



# An Overview of Compliance Strategy and the Tax Gap

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# Defining the Tax Gap

- **Difference between tax that should be paid for a given year and amount actually paid voluntarily on a timely basis**
- **Annual amount of noncompliance with our tax laws in dollar terms**
- **Does not reflect taxes owed on income from illegal activities**

# Components of the Tax Gap

- **Non-filing** – tax not paid on time by taxpayers who filed late or not at all
- **Underreporting** – timely-filed returns with understated income or over-stated deductions or credits
- **Underpayment** – failure to pay on time all of the reported tax liability

# Tax Gap Data

**Tax Gap Total = \$345 billion**

- **Nonfiling = \$27 billion**
- **Underpayments = \$33 billion**
- **Underreporting = \$285 billion**

**Net Tax Gap = \$290 billion**

**after collections and late payments**

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# National Research Program reporting compliance study

- Replaced 15-year old data
- 46,000 individual returns from tax year 2001
- 3,000 returns accepted as filed
- 2,000 correspondence exams
- 41,000 face-to-face exams from Oct 2002 to Sept 2004

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# Uses of TY 2001 NRP Data

- Update Tax Gap estimates
- Recognize the general level of noncompliance
- Improve audit selection criteria
- Understand taxpayer behavior

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# Second NRP S-Corporation reporting compliance study

- Reflects increase in S-Corporation filing
- 5,000 Form 1120S returns for TY 03 and TY 04
- Over 800 examinations complete
- Updates individual tax gap figures and identifies additional compliance issues



# Compliance Priorities for Increased Enforcement Results

- Promoters and participants in abusive tax avoidance transactions
- High income – high risk taxpayers
- High income non-filers
- Unreported income
- Employment tax noncompliance

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# Tax Professionals and the Tax Gap

## April 2006 GAO report

- Significant errors and omissions on returns prepared by paid preparers
- 10 out of 19 excluded side income

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# FY08 IRS Tax Gap Priorities

- **Enhancing information reporting and matching**
- **Revamping audit selection formulas**
- **Increasing enforcement actions for noncompliance**
- **Working with Treasury on legislative proposals**
- **Educating small business and self-employed taxpayers on their tax obligations**

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# Future IRS Compliance Studies

- Update Tax Gap estimates
- Learn about compliance behavior for new groups of taxpayers
- Research more than one tax year
- IRS partners with external stakeholders

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## Outreach & Education Products

- **Virtual Small Business Tax Workshop DVD – 10-lesson interactive video**
- **Small Business Resource Guide CD-ROM**
- **Tax Calendar for Small Businesses and Self-Employed**
- **Tax Talk Today – Monthly Web cast for tax professionals**
- ***E-News for Tax Professionals* and *E-News for Small Businesses* – Weekly electronic newsletters**