



Highlights of [GAO-05-527T](#), a testimony to the Committee on Finance, U.S. Senate

# TAX COMPLIANCE

## Reducing the Tax Gap Can Contribute to Fiscal Sustainability but Will Require a Variety of Strategies

### Why GAO Did This Study

The Internal Revenue Service's (IRS) recent estimate of the difference between what taxpayers timely and accurately paid in taxes and what they owed ranged from \$312 billion to \$353 billion for tax year 2001. IRS estimates it will eventually recover some of this tax gap, resulting in a net tax gap from \$257 billion to \$298 billion. The tax gap arises when taxpayers fail to comply with the tax laws by underreporting tax liabilities on tax returns; underpaying taxes due from filed returns; or "nonfiling," which refers to the failure to file a required tax return altogether or in a timely manner.

The Chairman and Ranking Minority Member of the Senate Committee on Finance asked GAO to review a number of issues related to the tax gap. This testimony will address GAO's long-standing concerns regarding tax compliance; IRS's efforts to ensure compliance; and the significance of reducing the tax gap, including some steps that may assist with this challenging task. For context, this testimony will also address GAO's most recent simulations of the long-term fiscal outlook and the need for a fundamental reexamination of major spending and tax policies and priorities.

### What GAO Recommends

GAO is not making any new recommendations but discusses some past recommendations and highlights some new areas for possible attention.

[www.gao.gov/cgi-bin/getrpt?GAO-05-527T](http://www.gao.gov/cgi-bin/getrpt?GAO-05-527T).

To view the full product, including the scope and methodology, click on the link above. For more information, contact Michael Brostek on (202) 512-9110 or [brostekm@gao.gov](mailto:brostekm@gao.gov).

### What GAO Found

Our nation's fiscal policy is on an unsustainable course. As long-term budget simulations by GAO, the Congressional Budget Office, and others show, over the long term we face a large and growing structural deficit due primarily to known demographic trends and rising health care costs. All simulations indicate that the long-term fiscal challenge is too big to be solved by economic growth alone or by making modest changes to existing spending and tax policies. Rather, a fundamental reexamination of major policies and priorities will be important to recapture our fiscal flexibility. Especially relevant to this committee will be deciding whether and how to change current tax policies and how to ensure that tax compliance is as high as practically possible. Tax law enforcement is one factor affecting compliance that has caused concern in the past, due in part to declines in IRS enforcement occupations, examinations, and other enforcement results. The recent turnaround in staffing and some enforcement results is good news, but IRS's recent compliance estimate indicates that compliance levels have not improved and may be worse than it originally estimated. Thus, sustained progress in improving compliance is needed.

Reducing the tax gap would help improve fiscal sustainability, but will be challenging given persistent noncompliance. This task will not likely be achieved through a single solution. Rather, the tax gap must be attacked on multiple fronts and with multiple strategies over a sustained period of time, including reducing tax code complexity, providing quality services to taxpayers, enhancing enforcement of tax laws, and evaluating the success of IRS's efforts to promote compliance. Also important is obtaining current information on the extent of, and reasons for, noncompliance. IRS's 2001 tax gap estimate is based in part on recently collected compliance data for individual income tax underreporting. However, IRS does not have firm plans to obtain compliance data for other areas of the tax gap or again collect data on individual income tax underreporting. Finally, IRS lacks quantitative, long-term goals for improving taxpayer compliance, which would be consistent with results-oriented management.

**IRS's Tax Year 2001 Gross Tax Gap Estimates by Type of Noncompliance and Type of Tax**

Dollars in billions

Type of noncompliance	Type of tax					Total
	Individual income	Corporate income	Employment	Estate	Excise	
Underreporting	\$150-\$187	\$30	\$66-\$71	\$4	No estimate	<b>\$250-\$292</b>
Underpayment	19	2	7	2	1	<b>\$32</b>
Nonfiling	28	No estimate	No estimate	2	No estimate	<b>\$30</b>
<b>Total</b>	<b>\$198-\$234</b>	<b>\$32</b>	<b>\$73-\$78</b>	<b>\$8</b>	<b>\$1</b>	<b>\$312-\$353</b>

Source: IRS.

Note: Figures may not sum to totals due to rounding.