TREASURY INSPECTOR GENERAL FOR TAX ADMINISTRATION

Additional Actions Are Needed to Effectively Address the Tax Gap

April 23, 2008

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Phone Number | 202-622-6500
Email Address | inquiries@tigta.treas.gov
Web Site | http://www.tigta.gov

TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY

WASHINGTON, D.C. 20220

April 23, 2008

MEMORANDUM FOR DEPUTY COMMISSIONER FOR OPERATIONS SUPPORT
DEPUTY COMMISSIONER FOR SERVICES AND ENFORCEMENT

FROM: Michael R. Phillips
Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Additional Actions Are Needed to Effectively Address the Tax Gap (Audit # 200730IE029)

This report presents the results of our review of the tax gap reduction efforts that are underway. The overall objective of this review was to determine the progress of the plans and actions taken by the Internal Revenue Service (IRS) to reduce the tax gap. The audit was initiated by the Treasury Inspector General for Tax Administration during Fiscal Year 2007 because of ongoing Congressional interest in the area.

Impact on the Taxpayer

The tax gap, estimated at $345 billion for Tax Year 2001, is the difference between taxes that are legally owed and taxes that are paid on time. The Department of the Treasury and the IRS developed a multiyear strategy for improving compliance and reducing the tax gap. However, the strategy is dependent on overcoming several high-risk challenges. While the United States has one of the highest tax compliance rates in the world at 83.7 percent, each percentage point of noncompliance costs the Federal Government approximately $21 billion in lost revenue. Taxpayers who do not voluntarily pay their share of taxes create unfair burden on honest taxpayers and diminish the public's respect for the tax system.

Synopsis

In August 2007, the Department of the Treasury and the IRS issued a report entitled *Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance*. The report details the steps currently being taken by the IRS, as well as those under development, to address key elements of the tax gap. After reviewing the report, the Chairman, Senate Finance Committee, stated that he was "very encouraged . . . and believe[d] that it is an important step toward fairer and more efficient tax administration."

The current IRS strategy is significantly more comprehensive and detailed than the previous efforts. The strategy identifies seven components that support a multifaceted approach to reducing the tax gap. Each component identifies ongoing and planned actions for the component. However, the strategy is largely predicated on receiving funding for additional compliance resources and enactment of legislative changes. Long-term success will in large part be dependent on addressing several risk factors, some of which are beyond the control of the IRS. For example, there are proposals for additional information reporting that are dependent on legislative action. Also, additional compliance staffing and resources for research require budget increases. When these factors are combined with the IRS' managing of high-risk areas like Business Systems Modernization, additional progress in IRS capabilities and capacities must be realized.

Examples of the challenges are the proposed legislation changes that are critical to the Reduce Opportunities for Evasion component of the tax gap strategy. Although the legislative changes[1] proposed in the Fiscal Year 2008 budget were a step in the right direction, the $29.5 billion in revenue expected to be generated over 10 years would have a minimal impact (less than 1 percent) on the estimated Tax Year 2001 gross tax gap of $345 billion. In addition, approximately 97 percent ($28.8 billion of $29.5 billion) of the additional revenue generated by the legislative proposals would be derived from increased information reporting requirements. Therefore, any reductions in evasion seem very dependent on new information reporting requirements. While expanding information reporting is a proven method to increase taxpayer compliance, there is resistance to the proposals.

In the Make a Multiyear Commitment to Research component, the Fiscal Year 2009 budget request included approximately $51 million to improve tax gap estimates, measurements, and detection of noncompliance.[2] Through research studies funded by this initiative, the IRS plans to analyze new taxpayer segments and update existing estimates of noncompliance. However, there are other budget requirements to conduct research. The estimated cost of the National Research Program (NRP) of Tax Year 2001 individual taxpayers was approximately $150 million.[3] The NRP study of Subchapter S corporations began in October 2005, and preliminary internal data were available in January 2008. Some tax segments could require sample sizes larger than the annual number of returns examined in the operational examination program, which would put

[1] Our review focused primarily on the legislative proposals in the IRS' Fiscal Year 2008 budget request. Only 3 of the 16 Fiscal Year 2008 legislative proposals were passed. With the exception of 1 proposal (Expand broker information reporting), the remaining 12 proposals are included in the IRS' Fiscal Year 2009 budget request.

[2] The Fiscal Year 2008 budget request included $41 million for research, which the IRS did not receive.

[3] A significant portion of the $150 million was for examination resources in the form of examiner labor hours. Those examiners would have worked other cases if they did not work NRP cases.

considerable strain on operational resources. The IRS is addressing this issue by moving to multiyear studies such as the Tax Year 2006 NRP of individual taxpayers, which is the first in a series of ongoing annual individual taxpayer studies. Consistent funding above operational levels is required to assure that this component of the tax gap strategy will be successful.

Finally, a major risk to long-term success is the Business Systems Modernization program. While the IRS is making progress in addressing concerns with the management of this highly complex, multibillion-dollar effort, it remains a top management challenge. This is not surprising given the considerable investment that has been made in the program, the shortcomings the IRS has experienced in meeting cost and completion commitments, and the critical role it has in supporting IRS tax gap reduction strategies.

Recommendation

We made no recommendations in this report. However, we discussed the issues contained in the report with appropriate IRS management officials and have incorporated their viewpoints where appropriate.

Copies of this report are also being sent to the IRS managers affected by the report issues. Please contact me at (202) 622-6510 if you have questions or Margaret E. Begg, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs), at (202) 622-8510.

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Abbreviations

AICPA	American Institute of Certified Public Accountants
BSM	Business Systems Modernization
IRS	Internal Revenue Service
NRP	National Research Program
TCMP	Taxpayer Compliance Measurement Program

Background

The Internal Revenue Service (IRS) has performed detailed studies of taxpayer compliance for more than four decades. Beginning in 1963, the IRS conducted periodic studies of compliance under the Taxpayer Compliance Measurement Program (TCMP). The studies consisted of examinations that required a detailed, line-by-line verification of all items on a taxpayer's return. The TCMP studies were discontinued because stakeholders considered them costly, intrusive, and burdensome. The last TCMP study was of 1988 individual income tax returns that were filed in 1989.

The National Research Program (NRP) replaced the TCMP. It is a comprehensive effort to measure voluntary compliance and to develop updated return selection formulas for the different tax return types. The mission of the NRP Office is to design and implement systems and studies that will produce timely, reliable information about filing, reporting, and payment compliance.

The initial NRP reporting compliance study addressed individual taxpayer compliance by examining approximately 46,000 randomly selected individual income tax returns for Tax Year 2001. The resulting data were used to estimate the individual income tax reporting subcomponent of the tax gap and to improve workload selection (audit selection) formulas. Additional studies to update individual and other subcomponents of the tax gap are planned.

The tax gap is the difference between taxes that are legally owed and taxes that are paid on time. In February 2006, the IRS released the estimate that the gross tax gap was $345 billion for Tax Year 2001. The voluntary compliance rate (the percentage of taxes that are paid voluntarily and on time) is 83.7 percent, which gives the United States one of the highest tax compliance rates in the world. However, each percentage point of noncompliance costs the Federal Government approximately $21 billion in lost revenue. Figure 1 defines the three components of the tax gap and shows the amount of noncompliance for each component.

Figure 1: Components of the Tax Gap for Tax Year 2001

Component	Definition	Amount (in $ billions)	Percentage of Total
Nonfiling	Tax not paid on time by taxpayers who filed late or not at all	**$27**	7.8
Underreporting	Misstatement of tax by taxpayers on returns that are filed on time	**$285**	82.6
Underpayment	Failure by taxpayers to pay all of the reported tax liability on time	**$33**	9.6
Totals		**$345**	**100.0**

Source: Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance, August 2, 2007 (issued by the Department of the Treasury and the IRS).

Different information sources are used to estimate the tax gap for various types of taxes within the three components. For example, United States Census data were used to estimate the nonfiling tax gap for individual income and estate taxes. Estimates for the underreporting tax gap were based on random samples of tax returns that were subjected to a thorough tax examination. The underpayment tax gap estimates were derived from IRS accounting data and include individual income, corporate income, employment, estate, and excise taxes. Appendix V presents the IRS' detailed Tax Year 2001 "Tax Gap Map" for the three components and the various types of taxes.

This review was performed at the Treasury Inspector General for Tax Administration Office of Audit in Philadelphia, Pennsylvania, during the period January through November 2007. We used information from various IRS systems during our review. Due to time and resource constraints, we did not audit IRS systems to validate the accuracy and reliability of their information. Also, we did not assess internal controls because to do so would not have been applicable within the context of our audit objective. Otherwise, we conducted this performance audit 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 objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.

Results of Review

Progress Has Been Made in Identifying a Strategy to Reduce the Tax Gap

In August 2007, the Department of the Treasury and the IRS issued a report entitled *Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance.* The report details the steps currently being taken by the IRS, as well as those under development, to address key elements of the tax gap. The report recognizes that no single approach will be successful at substantially reducing noncompliance. The strategy is presented as a comprehensive, integrated, multiyear approach that must be implemented within the context of the annual budget process. The report builds on *A Comprehensive Strategy for Reducing the Tax Gap*, which the Department of the Treasury released in September 2006.

Senator Max Baucus, Chairman, Senate Finance Committee, expressed his less than full satisfaction with the September 2006 report, *A Comprehensive Strategy for Reducing the Tax Gap*, by stating that the Department of the Treasury did "not have a comprehensive credible plan for the tax gap." However, after reviewing the August 2007 report, the Chairman stated that he was "very encouraged . . . and believe[d] that it is an important step toward fairer and more efficient tax administration." The tax gap strategy consists of seven components:

- Reduce Opportunities for Evasion.
- Make a Multiyear Commitment to Research.
- Continue Improvements in Information Technology.
- Improve Compliance Activities.
- Enhance Taxpayer Service.
- Reform and Simplify the Tax Law.
- Coordinate With Partners and Stakeholders.

Reduce Opportunities for Evasion

The Reduce Opportunities for Evasion component contains two approaches. The first involves 16 legislative proposals submitted with the IRS' Fiscal Year 2008 budget request.[1] The

[1] Our review focused primarily on the IRS' Fiscal Year 2008 budget request including legislative proposals. Only 3 of the 16 Fiscal Year 2008 legislative proposals were passed. With the exception of 1 proposal (Expand broker information reporting), the remaining 12 proposals are included in the IRS' Fiscal Year 2009 budget request.

legislative proposals addressed expanding information reporting, improving compliance by businesses, strengthening tax administration and strengthening penalties. Altogether, the legislative changes were projected to generate about $29.5 billion in additional revenue over a 10-year period.

The other approach to reduce opportunities for evasions is to use published guidance that includes regulations, revenue rulings, revenue procedures, notices, and announcements. Published guidance is seen as a critical method to reduce tax avoidance, increase taxpayer compliance, and clarify ambiguous areas of the law. No estimates are provided on the projected revenue effect of providing the published guidance.

The 16 legislative proposals fall into 4 categories: expand information reporting, improve compliance by businesses, strengthen tax administration, and expand penalties. Appendix VI lists the 16 legislative proposals by category and provides an estimate of the revenue for each proposal.

Seven of the legislative proposals concern the expansion of information reporting requirements and are expected to generate an estimated $28.8 billion in revenue over 10 years. The IRS estimates that more than 80 percent ($285 billion) of the gross tax gap is caused by the underreporting of tax, which occurs when a taxpayer understates income, overstates deductions, and/or overstates credits. Numerous IRS studies indicate that tax compliance increases significantly when there is third-party information reporting. The NRP study shows that underreporting for individuals is 1.2 percent when there is withholding and information reporting. In contrast, underreporting is 53.9 percent when there is no information reporting.

Figure 2 shows the sources of the Underreporting component of the tax gap.

Figure 2: Underreporting Component of the Tax Gap for Tax Year 2001

Source (type of tax)	Amount (in $ billions)	Percentage of Total*
Individual Income	**197**	**69.1**
Non-Business Income	56	19.6
Business Income	109	38.2
Adjustments, Deductions, and Exemptions	15	5.3
Credits	17	6.0
Corporation Income	**30**	**10.5**
Small Corporations (Assets of less than $10 million)	5	1.8
Large Corporations (Assets of $10 million and greater)	25	8.8
Employment	**54**	**18.9**
Social Security and Medicare	14	4.9
Self-Employment	39	13.7
Unemployment	1	.4
Estate	**4**	**1.4**
Totals	**285**	**100.0**

Source: Reducing the Federal Tax Gap: A Report on Improving Voluntary Compliance, August 2, 2007 (issued by the Department of the Treasury and the IRS).
** Amounts might not add to total due to rounding.*

Individuals account for more than 80 percent ($236 billion) of the overall underreporting gap of $285 billion. This includes both the underreporting of individual income tax ($197 billion) and the underreporting of self-employment taxes ($39 billion). Of this amount, $148 billion (or approximately one-half of the $285 billion underreporting gap) arises from the underreporting of business income by individuals ($109 billion of individual income tax and $39 billion of self-employment taxes). The IRS Commissioner has stated "that we [the IRS] will never be able to audit our way out of the tax gap." Information reporting is seen as a proven method to improve voluntary tax compliance.

Another category of legislative proposals is to improve compliance by businesses. Three proposals in this category are estimated to generate revenue of $421 million over 10 years. Three legislative proposals designed to improve administration of the tax laws comprise the third category and were estimated to generate $17 million over 10 years. The fourth and final category of legislative proposals, expand penalties, was expected to generate $178 million over 10 years.

Make a Multiyear Commitment to Research

IRS experience shows that research is very important in identifying and combating specific areas of noncompliance. For example, the Tax Year 2001 NRP data updated tax return selection formulas and should help the IRS better pursue noncompliant taxpayers. The new formulas, the first update since 1992, were used to select Tax Years 2005 and 2006 individual income tax returns for examination. These efforts should help to focus compliance resources on more productive examinations, resulting in increased dollar yield per case and fewer no-change audits.

To make the multiyear commitment to research, the Fiscal Year 2009 budget request includes approximately $51 million to improve tax gap estimates, measurements, and detection of noncompliance.[2] Through research studies funded by this initiative, the IRS plans to analyze new taxpayer segments and update existing estimates of noncompliance. Most of this funding will cover the cost of examination resources. The IRS estimates that this initiative will produce almost $16 million in additional annual enforcement revenue once the employees hired to carry out the initiative reach their full potential in Fiscal Year 2010. This initiative includes the following:

- Increasing compliance studies to update information on corporation income tax, employment tax, and partnership compliance and obtain information on excise tax compliance.
- Updating existing data for individual income tax return filers.

Additionally, the IRS received $5 million in the Fiscal Year 2008 budget to research the effect of service on taxpayer compliance.

Continuous research is required because the tax gap estimate and return selection model data become dated. The IRS has plans for completing and initiating several new studies. First, a new NRP individual taxpayer study was begun in October 2007. The study will include approximately 13,000 randomly selected Tax Year 2006 individual income tax returns and will be the first in a series of ongoing annual individual taxpayer studies. The goal is to make annual updates to the tax gap estimate after the first three annual studies. A separate sample of international tax returns is included in this study.

Second, the Subchapter S Corporation NRP study is in process. The study began in October 2005, and preliminary internal data were available in January 2008. This study is especially important because of the significant increase in the filing of Subchapter S corporation returns from approximately 722,000 in 1985 to more than 3.6 million in 2004. The last time the IRS evaluated compliance rates for Subchapter S corporations was in 1984.

[2] The Fiscal Year 2008 budget request included $41 million for research, which the IRS did not receive.

Finally, the NRP Office is in discussions with the Large and Mid-Size Business, Small Business/Self-Employed, and Tax Exempt and Government Entities Divisions staff regarding studies of employment taxes.

Continue Improvements in Information Technology

The IRS strategy states that information technology modernization is critical to ensuring the most productive use of taxpayer service and compliance resources. The Fiscal Year 2008 budget provides resources for the planning and capital assets acquisition of information technology necessary to modernize IRS business systems. Specifically, funding is provided to improve the information technology infrastructure and to continue development and deployment of the IRS Business Systems Modernization (BSM) program.

Progress in this area is vital to improving enforcement and services capabilities. The Fiscal Year 2008 budget included funding for the IRS to upgrade its critical information technology infrastructure, enhance the Computer Security Incident Response Center,[3] and enhance network infrastructure security.

The IRS has a backlog of equipment that has exceeded its life cycle. Failure to replace the information technology infrastructure will increase the risk of disrupting business operations.

Enhancements to the Computer Security Incident Response Center and network infrastructure security should allow the IRS to keep pace with the ever-changing security threat environment through enhanced detection and analysis, improved forensics, and the ability to identify and respond to potential intrusions before they occur. Funding should help address threats by providing the IRS with resources to employ additional security safeguards and use up-to-date technologies. Enhancement of the network infrastructure security should provide the IRS with the ability to continuously monitor the security of operational systems.

Funding for the BSM program should allow the IRS to continue development of modernization projects, such as the Customer Account Data Engine, Account Management Services, and Modernized e-File projects. The development of the Customer Account Data Engine and Account Management Services systems should enable the IRS to process tax returns and address taxpayer issues in a near real-time manner. The Modernized e-File project is the future of electronic filing. It should enable the IRS to better analyze tax compliance issues and address noncompliance among taxpayers by reengineering much of the IRS' current manual and time-consuming compliance processes.

Many of the initiatives to improve information technology and to continue BSM efforts have a direct impact on efforts to improve compliance. Some examples of the initiatives that support both the Continue Improvements in Information Technology and the Improve Compliance Activities components of the tax gap strategy are:

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[3] See Appendix IV for a glossary of terms used in this report.

- Improve high-income examination workload selection and method of delivery.
- Expand Automated Underreporter Auto Notice Generation to include additional income types and all individual income tax returns.
- Evaluate the Automated Underreporter matching process and implement an improved case scoring and selection concept to select the most productive cases.
- Develop enhancements to the Compliance Data Warehouse to improve workload identification and prioritization formulas.
- Automate lien delivery, recording, and release processes with State and local jurisdictions to improve the timeliness of lien filings and the payment of fees.
- Develop and implement a set of compliance decision analytical tools to support analysis of Tax Exempt and Government Entities Division returns and other data to detect compliance trends and improve case and issue selection.

Additionally, plans to continually improve information technology also affect the Enhance Taxpayer Service component of the tax gap strategy.

Improve Compliance Activities

The Improve Compliance Activities component strategy addresses the tax gap by balancing three enforcement elements: coverage, yield, and intentional noncompliant behavior. Balanced coverage is important from a presence and noncompliance deterrence perspective. Yield addresses applying compliance resources to noncompliance areas that provide the greatest revenue. Finally, intentional noncompliant behavior involves larger components of the tax gap, more complex issues, and/or unreported income requiring more in-depth audits or criminal investigations.

As of August 2007, the Deputy Commissioner for Services and Enforcement had formed an executive-level tax gap committee that analyzes compliance data and makes recommendations for allocating compliance resources. The goal is to maximize the use of resources to better address coverage, yield, and noncompliant behavior.

The IRS did not receive funding for FY 2008 for six initiatives that were aimed at improving compliance activities. However, the FY 2009 budget request includes the following four enforcement initiatives, including funding for an additional 2,664 employees:

- Reduce the tax gap for small business and self-employed taxpayers.
- Reduce the tax gap for large businesses.
- Increase reporting compliance of United States taxpayers with offshore activities.
- Expand document matching.

The IRS estimates that when the newly hired employees reach full potential in Fiscal Year 2011, the initiatives should generate approximately $1.99 billion in additional enforcement revenue per year.

The IRS has several other initiatives designed to improve compliance activities. Examples include plans to enhance the ability to identify and address tax schemes of businesses and individuals involving offshore activity, address illegitimate use of tax havens to shelter income, increase information matching and examination activity for individuals living abroad, enhance collection programs, and improve compliance by tax preparers by implementing the Service-Wide Preparers Strategy.

The IRS has already made strides to enhance enforcement of the tax law. According to IRS statistics, approximately $59.2 billion of the tax gap in Fiscal Year 2007 was recovered through enforcement efforts. This represents an increase of 21.6 percent from the prior year. The IRS has also reported that audit rates of individuals, Subchapter S corporations, and partnerships increased from Fiscal Year 2006 to Fiscal Year 2007. These positive trends reflect the IRS' commitment to enforce the tax law and reduce the tax gap.

Enhance Taxpayer Service

The Department of the Treasury and the IRS recognize that effective taxpayer service has a significant impact on voluntary tax compliance. Assisting taxpayers in preparing their returns by answering tax questions reduces the burden of notices and correspondence that taxpayers might have received if they made errors on their returns. Taxpayer service also reduces overall unintentional noncompliance and the need for compliance activity in the future.

The IRS needs to conduct research to determine the impact that taxpayer service activities have on taxpayer compliance. The Fiscal Year 2008 budget included funding of $5 million for this important research. The study plans to evaluate the relationship between service and taxpayer compliance and to examine the needs, preferences, and behaviors of taxpayers. The study will strive for a better understanding of why taxpayers make errors and will assist the IRS in developing strategies to change noncompliant behavior. It will focus on four areas:

- Meeting taxpayer needs by providing the right channels of communication.
- Better understanding of taxpayer burden.
- Understanding taxpayer needs through the errors they make.
- Researching the impact of service on overall levels of voluntary compliance.

Taxpayer service is important in helping taxpayers avoid unintentional errors by providing them with year-round customer service. Taxpayer service has become more necessary because of the increasing complexity of the tax code. By assisting taxpayers who want to be compliant, the IRS can focus on taxpayers who intentionally evade their tax obligations.

The IRS presented a Taxpayer Assistance Blueprint to Congress in response to a Congressional mandate for the development of a 5-year plan for the delivery of taxpayer service. The Blueprint was prepared by the IRS, the IRS Oversight Board, and the National Taxpayer Advocate. It addresses the service delivery plans for individual taxpayers and is integrated with the Department of the Treasury tax gap strategy. The Blueprint includes a multiyear research portfolio, consisting of a set of research projects that includes studies to better understand the impact of service on compliance.

Reform and Simplify the Tax Law

Most taxpayers agree that the Internal Revenue Code is too complicated--which can lead to unintentional errors because taxpayers find it difficult to understand complicated rules and forms--and, therefore, make honest mistakes when completing their tax returns. Complexity also provides opportunities for noncompliance. Simplification would reduce unintentional errors caused by a lack of understanding, reduce opportunities for intentional evasion, and make tax law administration more efficient.

In testimony before the Committee on the Budget, House of Representatives,[4] the Government Accountability Office stated that, "Simplifying the tax code or fundamental tax reform has the potential to reduce the tax gap by billions of dollars." The IRS estimates that approximately $32 billion of the tax gap is due to errors in claiming tax credits and deductions. Therefore, reducing the numbers of credits and deductions would potentially have some direct effect on reducing the tax gap. The Government Accountability Office acknowledges that the elimination of such credits and deductions would be difficult, however, because they serve purposes that Congress considers important.

The Fiscal Year 2008 budget included specific, but very limited, proposals that would assist with simplification, reduce errors, and improve taxpayers' understanding of available tax benefits. The following proposals should help compliant taxpayers avoid inadvertent errors, though they do not address intentional noncompliance:

- Clarify the uniform definition of a child.
- Simplify Earned Income Tax Credit eligibility requirements.
- Reduce the computational complexity of the refundable Child Tax Credit.

The IRS continues its internal efforts to reduce taxpayer burden by simplifying forms and procedures. For example, in 2002, the IRS established the Office of Taxpayer Burden Reduction. Taxpayer burden is defined as the time and money taxpayers spend to comply with their Federal tax obligations, such as the average time and expense required to complete and file

[4] *Tax Compliance: Multiple Approaches Are Needed to Reduce the Tax Gap* (GAO-07-488T, dated February 16, 2007).

a form. The IRS has recently made improvements in forms, processes, and procedures such as simplifying filing requirements for the Employer's ANNUAL Federal Tax Return (Form 944). The Office of Taxpayer Burden Reduction is reviewing additional projects through which to simplify tax forms and processes.

Other efforts to help simplify the administration of the tax law include continuing efforts to improve forms and publications, using IRS.gov to disseminate tax product information and changes, and conducting focus groups to obtain taxpayer information.

Coordinate With Partners and Stakeholders

The Department of the Treasury tax gap strategy suggests that closer coordination is needed among IRS and State and foreign Governments to share information and compliance strategies. Closer coordination is also needed with practitioner organizations to maintain and improve methods to ensure that tax advisors provide taxpayers with appropriate tax advice.

The IRS has made significant steps in coordinating with partners and stakeholders. IRS officials solicited from tax executives of global accounting firms in the United States their views on ways in which voluntary compliance could be improved and the tax gap reduced, while maintaining taxpayer services and minimizing taxpayer burden. The resulting *Tax Gap Whitepaper*[5] offered valuable comments and observations about the Department of the Treasury strategy.

In an example of outreach, the IRS is partnering with local, State, and Federal agencies across the country. Examples of some current initiatives include:

- The Questionable Employment Tax Practices initiative to develop a Federal and State interagency approach to combat employment tax schemes and increase voluntary compliance.
- The State Reverse File Match initiative, a pilot project that is assessing the potential use of State-provided data to identify underreported income and nonfiled returns.
- The Tax Education initiative to enter into agreements with State education departments and Federal immigration agencies to promote materials to educate younger citizens and foreign taxpayers about United States tax responsibilities.

The IRS also has an extensive outreach and education program through relationships with national and local payroll, practitioner, small business, and industry stakeholder organizations. Examples of accomplishments include developing relationships with more than 1,500 small business industry and tax professional organizations to deliver key tax-related messages, implementing Small Business Forums with industry representatives and small business owners, developing and widely distributing educational information on areas of high noncompliance, and establishing a system to track the resolution of problems identified by stakeholders.

[5] Published May 24, 2007.

The following initiatives are examples of further coordination with partners and stakeholders:

- Develop a strategy to reach practitioners who have no affiliation with a professional organization.
- Develop an educational, targeted outreach DVD for military personnel preparing for retirement.
- Develop strategies to educate first-time business filers.
- Deliver educational messages through existing relationships with universities and colleges.
- Request feedback from internal and external stakeholders on existing outreach and educational programs to identify best practices and enhancements.

Significant Challenges Exist in Implementing the Tax Gap Strategy

The IRS and the Department of the Treasury strategic plan to reduce the tax gap is largely predicated on receiving funding for additional compliance resources and enactment of legislative changes. Furthermore, sizeable efficiency gains in taxpayer service and compliance resources are dependent on the successful implementation of information technology enhancements and the IRS' ability to manage other risks. Beyond these challenges, the IRS will have a major workforce transition in the near future because 41 percent of revenue agents are eligible to retire by the end of Calendar Year 2008. In combination, the IRS faces significant challenges as it attempts to reduce the tax gap and improve voluntary compliance.

While we are encouraged by the development of a detailed strategy to reduce the tax gap, long-term success will in large part be dependent on addressing several risk factors, some of which are beyond the control of the IRS. For example, there are proposals for additional information reporting that are dependent on legislative action. Also, additional compliance staffing and resources for research require budget increases. When these factors are combined with the IRS' managing of high-risk areas like BSM, additional progress in IRS capabilities and capacities must be realized.

Legislative proposals will have a minimal impact on the tax gap and face resistance

Legislation changes are critical to improving compliance and reducing the tax gap. Although the changes proposed in the Fiscal Year 2008 budget were a step in the right direction, the $29.5 billion in revenue expected to be generated over 10 years would have a minimal impact (0.85 percent) on the estimated Tax Year 2001 gross tax gap of $345 billion. In addition, approximately 97 percent ($28.8 billion of $29.5 billion) of the additional revenue generated by the legislative proposals would be derived from increased information reporting requirements.

Therefore, any reductions in evasion seem very dependent on new information reporting requirements.

While expanding information reporting is a proven method to increase taxpayer compliance, there is resistance to the proposals. Representatives from the National Association for the Self-Employed and the National Small Business Association testified and expressed concerns that the legislative proposals place unreasonable burden on taxpayers.[6] Furthermore, in a recently issued document,[7] tax professionals from six major accounting firms agree that "properly used, information reporting is a useful tool to follow up with taxpayers on underreported income and identify high-noncompliance issues. . . . However, new information reporting, especially coupled with withholding, likely would pose new burdens and challenges to taxpayers and third-party reporters of information." Thus, legitimate concerns about increased taxpayer burden, when compared to the benefits, could make it very difficult for all 16 legislative proposals to become law.

We believe that the IRS needs to continue to pursue common areas of tax abuse. For example, we recently identified significant concerns about taxpayers with substantial wage and pension sources of income taking Profit or Loss From Business (Schedule C) losses for 4 consecutive years.[8] The current tax law makes it difficult for the IRS to effectively and efficiently address potential abuses without conducting a full examination of an individual's books and records. We identified 1.2 million taxpayers who potentially avoided paying $2.8 billion in taxes in Tax Year 2005 by claiming Schedule C losses. Similarly, there are potential abuses of employment tax laws caused by misclassified workers and single shareholder owners of Subchapter S corporations. In addition, a prior Treasury Inspector General for Tax Administration audit found that a significant number of single shareholder owners of Subchapter S corporations did not pay themselves salaries to avoid paying employment taxes.[9] We estimated that this would cost the Department of the Treasury approximately $60 billion in employment taxes over 5 years. We believe that the combination of increased transparency through expanded information reporting and targeted legislation aimed at tax abuse loopholes would make the strategy for the Reduce Opportunities for Evasion component more robust.

Consistent funding for multiyear research is necessary to update estimates and understand noncompliant behavior

We concur that a multiyear commitment to research is a vital component to reducing the tax gap. We also agree that continuous measurement and updating of the various taxpayer segments and

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[6] House Small Business Committee Hearing on Tax Gap, April 26, 2007.
[7] *Tax Gap Whitepaper*, dated May 24, 2007.
[8] *Significant Challenges Exist in Determining Whether Taxpayers With Schedule C Losses Are Engaged in Tax Abuse* (Reference Number 2007-30-173, dated September 7, 2007).
[9] *Actions Are Needed to Eliminate Inequities in the Employment Tax Liabilities of Sole Proprietorships and Single-Shareholder S Corporations* (Reference Number 2005-30-080, dated May 2005).

components are needed to identify where scarce resources can be applied to improve compliance. However, research efforts need to go beyond compliance measurement. The behavioral aspects of noncompliance need to be better understood so that effective treatment remedies can be applied. For example, IRS research studies show that there is an extremely high recidivism rate for individual nonfilers in the years following IRS-imposed tax assessments and penalty treatments. This situation suggests that the IRS process is less than effective in achieving future compliance.

Further, the NRP research measurement process is very costly in terms of time expended and the use of examination resources. The estimated cost of the NRP of Tax Year 2001 individual taxpayers was approximately $150 million.[10] The NRP study of Subchapter S corporations will take 2 to 3 years to complete. Some tax segments could require sample sizes larger than the annual number of returns examined in the operational examination program, which would put considerable strain on operational resources. Thus, consistent funding above operational levels is required to assure that this component will be successful.

Finally, we previously recommended that the IRS Commissioner consider establishing a tax gap advisory panel that includes tax and economic experts to identify ways to better measure voluntary compliance.[11] In 2007, the IRS established an advisory group to validate and improve its estimation methods.

Continued improvements in information technology and the success of BSM are essential for reducing the tax gap

Improving tax administration by modernizing the IRS' outdated computer systems is necessary to more efficiently collect taxes. However, the success of BSM is contingent on continued funding and successful planning, design, development, and implementation. Both the Government Accountability Office and we regularly review BSM and have noted the progress the IRS is making in addressing concerns raised about the management of this highly complex, multibillion-dollar effort. For example, we recently reported[12] that the IRS successfully developed and executed plans for delivering a key automated system intended to provide employees with the ability to update taxpayer accounts on demand and respond to taxpayer inquiries more quickly and accurately.

While the IRS has made progress, the BSM program remains on the Government Accountability Office's high-risk list, in part, to ensure that the program receives the requisite amount of oversight. This is not surprising given the considerable investment that has been made in the

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[10] A significant portion of the $150 million was for examination resources in the form of examiner labor hours. Those examiners would have worked other cases if they did not work NRP cases.
[11] *Some Concerns Remain About the Overall Confidence That Can Be Placed in the Internal Revenue Service Tax Gap Projections* (Reference Number 2006-50-077, dated April 2006).
[12] *Account Management Services Is Meeting Its Development Goals* (Reference Number 2008-20-053, dated March 3, 2008).

program, the shortcomings the IRS has experienced in meeting cost and completion commitments, and the critical role it has in supporting IRS tax gap reduction strategies. Like the Government Accountability Office, we consider BSM a major management challenge.

Since Fiscal Year 2002, our Modernization program annual assessments have cited the following four specific challenges that the IRS needs to overcome to deliver a successful modernization effort:

1. Implement planned improvements in key management processes and commit necessary resources to enable success.
2. Manage the increasing complexity and risks of the Modernization program.
3. Maintain the continuity and strategic direction with experienced leadership.
4. Ensure that contractor performance and accountability are effectively managed.

In the 2007 Annual Assessment of BSM, we recommended that the Chief Information Officer continue to address Modernization program corrective actions from our and Government Accountability Office reports through the *Highest Priority Initiatives* process. By focusing corrective action efforts through this process, the IRS could achieve resolution of the challenges that we had identified and subsequently address downgrading the Modernization material weakness. IRS management agreed with the recommendation.

We consider BSM the greatest management challenge to the IRS.[13] Because the tax gap reduction strategy places significant emphasis on improving and enhancing information technology to achieve greater efficiencies, there is considerable management risk. Therefore, continued attention to the challenges we have identified, along with sufficient funding, are necessary to address the risk that BSM delays and failures will adversely affect tax gap reduction plans.

Improving compliance activities is costly and might have a limited effect on reducing the tax gap

To significantly reduce the tax gap, the enforcement cycle must be completed. In other words, the tax noncompliance must be identified, and the tax must be assessed and collected.

With regard to the tax gap, the process of detecting noncompliance and collecting the revenue is costly and often a resource-intensive task. Noncompliance is virtually nonexistent when there is withholding and information reporting. When there is some information reporting, noncompliance is 8.6 percent. However, when there is little or no information reporting, the

[13] *Treasury Inspector General for Tax Administration Office of Audit Annual Audit Plan Fiscal Year 2008, Appendix II.*

noncompliance rate exceeds 53 percent. The primary method used to identify noncompliance by self-employed taxpayers, who make up one-half of the underreporting tax gap, is examination.

However, the methods used to estimate the underreporting portion of the tax gap highlight the difficulties encountered in identifying the noncompliance. Dr. Eric J. Toder, a Senior Fellow at the Urban Institute, recently described the estimation method that the IRS uses to determine the amount of underreported income that examiners do not detect. As a hypothetical example, Dr. Toder used a factor of approximately 3.5 times the amount that was identified. That is, if an examiner identified $100 in underreported income, the IRS would project that the examiner did not detect another $250 of underreported income, resulting in a total estimate of $350 in unreported income. Obviously, the IRS cannot assess tax on the $250 if it cannot be detected. So, even if the IRS examined 100 percent of all returns, they would identify only a small portion of the $285 billion underreporting gap.

Further, while there is little debate on the need for increased IRS enforcement resources, this is not a quick path to eliminating the tax gap. Because the largest portion of the tax gap is not yet assessed, the IRS must identify the noncompliant taxpayer, examine the return, and then assess the tax. After these processes, the IRS attempts to collect the tax due. The ability to efficiently and effectively complete this enforcement cycle is affected by a combination of laws and regulations, internal polices and procedures, technology, and human capital management.

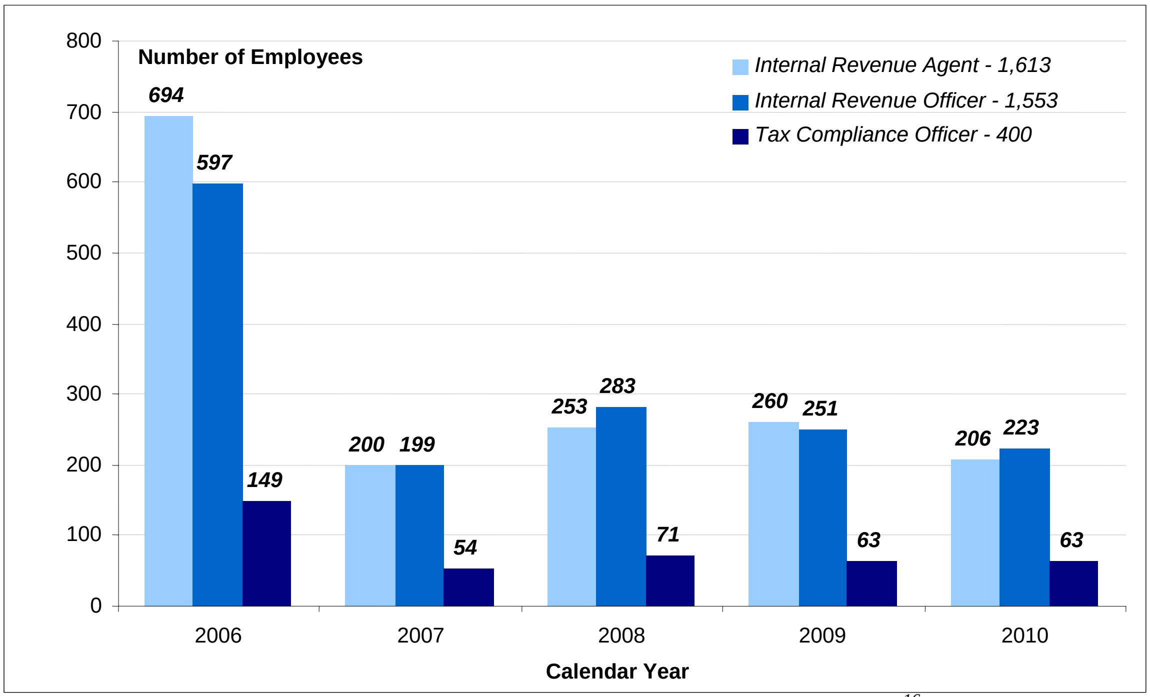
Realizing additional collected revenue by adding additional examination resources shows a modest initial return on investment. Newly hired agents need to be trained and take several years to reach their full potential. Our analysis showed that from January 1, 2003, through December 31, 2005, the IRS hired 1,529 new revenue agents.[14] For every $1 in salary that was paid, the Department of the Treasury has collected $1.40 in additional tax revenue. The salary figures do not include overhead, training, or opportunity costs for experienced revenue agents working with new revenue agents. As the Federal Government workforce changes over the next decade, the challenges of replenishing IRS enforcement programs with new employees could adversely affect the IRS' ability to significantly increase revenue through the enforcement process. The IRS estimates that approximately 40 percent of its more than 12,000 revenue agents will be eligible to retire by the end of Fiscal Year 2008.

The Small Business/Self-Employed Division is responsible for taxpayers who contribute the most to the tax gap. The workforce transition for this Division will be considerable in the next few years. A Treasury Inspector General for Tax Administration analysis of IRS data shows that by December 31, 2010, approximately 27 percent (3,566 of 13,397) of the compliance employees[15] in the Division will be eligible to retire. Figure 3 shows when these employees will

[14] The 1,529 new revenue agents were identified from the Treasury Integrated Management Information System. See details in Appendix I.
[15] Revenue agents, revenue officers, and tax compliance officers who are not part of the Small Business/Self-Employed Division Campus Compliance Services Organization.

be eligible to retire. The IRS has a limited ability and capacity to effectively hire and train new employees. The combination of increased compliance staffing and replacing retired employees could adversely affect compliance results.

Figure 3: Retirement Eligibility - Select Small Business/Self-Employed Division Employees



Source: Our analysis of Treasury Integrated Management Information System data.[16]

While the IRS has devoted significant efforts to the human capital issue, the risks of this major workforce transition to the enforcement cycle are considerable. For example, the number of sole proprietors, who commonly operate on a cash basis, is expected to grow. There is very little or no information reporting for this sector of taxpayers, and noncompliance is high. As a result, the IRS' ability to continue to enforce compliance through the examination process could be significantly challenged.

Enhanced taxpayer service might reduce only the part of the tax gap related to unintentional errors

Taxpayer service is an important component in combating the tax gap. However, it can address only the noncompliance that is related to unintentional errors caused by the complexity and

[16] For 2006, the numbers represent the number of employees eligible to retire as of the end of 2006 and include employees who became eligible to retire in previous years but have not yet retired. For all other years, the numbers represent the number of employees who will become eligible to retire in that year.

confusion surrounding the tax laws. The IRS does not know what portion of the tax gap is the result of intentional errors. Offering assistance to taxpayers who do not intend to comply will have no effect on the voluntary tax compliance rate and thus not reduce the tax gap.

Reforming and simplifying the tax law might result in reducing the tax gap, but few recommendations have been identified

Stakeholders have provided specific suggestions for tax simplification for many years. Since the inception of the Internal Revenue Code, there have been calls for simplification. For example, a March 1920 *New York Times* article discussed the complexity of the tax system and the need for tax simplification when there were only 7 million taxpayers who filed tax returns. The Joint Committee on Taxation was founded in 1926 to make recommendations to simplify the tax code.

More recently, in April 2001, the Joint Committee on Taxation released a report on the overall state of the Federal tax system and recommendations for simplification.[17] The report contained more than 1,300 pages and took approximately 18 months to complete. The study made specific recommendations for ways to simplify the tax code without changing the policy behind the law. The report was issued because Internal Revenue Code Section 8022(3)(B) requires that a report on the overall state of the Federal tax system and recommendations with respect to possible simplification proposals be produced during each Congress.

The Joint Committee on Taxation study addressed the effect that tax law complexity has on voluntary compliance. The overall thrust of the analysis was targeted at the confusion that taxpayers face when the law is complex or the opportunity that complexity ". . . fosters with multiple interpretations of the law and aggressive planning opportunities." However, the link between tax simplification and the tax gap was not made beyond the adverse effect complexity has on voluntary compliance.

In that same year, the American Institute of Certified Public Accountants (AICPA) issued the *Guiding Principles for Tax Simplification*,[18] which provided that organization's framework for achieving tax simplification. The Guiding Principles developed by the AICPA are:

- *Make simplification a priority*. Simplification must be viewed as a priority tax policy objective and given substantial consideration in conjunction with the development of legislation and administrative guidance.
- *Seek simplest approaches.* Once tax lawmakers identify desired tax policy or revenue objectives, the simplest and most transparent approaches to implementation should be sought.

[17] *Joint Committee on Taxation, Study of the Overall State of the Federal Tax System and Recommendations for Simplification*, April 2001.
[18] *Tax Policy Concept Statement No. 2: Guiding Principles for Tax Simplification*, 2002.

- *Minimize compliance burdens.* Compliance costs, in terms of both time and money, should be minimized and should be commensurate with the resources and abilities of the affected taxpayers.
- *Reduce frequency of tax law change.* Change in and of itself increases complexity in the short term, even if the change will produce long-term simplification. Tax laws should be revised only to address changes in revenue needs, to implement significant changes in tax policy, or to alleviate existing complexities and inconsistencies.
- *Use consistent concepts and definitions.* Inconsistencies in legal concepts and definitions should be eliminated in existing law and avoided in the drafting of new laws.
- *Consider administrative burdens.* The ability of tax agencies to administer, provide guidance on, and enforce the law must be considered in the development of legislative and administrative guidance.
- *Avoid limited applicability.* Tax rules that apply to a limited set of taxpayers or for only a short period of time should be avoided.

The AICPA also provided a noteworthy Policy Statement:

> *In this document, Tax Policy Concept No. 2, Guiding Principles for Tax Simplification[,] the AICPA reaffirms its support of efforts to reduce complexity in existing federal and state tax laws and to curtail incremental complexity in the future. Although an absolutely simple tax system may not be feasible in today's complex business and economic environment, a relatively simpler tax system is possible. Further, a simpler tax system will benefit individual taxpayers, businesses, federal and state tax agencies and the economy.*

While it is clear that major tax system stakeholders believe simplification would improve voluntary compliance, the Reform and Simplify the Tax Law component has only three recommendations for simplification. The IRS has some information concerning where the Internal Revenue Code could be improved through simplification. However, there is a longstanding Department of the Treasury policy that the IRS does not comment on "tax policy." We believe that the IRS and the Department of the Treasury must coordinate to provide comprehensive recommendations to reform and simplify the tax law.

Appendix I

Detailed Objective, Scope, and Methodology

The overall objective of this review was to determine the progress of the plans and actions taken by the IRS to reduce the tax gap.[1] During our review, we relied on computer-processed data contained in the Treasury Integrated Management Information System, the Examination Return Control System, the Audit Information Management System, and the Master File.[2] We did not establish the reliability of these data because extensive data validation was outside of the scope of this audit. This did not affect the results contained in the report. Also, we did not assess internal controls because to do so would not have been applicable within the context of our audit objective. To accomplish our objective, we:

I. Compiled and evaluated the IRS' strategies, plans, and actions designed to address tax gap issues.

   A. Interviewed IRS officials and determined progress made on plans to reduce the tax gap, including the Department of the Treasury Office of Tax Policy September 2006 report entitled *A Comprehensive Strategy for Reducing the Tax Gap*.

   B. Identified completion dates, barriers, and whether management actions will have a quantifiable impact on the tax gap.

   C. Calculated the return on investment of hiring additional revenue agents.

      1. Identified the number of new revenue agents hired from January 1, 2003, through December 31, 2005, on the Treasury Integrated Management Information System. The revenue agents were on this System as of the end of 2006 and were hired in 2003, 2004, and 2005. Salary information for the 1,529 agents was extracted from the System for the end of 2003, 2004, 2005, and 2006.

      2. Matched the Treasury Integrated Management Information System information on the 1,529 new revenue agents with the Examination Return Control System to identify the return examinations conducted by each agent. The combined information was then matched to the Audit Information Management System for assessment data and the Individual Master File for payment data for examinations closed before July 1, 2006.

[1] The tax gap, estimated at $345 billion for Tax Year 2001, is the difference between taxes that are legally owed and taxes that are paid on time.
[2] See Appendix IV for a glossary of terms used in this report.

D. Determined the number of Small Business/Self-Employed Division compliance employees[3] eligible to retire by December 30, 2010, by extracting retirement-eligible date information from the Treasury Integrated Management Information System.

E. Determined whether the IRS has considered external studies and reports on the tax gap and has used this information in its planning efforts.

F. Identified Congressional concerns for tax gap areas and determined how and whether these issues have been addressed by the IRS.

II. Identified research efforts by the Office of Research, Analysis, and Statistics to reduce the tax gap.

A. Evaluated the plans for the NRP and other research efforts related to the tax gap.

B. Determined when research data will be available and how and when the IRS plans to use the research data.

III. Reviewed completed, ongoing, and planned research efforts of the National Taxpayer Advocate that would affect the tax gap.

IV. Obtained the status of the 16 Fiscal Year 2008 tax gap legislative proposals and analyses to determine their viability and potential revenue impact.

[3] Revenue agents, revenue officers, and tax compliance officers who are not part of the Small Business/ Self-Employed Division Campus Compliance Services Organization.

Appendix II

Major Contributors to This Report

Daniel R. Devlin, Assistant Inspector General for Audit (Small Business and Corporate Programs)
Margaret E. Begg, Acting Assistant Inspector General for Audit (Small Business and Corporate Programs)
Frank Dunleavy, Director
Philip Shropshire, Director
Lisa Stoy, Audit Manager
Joan R. Floyd, Lead Auditor
Earl Charles Burney, Senior Auditor
Theodore J. Lierl, Senior Auditor
Rosemarie M. Maribello, Senior Auditor

Appendix III

Report Distribution List

Commissioner C
Office of the Commissioner – Attn: Chief of Staff C
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Commissioner, Tax Exempt and Government Entities Division SE:T
Commissioner, Wage and Investment Division SE:W
National Taxpayer Advocate TA
Director, Office of Research, Analysis, and Statistics RAS
Chief Counsel CC
Director, Office of Legislative Affairs CL:LA
Director, Office of Program Evaluation and Risk Analysis RAS:O
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- Commissioner, Tax Exempt and Government Entities Division SE:T
- Commissioner, Wage and Investment Division SE:W
- National Taxpayer Advocate TAS
- Director, Office of Research, Analysis, and Statistics RAS

Appendix IV

Glossary of Terms

Account Management Services – A project that will modernize the ability to collect, view, retrieve, and manage taxpayer information by providing a common user interface for access and update of taxpayer accounts managed by a number of systems.

Audit Information Management System – A computer system used to control returns, input assessments/adjustments to the Master File, and provide management reports.

Automated Collection System – A telephone contact system through which telephone assistors collect unpaid taxes and secure tax returns from delinquent taxpayers who have not complied with previous notices.

Automated Substitute for Return Refund Hold Program – A program that minimizes revenue loss by holding the current-year refunds of taxpayers who are delinquent in filing individual income tax returns and are expected to owe additional taxes.

Automated Underreporter – The automated analysis and processing of potential underreported and/or overreported issues identified through information return matching.

Campus – The data processing arm of the IRS. The campuses process paper and electronic submissions, correct errors, and forward data to the Computing Centers for analysis and posting to taxpayer accounts.

Collection Due Process – A process that gives taxpayers an opportunity to raise any relevant issues pertaining to a lien or proposed levy by filing a hearing request.

Collection Field function – The unit in the field offices consisting of revenue officers who handle personal contacts with taxpayers to collect delinquent accounts or secure unfiled tax returns.

Compliance Data Warehouse – A data warehouse specifically designed to meet the unique needs of research analysts throughout the IRS.

Computer Security Incident Response Center – The organization that provides proactive prevention, detection, and response to computer security incidents targeting the IRS' enterprise information technology assets.

Customer Account Data Engine – An online, modernized data infrastructure that will house the taxpayer account and return data. The Customer Account Data Engine replaces the IRS Master File, the repository of all taxpayer information.

Examination Return Control System – An automated inventory system used for controlling tax returns and technical time charges.

Individual Master File – The IRS database that maintains transactions or records of individual tax accounts.

IRS Oversight Board – The organization responsible for oversight of the IRS in its administration, management, conduct, direction, and supervision of the execution and application of the internal revenue laws.

Master File – The IRS database that stores various types of taxpayer account information. This database includes individual, business, and employee plans and exempt organizations data.

Misclassified Worker – An individual that has been classified by his or her employer as an independent contractor/self-employed individual instead of an employee to reduce the tax liability by not paying State and Federal Unemployment Insurance, Social Security, and Medicare taxes.

National Taxpayer Advocate – The individual who heads the National Taxpayer Advocate Service, an independent organization within the IRS whose employees assist taxpayers who are experiencing economic harm, who are seeking help in resolving tax problems that have not been resolved through normal channels, or who believe that an IRS system or procedure is not working as it should.

Return on Investment – The net profit or loss in an accounting period divided by the capital investment used during the period, usually expressed as an annual percentage return.

Revenue Agent – An employee in the Examination function who conducts face-to-face examinations of more complex tax returns such as businesses, partnerships, corporations, and specialty taxes (e.g., excise tax returns).

Revenue Officer – An employee in the Collection Field function who attempts to contact taxpayers and resolve collection matters that have not been resolved through notices sent by the IRS campuses (formerly known as service centers) or the Automated Collection System.

Revenue Procedure – An official IRS statement spelling out the administrative practices used by the IRS.

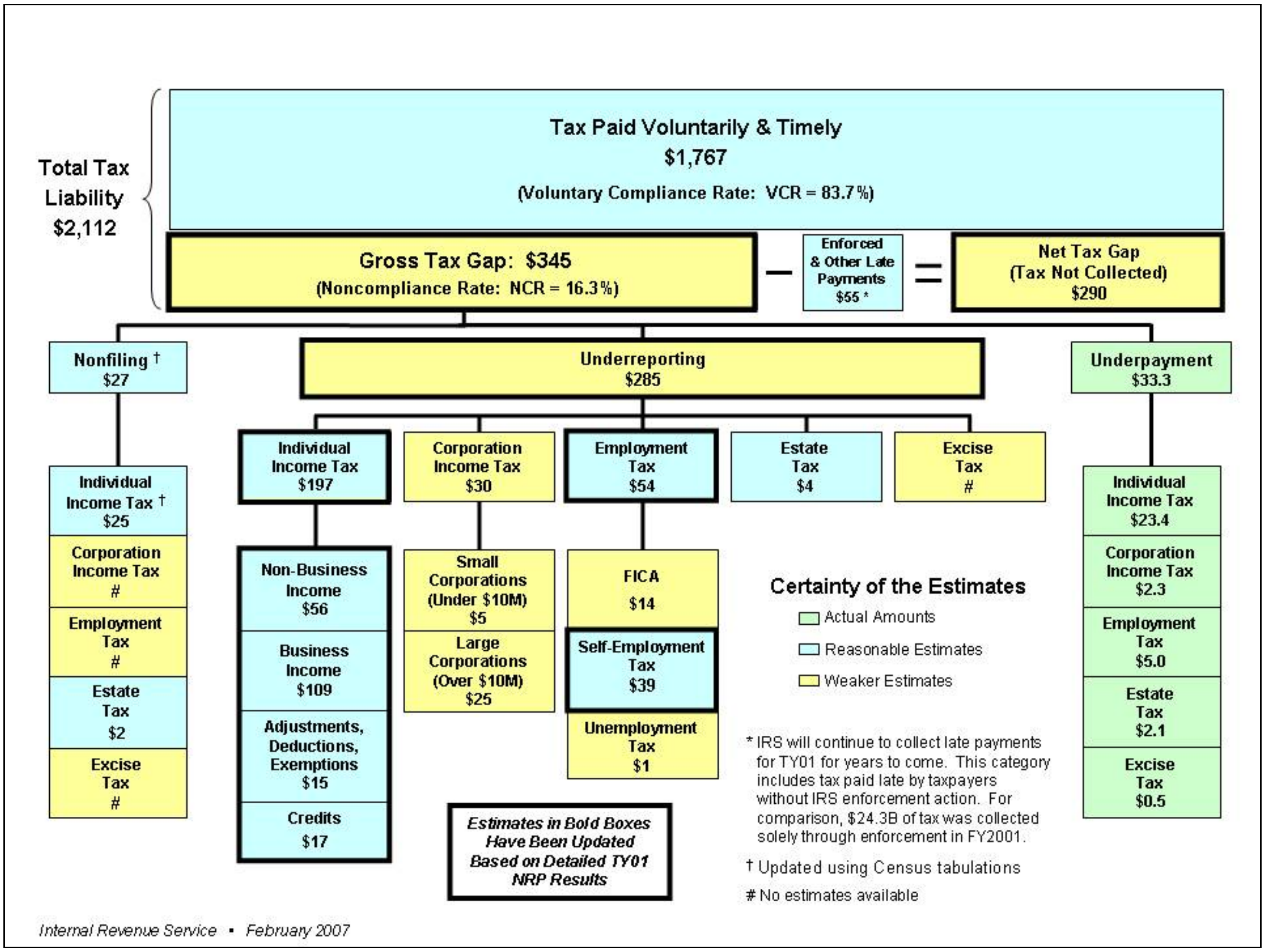
Revenue Ruling – A published decision by the IRS, printed in the Internal Revenue Bulletin, dictating how the Federal tax code applies to a particular situation.

Tax Compliance Officer/Tax Auditor – An employee in the Examination function who primarily conducts examinations of individual taxpayers through interviews at IRS field offices. The position title was changed in 2002 from tax auditor to tax compliance officer.

Treasury Integrated Management Information System – The official automated Department of the Treasury personnel and payroll system.

Appendix V

Tax Gap Map for Tax Year 2001
(in $ Billions)



Source: IRS Office of Research, Analysis, and Statistics.
Legend: FICA = Federal Insurance Contribution Act. TY = Tax Year; TY01 = Tax Year 2001. FY = Fiscal Year. Small Corporations include corporations with assets of less than $10 million. Large Corporations include corporations with assets of $10 million and greater.

Appendix VI

Summary of Legislative Proposals for Fiscal Year 2008

Proposal (* = Similar proposal included in Fiscal Year 2007 Budget)	Revenue Estimates ($ millions): Department of the Treasury	Revenue Estimates ($ millions): Joint Committee on Taxation	Status[1]
1. Require information reporting on payments to corporations	7,736	1,690	N
2. Require basis reporting on security sales	6,709	3,265	I
3. Expand broker information reporting	1,974	2,470	N
4. Require information reporting on merchant payment card reimbursements*	10,745	10,745	N
5. Require a certified Taxpayer Identification Number from contractors	749	174	N
6. Require increased information reporting for certain Federal Government payments for property and services*	390	100	N
7. Increase information returns penalties	546	546	I
Totals: Proposals to expand information reporting	**28,849**	**18,990**	
8. Require electronic filing by certain large organizations	0	0	N
9. Implement standards clarifying when employee leasing companies can be held liable for their clients' Federal employment taxes*	57	0	N
10. Amend Collection Due Process[2] procedures for employment tax liabilities*	364	288	P
Totals: Proposals to improve compliance by businesses	**421**	**288**	

[1] Legend: N = Not included in any current legislation as of November 2007.
I = Included in current pending legislation as of November 2007.
P = Passed as part of the Small Business and Work Opportunity Tax Act of 2007, Pub. L. No. 110-28, Sections 8201-8248.

[2] See Appendix IV for a glossary of terms used in this report.

Proposal (* = Similar proposal included in Fiscal Year 2007 Budget)	Revenue Estimates ($ millions): Department of the Treasury	Revenue Estimates ($ millions): Joint Committee on Taxation	Status
11. Expand IRS access to information in the National Directory of New Hires for tax administration purposes	0	0	N
12. Permit disclosure of prison tax scams	5	5	I
13. Make repeated willful failure to file a tax return a felony	12	5	N
Totals: Proposals to strengthen tax administration	**17**	**10**	
14. Expand preparer penalties*	80	82	P
15. Impose a penalty on failure to comply with electronic filing requirements	0	0	N
16. Create an erroneous refund claim penalty	98	98	P
Totals: Proposals to expand penalties	**178**	**180**	
Grand Totals	**29,465**	**19,468**	

Source: General Explanations of the Administration's Fiscal Year 2008 Revenue Proposals, February 2007, and Description of Revenue Provisions Contained in the President's Fiscal Year 2008 Budget Proposal, March 2007 (except for those proposals that were included in the Small Business and Work Opportunity Tax Act of 2007). For those proposals, see Estimated Revenue Effects of the Small Business and Work Opportunity Tax Act of 2007, May 2007.