusions.

The Treasury estimate has two parts: an estimate of the increased compliance related to the increased information reporting, and a traditional ratio of revenue to cost for the increase in auditing. Although it acknowledges the importance of the investment in technology, it does not ascribe any specific revenue to that aspect of the program.

In their recent editorial supporting the administration's proposed investment in the IRS, five former secretaries of the Treasury explain the difference between our $1.4 trillion, 10-year revenue estimate and Treasury's $700 billion estimate as follows:

> This is because [the STTG's estimates] include, for example, modernizing outdated technological systems and improving taxpayer experiences with the I.R.S. — elements of the Administration's proposal whose revenue impact is not accounted for.[17]

The PWBM is a very detailed microsimulation model that uses a sample of tax returns and demographic data to estimate taxpayer response to tax change. Its model of the administration's proposal shows year-by-year gains in tax revenue. Although it is comprehensive, the model does not include an estimate of revenue gains from passthrough businesses at the business-entity level, which is a component of the other two estimates. In that respect, its estimate is inherently lower.

The STTG plan estimates the revenue gain by calculating how much would be added by moving income from the lowest-visibility category to the next-highest category over a 10-year period. Compliance rates by visibility category are well documented in IRS studies. The STTG estimate builds faster because of the use of technology, but by the 11th year, our estimate of the annual gain is almost identical to that of the PWBM.

Below in figure 2 is the traditional chart on income visibility and how it would change under our proposal[18] — although not reaching the improved level after 10 full years of investment.

One key fact about all these estimates is that the amount of revenue gained builds year by year and does not end after the first 10-year period. Rather, the gain continues to grow in both annual size and cumulative amount. This is very important for federal finances because the key financial problem for the federal government is not a short-term cash problem but rather a growing long-term debt.

Another key fact is that in all three estimates, the cumulative revenue gained exceeds the cumulative cost after only a few years and then produces gains far exceeding the costs.

If three different estimators, each using different methods, arrive at a similar conclusion, are they all wrong, or is their conclusion roughly right?

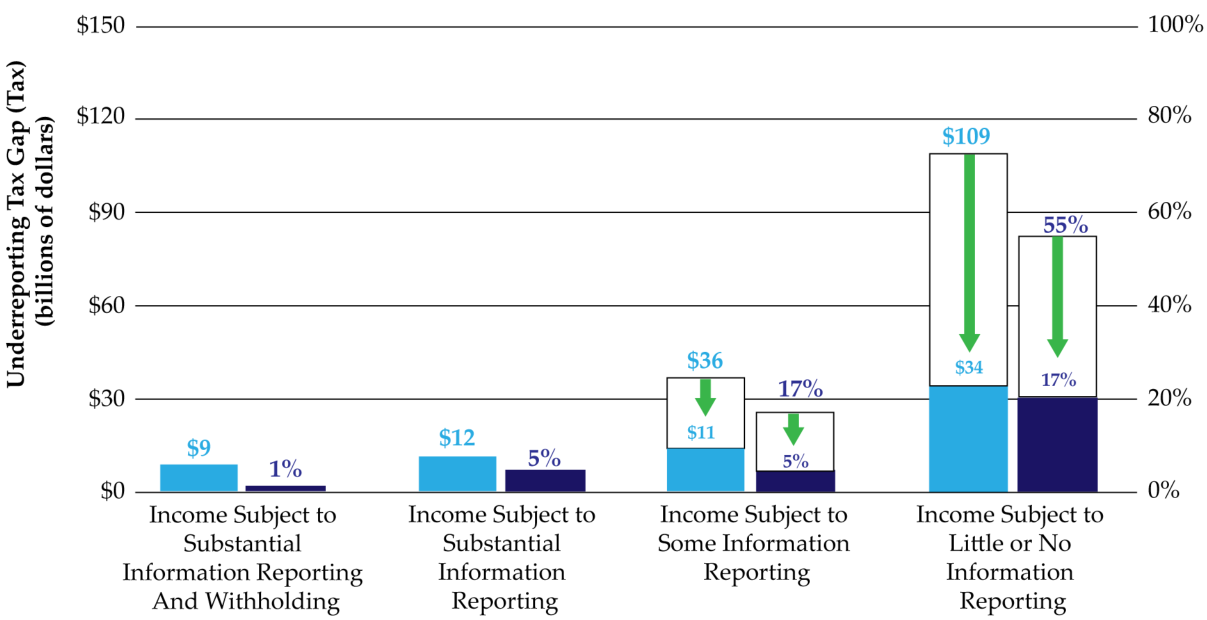
4. Is this program all about money? What about taxpayer service and taxpayer rights?

Helping taxpayers comply with the law and treating taxpayers fairly when there is a dispute are critical components of any program to achieve maximum overall tax compliance. Maximum voluntary compliance is the goal. The easier it is for taxpayers to comply, and the more confidence taxpayers have that others are also paying, the more likely it is to achieve this goal. In both our estimate and the Treasury estimate, most of the revenue gain would come from increased voluntary compliance.

[17] Timothy F. Geithner et al., "We Ran the Treasury Department. This Is How to Fix Tax Evasion," *The New York Times*, June 9, 2021.

[18] IRS, "Federal Tax Compliance," *supra* note 4.

Figure 2. Tax Year 2011-2013 Individual Income Tax Underreporting Tax Gap and Net Misreporting Percentage Estimates by 'Visibility' Category of Income Items



a. Taxpayer service.

The consistent funding for technology and staffing investment provided for in the administration's plan would improve the quality of service to taxpayers in two ways that are most important to taxpayers: prompt and efficient resolution of issues, and avoidance of unnecessary audits.

When a taxpayer receives a letter from the IRS, often stating a problem of some kind with the taxpayer's return, it is an important and sometimes stressful communication that needs to be resolved promptly and fairly.

Today, even a simple examination (called a correspondence exam) is often initiated by a letter from the IRS that is neither clear nor specific about the issue or how to resolve it. Even these simple cases typically take more than six months to resolve.[19] Moreover, lack of adequate staffing and inadequate tools for employees often make it very slow or difficult to reach an IRS employee who can resolve a case, even when the taxpayer wants to comply.

New technology will allow the IRS to make letters more specific and clearer, provide for a wider range of options for IRS employees to communicate with taxpayers, and provide IRS employees better tools to resolve cases. The increased staffing resources will provide for an adequate number of well-trained employees to resolve taxpayer issues promptly.

The technology provided for in the administration's plan will also allow the IRS to reduce the number of so-called false positive audits — namely, audits in which no deficiency is found. Those audits are unnecessary and costly to the taxpayers and the IRS, and today they can be as high as 20 percent for individuals and even higher for businesses. These false positive rates would be even higher if cases in which only immaterial amounts of deficiencies were included. Modern technology that uses all the information available to the IRS before starting an audit will enable a much more effective and accurate way to identify returns and issues on returns with the largest deficiencies.

b. Taxpayer rights.

All taxpayers are entitled to protections that are mandatory for the IRS to observe whenever the agency exercises its authority to audit a return

[19]GAO, "IRS Correspondence Audits," *supra* note 12.

or to propose a deficiency. When Congress passes legislation providing authority to the IRS, it often establishes new or clarified taxpayer rights. The following are two of the most important rights relevant to the proposed tax compliance plan:

- *Issue resolution process.* No taxpayer should ever be presented with a notice asserting a deficiency in tax without a prompt opportunity to communicate with a qualified IRS employee who has the skills, tools, and data to explain the basis for the asserted deficiency and how it can be resolved. This commitment could be further clarified by law or regulation.
- *Appeal rights*. Right of appeal of an asserted deficiency to the IRS Independent Office of Appeals (recently strengthened by the Taxpayer First Act).

Although taxpayer rights are established in law, funding is still required to ensure their observance in practice. The right of appeal, for example, is not effective if there are no qualified Appeals officers to hear the appeal in a reasonable time. The administration's funding plan will assure adequate funding to observe taxpayer rights as an integral part of the enforcement process.

Every taxpayer is required by law to file an accurate return and pay the tax due and sometimes must interact with the IRS to resolve problems. Should the IRS have the technology and the resources, as well as the obligation, to perform its part of this process efficiently and fairly, or should the current situation continue?

5. Is an additional Form 1099 information report too much of an invasion of privacy?

The administration's plan proposes additional information reporting on the annual total inflows and outflows of some financial accounts. That report will fill in a current gap in third-party reporting of business income, providing the taxpayer information to help prepare an accurate return and providing the IRS information to check returns.

Here is the way information reporting works today:

- If your grandmother has $1,000 per month in Social Security payments, the Social Security Administration reports that to the IRS.
- If you sell stock worth $10,000, your broker will send a Form 1099 to the IRS saying how much money you received and what you paid for the stock, regardless of how much or little other income you earned.
- If your daughter received $900 from selling her handmade pottery on eBay, the IRS will get a Form 1099 showing how much she received, even if that amount is less than what it cost her more to make the pottery.
- If a grocery clerk received a $500 bonus for working during the pandemic, the IRS will get a Form W-2 reporting that income.
- If a retired couple receives $2,500 from short-term rentals of their home while they are away visiting their grandchildren, the IRS will receive a Form 1099 showing their rental receipts.
- If your grandson has a bank account that earned $50 in interest, the bank will send a Form 1099 to the IRS reporting that interest.

The IRS now receives more than 3.3 billion information reports on 30 different forms.[20] The number of reports will increase significantly because new legislation reduced the reporting threshold from $20,000 to $600 on payments made to individuals by all third-party payers, not only by banks.

Largely because of information reporting, 99.5 percent of tax revenue is received by the IRS without having to do any auditing.[21]

If everyday workers have sources of their income reported to the IRS by a bank or other third party, why should some upper-income earners be exempt from reporting?

Is it an invasion of privacy if the IRS receives a Form 1099 reporting only two annual summary numbers: money in and money out of an account (no transaction details would be disclosed)?

If information is not reported to the IRS by a third party, the agency can get the same

---

[20] IRS Publication 6961, "Calendar Year Projections of Information and Withholding Documents for the United States and IRS Campuses, 2018 Update" (Aug. 2018).

[21] IRS, "Congressional Budget Justification," *supra* note 10, at 113. Revenue of $15.71 million is 2.7 percent of the tax gap and is 0.4 percent of $3.5 trillion in collections.

information by starting an audit. As a taxpayer, which would you prefer — having the IRS receive a Form 1099 report from a third party or being required to provide the same information to the IRS in an audit?

6. Is producing the additional Form 1099 too much of a burden on banks and other financial service providers?

Banks and other financial service providers already send information reports to the IRS and to millions of customers with accounts, including any account that had more than $10 of interest. The additional Form 1099 would simply add a few more numbers to this type of report. It could be fully automated, requiring a computer program report to be run once a year.

Most smaller banks rely on software vendors that already provide annual updates to meet changing requirements for compliance and other services.

Robert Spicer, a 30-year veteran bank chief information officer recently posted this comment on the STTG website:

> In order to help recover some of the taxes not paid by partnerships and sole proprietor businesses, the shrink the tax gap program recommends a new summary 1099 report of total annual deposits and withdrawals on certain financial accounts. This report is similar to other 1099 reports that banks and other financial providers already produce, such as the report on interest income, and would not pose a major technical challenge or burden for the providers.

Taxpayers who receive these reports would not have to do anything to receive them.

Some financial service providers have expressed concern that this requirement would cause the banks to make subjective judgments, such as they now are required to do with some anti-money-laundering reports. Treasury's proposal makes it clear that this new report is a mechanical summary, like other Forms 1099, and does not require any judgmental decisions by the financial service provider.

Banks have also expressed concern that only regulated banks would have to provide this new report. The Treasury proposal clarifies that "other accounts with characteristics similar to financial institution accounts will be covered under this information reporting regime." It also clarifies that "similar reporting requirements would apply to crypto asset exchanges and custodians."[22]

These requirements have already been applied to non-bank-account providers in the legislation updating the requirements for the Form 1099-K report.

Is running a computer program once a year too great a burden on banks and financial service providers if the resulting report will help taxpayers comply and help the IRS collect billions of dollars efficiently?

7. Can the IRS implement this proposal? Can it manage the technology investment and hire the skilled staff? Can it modernize the way it does business?

The administration's program calls for a major rebuilding of the IRS over a 10-year period. It would require not simply scaling up what the IRS does today but adopting new methods and making more use of modern technology to improve compliance and service. How can you assess the likelihood that this program will achieve its goals?

The only way to make that assessment is to review the long-term history of the agency in executing its main mission. Has it succeeded over time in executing this mission, despite challenges and setbacks along the way?

The IRS's most challenging assignment is its most basic one: efficiently collecting almost all the government's revenue, more than $3.5 trillion per year from more than 160 million filers, based on a complex tax code that changes every year. The IRS has also been given increasing responsibility as a payments agency — dispensing $450 billion annually in tax refunds. Fulfilling those obligations consistently and on time each year requires the IRS to have in place a set of management practices, including technology management, that are geared to executing the requirements embedded in the tax code.

That task is not static. The past two filing years have been especially challenging because the IRS

[22]Treasury, "General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals" (May 28, 2021).

has executed its responsibilities while subject to COVID-19 pandemic restrictions on its workforce and being responsible for disbursing three different economic recovery payments.

a. IRS technology.

i. Electronic filing.

It would have been impossible for the IRS to fulfill its responsibilities in the past two years without the significant improvements it has made in technology. Most importantly, the vast majority of tax returns are now filed electronically, a major transition that required years of work internally and with outside parties such as tax software providers. If most returns were still filed on paper, and if IRS workers could not have worked remotely with technology, the impact of the COVID-19 pandemic on the tax system might have been catastrophic.

ii. Return review program.

The IRS has also used new technology to increase compliance with returns at a much higher rate than traditional auditing. The IRS's current return review program was built as a new system to support a modernized process to detect and hold returns with suspect refund claims. It has been successfully expanded to incorporate new fraud analysis and identity theft models and additional information sources. This system is a modern foundation for steadily adding increasingly effective methods and technology for screening tax returns that claim refunds. According to the Government Accountability Office, the IRS has produced returns on cost of about 15 to 1.[23] In the same report, the GAO recommended that the IRS consider expanding this approach to identifying all forms of underreporting. That approach is the basis for the SSTG plan, which has been largely adopted in the administration's plan.

iii. Criminal Investigation.

In 2017 the IRS Criminal Investigation division began a major initiative, the Nationally Coordinated Investigations Unit (NCIU), to identify, select, and develop the most significant cases that will have the greatest impact on voluntary compliance. The models and algorithms identify potential criminal tax noncompliance, which subject-matter experts then analyze to determine the proper treatment stream.

These algorithms use all available IRS data, including not only tax returns but also FATCA data and other sources. The technology that the NCIU has deployed to develop early models and algorithms consist of internal IRS tools and software provided by leading vendors of analytical software. It uses these off-the-shelf tools to develop and apply the algorithms with IRS data.

In fiscal 2018 the NCIU referred 55 cases to all 25 CI field offices. Demonstrating early success, 32 of 55 field referrals were elevated to full criminal investigations. The estimated average amount of criminal tax deficiency was $2.4 million, and the total criminal tax deficiency was $68 million.

In fiscal 2019 the NCIU referred a total of 106 cases to all 21 CI field offices. The average criminal deficiency for NCIU referrals was approximately $4.6 million, which is noticeably higher than the average deficiency in traditional tax investigations (at approximately $2.9 million).

In fiscal 2020 the NCIU referred 117 cases to field offices across the country.[24]

Because criminal cases are public, it is revealing to read summaries of some of them because they show the many ways some taxpayers try to conceal or reduce their reported income.[25]

These results represent a major increase in the productivity of scarce special agent resources and

[23] GAO, "Tax Fraud and Noncompliance: IRS Could Further Leverage the Return Review Program to Strengthen Tax Enforcement," GAO-18-544 (July 2018) ("IRS reported that between January 2015 and November 2017, [the Return Review Program] prevented the issuance of more than $6.51 billion in invalid refunds. As of March 30, 2018, IRS reports spending about $419 million developing and operating RRP.").

[24] IRS CI annual reports for 2017-2020.

[25] Here are summaries of three cases that might not have ever been found except for the new technology used by CI: Justice Department, "CEO of Financial Firm Pleads Guilty to Running Multi-Million Dollar Securities and Tax Fraud Scheme, and Operating an Unlicensed Money Services Business" (Oct. 7, 2020); U.S. Attorney's Office, District of New Jersey, "Bergen County Orthopedic Surgeon Charged With Failing to Pay Over Payroll Taxes and Failing to Report a Foreign Bank Account" (Dec. 19, 2019); and Justice Department, "Alabama Salesman Sentenced to Prison for Tax Evasion" (Oct. 28, 2020).

is representative of how technology can increase the productivity of all enforcement activities.

iv. Affordable Care Act.

In 2010 the IRS was assigned responsibility under the Affordable Care Act to administer its 47 tax and insurance subsidy provisions for individuals and businesses (but not its website or enrollment process). The GAO reported that 18 of these provisions *each* affected at least $1 billion of federal revenue or spending and had to be implemented in the first three years after passage. Those provisions also affected millions of individuals and businesses, as well as other state and federal agencies. The IRS developed the new processes and supporting technology under a dedicated program, drawing on executives and subject-matter experts across the IRS, as well as new hires and contractors, at a cost of about $881 million over three fiscal years.[26]

v. GAO review of IRS technology programs.

In 2013 the GAO removed the IRS from its list of high-risk federal programs, stating:

> Internal Revenue Service Business Systems Modernization. The Internal Revenue Service (IRS) made progress in addressing significant weaknesses in information technology and financial management capabilities. IRS delivered the initial phase of its cornerstone tax processing project and began the daily processing and posting of individual taxpayer accounts in January 2012. This enhanced tax administration and improved service by enabling faster refunds for more taxpayers, allowing more timely account updates, and faster issuance of taxpayer notices. In addition, IRS has put in place close to 80 percent of the practices needed for an effective investment management process, including all of the processes needed for effective project oversight.[27]

However, the IRS's technology progress has been restrained by limited and inconsistent funding. IRS technology spending is equal to about 25 percent of that of each of the four largest U.S. banks despite the agency's having many more taxpayers to serve than the banks have customers.[28]

The consistent funding called for in the administration's proposal will provide not only the funding but the consistency needed to fully modernize IRS technology over a 10-year period, with an enormous impact on the quality of service to taxpayers and the effectiveness of IRS compliance activities.

b. IRS workforce.

The IRS's workforce has been steadily declining for a quarter century, dropping about 20 percent in just the last decade. Although the IRS has continued to execute its critical mission of collecting the nation's revenue, its level of service to taxpayers and its enforcement effectiveness have inevitably declined, allowing the tax gap to continue to grow.

Over a 10-year period, the administration's plan would require rebuilding the workforce by adding tens of thousands of new staff members while replacing those in the existing workforce who will be retiring. This plan presents a major opportunity to build the IRS of the future. But it also presents a major challenge to first define the skills and expertise needed in the future IRS and then recruit, train, and integrate substantial numbers of people with those skills.

Can the IRS successfully rebuild a workforce with the skills needed for the future?

Based on our experience, we believe the IRS can attract and retain highly qualified people to lead and staff this IRS program — provided that it is clearly authorized by Congress and established as an important national mission by the administration and that the IRS and has long-term funding.

In our terms of service at the IRS and in later periods when important missions and related

[26]GAO, "Patient Protection and Affordable Care Act: IRS Should Expand Its Strategic Approach to Implementation," GAO-11-719 (June 29, 2011).

[27]GAO, "High-Risk Series: An Update," GAO-13-283 (Feb. 14, 2013).

[28]Ron Shevlin, "How Much Do Banks Spend on Technology? (Hint: It Would Weigh 670 Tons in $100 Bills)," *Forbes*, Apr. 1, 2019. Average technology spending of the four largest banks was $9.5 billion compared with $2.6 billion for the IRS.

programs were established, the IRS was able to attract exceptional people at top levels and for specialized roles. This included people who previously were top executives in major U.S. corporations, top executives in other government agencies, as well as very talented technical architects, program managers, and accounting professionals.

The opportunity to be part of a vital national priority while participating in a serious reform of a basic governmental function and a major technology program is attractive to many people. For those nearing the end of a successful career, it is a satisfying way to use that experience to contribute to a broad public good. For people early in their careers, it is an exciting opportunity to participate in a major project, gain experience, and build credentials.

Some additional authority will be needed for the IRS to streamline hiring because talented people have multiple opportunities. Even if people are attracted to the IRS mission and program, the hiring process needs to be prompt and efficient.

c. Timing.

It will take time to plan and build up the resources needed to execute the administration's program. Investing in technology, hiring skilled people, and, most importantly, planning and testing new methods must be done carefully. And that takes time. That is why the administration's long-term funding program is so important. This funding increase averages about 6 percent per year, over and above inflationary cost increases, which is a manageable level. However, even at this level, it is important to allow for flexibility in the rate of buildup.

The most significant risk in this program is timing. Some parts of the program may not work as planned, and in those cases, it is essential to redesign the work and set a new schedule. Although planning should allow for those contingencies, the overall program may take longer than initially expected. Such situations are manageable risks, not failures.

Given the extremely high returns from the investments in this program, even significant delays will still produce high returns. Using Treasury's estimate, the 10-year return is almost 10 to 1, and the revenue continues to build after the first 10 years. Even a few years' delay in the whole program would still produce a highly attractive financial return.

The IRS has repeatedly been given challenging assignments by Congress and has carried them out — not perfectly, and not without setbacks, but ultimately achieving the key objectives.

Implementing this program will be challenging, but based on our collective decades of managing programs in business and government, we believe it is achievable and clearly outbalances its risks.

Is that a reasonable conclusion? Or would it be better to continue making very limited investments while tolerating declines in service and growth in the tax gap?

8. Can Congress provide effective oversight to this long-term program?

An essential element of the administration's plan is assured long-term funding that will permit the IRS to make investments that take time to implement. This element raises the question of how Congress can provide effective oversight. Effective oversight is essential not only to assure Congress and the public that funds are being spent appropriately but also to ensure that the program is achieving the goals and benefits Congress and the public expect.

We believe an effective oversight process can be established if clear goals for the program are set forth in legislation and if regular reporting and review processes are established. The IRS as an institution is set up by culture and internal process to implement requirements in tax legislation. In addition to its internal processes, frequent audits by the Treasury Inspector General for Tax Administration and the GAO publicly report on how well the IRS is implementing legislation.

If clear goals are set forth by Congress, the IRS will establish its internal processes to meet those goals.

An example of how this process works is the goal set in the Internal Revenue Service Restructuring and Reform Act of 1998 that mandated conversion to electronic filing of 80 percent of specified returns. When this law was passed, electronic filing was at an early stage, but today the tax system could not function without it. The program required major behavioral change by taxpayers and technological change in the IRS, and it had to overcome many obstacles over the next 20 years.

Using the successful Restructuring and Reform Act as a model, the following is an example of how goals could be set for the new program.

It is the policy of Congress that:

1. Compliance
   a. Goal. It should be the goal of the IRS that, by the 10th tax year after the effective date of this statute, the net tax gap, as measured by the fraction of taxes due that are not reported and paid, should be reduced by at least 20 percent, as compared with the fraction estimated in the most recent IRS study before enactment of this statute.
   b. Priorities. Priorities for actions and resources to improve compliance should be guided by the relative dollar amounts of noncompliance.
2. Service
   a. Goal. It should be the goal of the IRS that the quality, timeliness, and accuracy of assistance provided to taxpayers interacting with the IRS be comparable to that provided by leading private financial services institutions.
3. Reporting
   a. Within one year of enactment, the IRS will prepare a plan to achieve the compliance and assistance goals and will define milestones and metrics indicating progress on achieving the goals. Milestones and metrics must be reported at least annually indicating progress in executing the plan.
   b. Further, within three years after the effective date of this statute and every two years thereafter, the IRS shall present a comprehensive quantitative and qualitative report that evaluates progress toward these goals and report changes to the overall plan.

If goals such as these are set and regularly monitored, the IRS and Congress will be able to provide clear direction on the results the IRS is supposed to achieve. Milestones and metrics could be established to monitor results and provide feedback for necessary adjustments.[29]

Because goals are such a powerful tool to guide priorities and actions in the IRS, it is important that they reflect as reliably as possible, the outcomes that Congress seeks. In particular, substantially reducing the tax gap will require an overall increase in compliance by taxpayers, most of which will come from better information reporting, improved technology to analyze taxpayer returns, and the direct — and indirect — effect of well-targeted auditing. The goal should be to get as much compliance as possible with only as much auditing as necessary. For this reason, setting quantitative goals for specific audit levels would be counterproductive.

In addition to the specific goals and reporting mechanisms Congress might establish in connection with the new compliance program, the IRS would, of course, continue to produce numerous reports on its operations, budget expenditures, and other items required by current laws and regulations.

The IRS already has substantial oversight from the executive branch and congressional committees. To support those oversight bodies, TIGTA and the GAO provide frequent and comprehensive independent audits and investigations of all IRS activities.

TIGTA and the GAO identify problems and make specific recommendations, but they do not collaborate with management and generally cannot advise on specific personnel and resource allocation issues. The Portman-Kerry commission, which studied the IRS thoroughly in the 1990s, recommended an IRS oversight board to fulfill this part of the oversight function in a manner intended to be modeled after well-functioning boards of large businesses. Advising on resource allocation and setting of priorities is a particularly important function that a reconstituted IRS oversight board could fulfill. The legislative framework for the board remains in place, and it could be revitalized to provide a

[29] STTG staff, "Goals, Metrics, Taxpayer Rights, and Oversight" (May 4, 2021).

valuable part of the oversight of the IRS reform program.

If Congress sets clear goals and regular reporting mechanisms for the IRS, can that, together with all current reports and oversight, provide an effective means of guiding IRS actions and monitoring its execution of the program that Congress establishes?

9. Can this program be passed with bipartisan support?

An ever-increasing tax gap can be compensated for only by increased burdens on everyone who pays their tax, either by tax increases now or by increased borrowing that will put pressure on future taxes. Inadequate IRS service also increases the burden on taxpayers who are trying to comply. Addressing those problems in a practical, efficient program is a goal we should all agree on.

For this reason, five former Treasury secretaries who served under Presidents Clinton, George W. Bush, and Obama; and five former IRS commissioners who served under Presidents Reagan, George H.W. Bush, Clinton, George W. Bush, and Obama, wrote editorials supporting the administration's proposal.[30] Moreover, 29 government and business leaders from both parties have posted statements of support.[31]

Over the years, major IRS reform proposals have garnered wide bipartisan support. The Restructuring and Reform Act passed the House by 401 to 8 and the Senate by 96 to 2, despite being initially proposed by congressional Republicans during the Clinton administration. More recently, the Taxpayer First Act passed by voice vote in both houses.

Although the current administration has proposed the new tax compliance plan, most of the revenue gain will benefit later administrations.

Should a proposal that will not increase taxes on anyone who is paying their tax and will reduce the need to increase their taxes be supported by representatives of both parties? ■

[30] Geithner et al., *supra* note 16. Lawrence B. Gibbs et al., "Five Former IRS Commissioners: Biden's Proposal Would Create a Fairer Tax System," *The Washington Post*, Mar. 4, 2021.

[31] This can be found on the STTG website at shrinkthetaxgap.com.