A Closer Look: Impacting the Tax Gap

The gross Tax Gap is the difference between the amount of tax owed by taxpayers for a given year and the amount that is actually paid timely for that same year. It represents, in dollar terms, an estimate of the annual amount of noncompliance with our tax laws. Many commentators have pointed to the Tax Gap as a roadmap for funding additional national priorities, cut taxes, or limit the need for tax increases. They reason that the government should prioritize full payment of taxes already legally owed before it looks to impose additional tax obligations on the general public. It is an important topic.

Reducing the Tax Gap and improving compliance is a central part of the IRS mission, which is to: “Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and enforce the law with integrity and fairness to all.” Our mission statement reflects our values: we put “service” first making it easier for Americans to understand and satisfy their tax obligations as the most important thing the IRS can do to affect the Tax Gap.

The IRS will also, however, enforce the tax laws against those who choose not to voluntarily fulfill their responsibilities. Indeed, our enforcement efforts serve taxpayers generally, the vast majority of whom want to comply with their tax obligations, by legitimizing that choice and giving them comfort that we support them and will aggressively enforce the laws against those who do not pay their fair share. In this regard, our enforcement efforts support compliant taxpayers and a fair and equitable tax system.

Computing the Tax Gap

The Tax Gap is determined by the IRS Research, Applied Analytics and Statistics (RAAS) organization. It is mostly divided into three components: non-filing (the tax not timely paid by those who do not timely file the required returns), underreporting (the net understatement of tax on timely filed returns), and underpayment (the amount of tax reported on timely filed returns that is not timely paid). More detail about the various components of the Tax Gap can be found in IRS Publication 5365.

The most recent Tax Gap study released in 2019 covered Tax Years (TY) 2011-2013 (generally returns filed during calendar years 2012-2014). For that time period, the estimated Gross Tax Gap (the amount of “true” tax that is not paid voluntarily and timely) was $441 billion. The Net Tax Gap is the amount of tax that will not be paid after subtracting from the Gross Tax Gap the portion that eventually will be collected as a result of IRS enforcement activities or paid late but voluntarily by taxpayers. RAAS estimated that $60 billion of the Gross Tax Gap eventually would be paid – either voluntarily or collected through IRS administrative and enforcement activities – resulting in an annual Net Tax Gap of $381 billion of taxes owed as compared to what is actually paid.

Looking at the components, the non-filing Gross Tax Gap was estimated at $39 billion, the underreporting Gross Tax Gap was $352 billion and the underpayment Gross Tax Gap was $50 billion. And by the various types of taxes, the estimated Gross Tax Gap for individual income tax was estimated at $314 billion, the Gross Tax Gap for corporate income tax was $42 billion, the Gross Tax Gap for employment tax $81 billion, and the Gross Tax Gap for estate and excise tax combined was $3 billion.

There have been four IRS Tax Gap estimate releases since resumption of actual examinations of statistically representative samples of individual income tax returns through the National Research Program (NRP) beginning with a large, periodic sample for TY 2001 and smaller, annual samples beginning with TY 2006 and through TY 2015. The Tax Gap for TY 2001 was released in 2005 and revised in 2006; for TY 2006 was released 2012; for TY 2008-2010 (average annual) was released in 2016; and for TY 2011-2013 (average annual) was released in 2019.

Over the years our studies have consistently suggested that overall tax compliance is holding steady in the 82 percent to 84 percent range (the actual dollars represented by the Tax Gap can be impacted by whether the country is experiencing a recessionary economy but the percentage has remained mostly steady since about 2001). For TY 2011-2013, the estimated Tax Gap translated into about 83.6% of taxes paid voluntarily and on time, which is in line with recent levels. This estimate is essentially unchanged from a *revised* TY 2008-2010 estimate of 83.8%.[1] After enforcement efforts are taken into account, the estimated share of taxes eventually paid is 85.8% for both periods and is in line with the estimates for TY 2001 and TY 2006 of 86.3% and 85.5%, respectively.

Tax Gap estimates are most accurate when based on actual taxpayer compliance data for the years being estimated. There is an inherent lag time between the years analyzed and the year the Tax Gap estimates are released by RAAS because it takes several years to conduct audits, collect payments, and close cases, and then analyze the results. However, there is a tradeoff between having more contemporaneous estimates and having underreporting Tax Gap

[1] The approaches used to estimate the various tax gap components for TY 2011–2013 generally follow the methods used for the previous TY 2008–2010 estimates. Newly available data, however, resulted in some modifications to the estimation approaches. For the TY 2011–2013 estimates, the availability and timing of new data allowed contemporaneous estimation of Detection Controlled Estimation (DCE), an improvement over the method used in the originally published TY 2008–2010 estimates.

estimates based on actual observed reporting behavior. In an effort to provide more frequent and timely updates, RAAS is actively developing methods to "forecast" the Tax Gap in advance of actually reporting compliance data and then revising the estimates as actual data are later collected and analyzed.

These new approaches and methodologies designed by RAAS would enhance the currency of future Tax Gap estimates as well as identify possible additional sources contributing to the Tax Gap. For example, the estimated Tax Gap for TY2011-2013 might be understated to the extent that they don't fully reflect the noncompliance associated with a measure attributable to compliance by taxpayers conducting transactions in virtual currencies. There are now approximately 8,600 virtual currencies with a current global market cap of almost $2 trillion.[2] Recognizing likely compliance challenges, the IRS has focused significant enforcement resources over the past two years in the virtual currency environment.

In addition to most taxable virtual currency transactions, the Tax Gap estimate for TY2011-2013 also doesn't fully reflect noncompliance related to certain foreign transactions and activities, illegal source income (which is taxable and is pursued by the IRS often in coordination with other federal and state agencies) and other types of concealed taxable income. A recently released study focusing on only two issues - unreported offshore income and concealment through the use of pass-through entities (partnerships and tiered partnership arrangements often coupled with S corporations, private foundations and foreign entities) – determined the current Tax Gap computation should include an additional $33 billion of taxes annually which is primarily attributable to the top 1% of all taxpayers.[3] The study further provides "We estimate that 36% of federal income taxes unpaid are owed by the top 1% and that collecting all unpaid federal income tax from this group would increase federal revenues by about $175 billion annually."[4]

Another recent study suggests that the aggregate Tax Gap over the course of the next decade will be approximately $7.5 trillion (or roughly $750 billion annually).[5] Grossed up to include taxable transactions involving virtual currencies, undisclosed offshore transactions, undeclared taxes associated with abuse in the use of pass-through organizations and tax exempt entities, illegal source income and other types of tax evasion vehicles, it would not be surprising if the noncompliance for tax years going forward exceeded $1 trillion, annually.

[2] https://coinmarketcap.com/

[3] "Tax Evasion at the Top of the Income Distribution: Theory and Evidence," John Guyton, Patrick Langetieg, Daniel Reck, Max Risch & Gabriel Zucman (March 2021), https://www.nber.org/papers/w28542

[4] Id.

[5] Shrinking the Tax Gap: Approaches and Revenue Potential," Natasha Sarin and Lawrence H. Summers, Tax Notes, November 18, 2019 ("Over the course of the next decade, barring changes in tax administration efforts, we can expect to lose an estimated $7.5 trillion, or around 3 percent of GDP, annually that our existing law should allow us to collect.").

As suggested, a multi-faceted approach of increased specialized enforcement staffing, enhanced electronic information reporting, and increased investments in technology could raise over $1 trillion by allowing the IRS to better leverage the information it receives.[6]

Information Reporting and Withholding

In terms of what makes up the Tax Gap, the underreporting of business income by individual taxpayers – income of sole proprietors, farmers and those earning rental, royalty, partnership, and S Corporation income – is a major contributor. RAAS estimates that about 60 percent of the Tax Gap comes from underreporting of income, including business income, on individual tax returns. The lack of reliable and comprehensive reporting and withholding for business income received by individuals is a significant reason for these findings.

Tax compliance is far higher when reported amounts are subject to third-party information reporting and, even more so, when also subject to withholding. IRS data shows that in instances where income is subject to little or no information reporting or withholding (such as in the sale of a business, sole proprietor, rents, and royalties), compliance is as low as 45 percent. When substantial information reporting is implemented (such as for interest and dividend income, pensions and annuities, unemployment and social security, and state income tax refunds), compliance rises above 95 percent. Combining substantial information reporting and withholding (such as for wages, salaries, and tips) results in nearly 100 percent compliance.

"Visibility" of income sources and financial transactions is a significant contributor to increasing the compliance rate, and enhanced information reporting is one of the few means of sizably increasing that rate. In short, the more transparent a taxable payment is to the IRS, the more likely it is to be reported. As one example of IRS efforts at transparency, the 2019 Form 1040 included, *for the first time,* specific questions regarding a taxpayer's involvement in virtual currencies. The first page of the 2020 Form 1040 now asks: "At any time during 2020, did you receive, sell, send, exchange, or otherwise acquire any financial interest in any virtual currency?"

Customer Service

It is important to point out that failures to comply with tax law often involve unintentional mistakes that are the result of not fully understanding what has come to be an extremely complex tax code. For that reason, efforts to reduce the Tax Gap and increase overall tax compliance absolutely must include efforts to assist taxpayers in meeting their filing,

---

[6] Id.

reporting and payment obligations, issuance of timely and clear guidance and programs to educate taxpayers in their tax obligations.

Taxpayers having questions are encouraged to initially go to IRS.gov, which has already received more than 1 billion visits in calendar year 2021. IRS "Level of Service" generally refers to the volume of telephone calls answered by IRS Customer Service Representatives (CSRs). The IRS has FY2021 appropriated funding for almost 14,800 CSRs, based on a Congressional Budget Justification that was submitted pre-COVID-19 pandemic, pre-EIP1, pre-EIP2, and pre-EIP3 with a requested LOS of ~75% and an appropriated LOS of 50%. Factors affecting our LOS delivery include staffing and hiring due to the COVID-19 pandemic; increased assistor call demand; and handle time due to call complexity and related factors. Each 10% increase in LOS requires a funding appropriation of ~$100 million and CSRs receive ~14 weeks of training before being available to respond to phone inquiries. As such, it is extremely difficult to somehow increase LOS during a significant, unexpected rise in taxpayer contacts.

To ensure taxpayers have immediate access to information without having to make a phone call, we provide taxpayers with options so they can now engage with us to address issues remotely and digitally, including access to a new "chat" function as part of our Taxpayer Digital Communications program. We've expanded customer callback, saving Americans hundreds of thousands of hours waiting for assistance, with plans to offer callback options on up to 40 percent of taxpayer calls during the FS21. We've added new features to the IRS Online Account and created new web applications like *"Get My Payment"* for tracking EIPs and the *"Tax Withholding Estimator"* for taxpayer use in estimating payroll withholding. We recently achieved the long-time goal of enabling taxpayers to e-File amended returns – effective for e-Filed 1040 and 1040-SR returns for tax year 2019 and later. We have also redesigned our online EITC Assistant such that is it more user friendly.

And to improve service to taxpayers who are more comfortable in languages other than English, the IRS is enhancing multilingual web content, forms and instructions and leveraging behavioral economics insights to promote voluntary compliance through improved outcomes for filing, payment, and reporting. We are extremely proud that for the 2021 filing season, for the first time, we are also providing the Form 1040 in Spanish. Also, for the first time, the 2020 Form 1040 will give taxpayers the opportunity to indicate whether they wish to be contacted in a language other than English. New Schedule LEP allows taxpayers to check a box letting us know in which of 20 languages they prefer to receive written communications from the IRS. So far this year more than 220,000 taxpayers have electronically submitted a Schedule LEP with their return. Additionally, through coordination and collaboration with our partners, Economic Impact Payment outreach materials were distributed in more than 35 languages.

Other recent changes include making Publication 1, *Your Rights as a Taxpayer*, available in 20 languages. Also, we have issued a new, streamlined version of Publication 17, *Your Federal Income Tax*, that is easier to navigate and faster to download than previous versions, and is now accessible on most personal electronic devices. The new Publication 17 is available in English, Spanish, Chinese (Traditional and Simplified), Vietnamese, Russian and Korean, and we are working to make it available in other languages as well.

Additionally, taxpayers who interact with an IRS representative by phone now have access to over-the-phone interpreter services in more than 350 languages. The IRS has also recently begun inserting information about translation services and other multilingual options into the high-volume notices we send out to taxpayers.

We are extremely proud to be serving taxpayers in their most comfortable language and by doing this we hope to reduce their anxiety and increase their knowledge and retention of the guidance being provided, leading to better compliance.

Modernization Improvements Impact Voluntary Compliance

We must modernize to reduce our dependency on our legacy systems and increase our ability to be as flexible as possible. Doing so will allow us to deliver improvements to tax administration that meet the needs, desires, and expectations of *all* taxpayers, including the most unsophisticated and the most sophisticated taxpayers. As we modernize, we must retain the ability to engage with taxpayers in-person, on the phone and through other traditional means of communication and interactions.

Modernization requires predictable, and consistent multi-year funding. In 2019, the IRS released a six-year IRS Modernization Plan and delivered 60 capabilities in the first two years of the plan. Through the first three years of the plan (FY 2019-2021), IRS has received just over half (~55%) of the planned Business Systems Modernization funding, requiring significant rescoping and rescheduling even with our use of supplementary sources such as inter-appropriation transfers to support delivery, which proceeded at a slower pace than initially planned.

Research on high wealth noncompliance

Several RAAS researchers recently participated in a study published by the National Bureau of Economic Research (NBER) entitled *"Tax Evasion at the Top of the Income Distribution: Theory and Evidence."* [7] This study examined tax evasion at the highest income levels and estimated that the top 1 percent of Americans hide more than 20 percent of their income

[7] "Tax Evasion at the Top of the Income Distribution: Theory and Evidence," John Guyton, Patrick Langetieg, Daniel Reck, Max Risch & Gabriel Zucman (March 2021), https://www.nber.org/papers/w28542

from the IRS. With more, specialized, and targeted enforcement resources, the IRS could significantly reduce the income tax gap for the top 1% and collect another $175 billion of taxes *annually.*

As to why sophisticated tax evasion seems so concentrated at the top, the study suggests that (i) concealment of tax evasion from auditors is costly, requiring substantial financial sophistication, (ii) high-income people can save huge amounts of tax with little risk by adopting sophisticated strategies, which makes it worth the cost, and (iii) audit rates are relatively high at the very top of the income distribution, so if the audits are not thorough enough to correct sophisticated evasion, then high audit coverage rates themselves incentivize the concealment of tax evasion.

A key difficulty in identifying tax evasion by the wealthy is the complexity of the forms of tax evasion at the top, which can involve legal and financial intermediaries, sometimes in countries with a great deal of secrecy. Income flows from assets outside of 3rd party reporting requirements or obscured through multiple layers of ownership make it difficult to associate the income with specific individuals. The study estimated that accounting for offshore and undercounted pass-through evasion alone could identify an additional $110 billion in undetected income which would have resulted in an additional $33 billion oftaxes annually.

The study concludes that effective tax enforcement at the very top of the U.S. income distribution requires a comprehensive approach, including:

- Greater scrutiny of pass-through businesses.
- More comprehensive audits, such as those conducted in the IRS Global High Wealth program.
- More thorough litigation of tax disputes.
- New regulations to clarify that certain activities are noncompliant.
- Programs to encourage whistleblowing.

Investing in IRS Enforcement

Investing in the agency that interacts with more Americans than any other public or private organization *and* touches almost 96% of the gross revenue of the United States of America is important. We must invest in in technology, data and analytics to improve the effectiveness of our existing enforcement workforce and programs, restore base enforcement functions that have declined substantially over the last decade, tackle key compliance priorities and emerging issues, and invest in programs that are essential to maintaining the broad compliance framework even though they may not directly generate revenue.

The Congressional Budget Office (CBO) recently reported that IRS appropriations have fallen by 20 percent in inflation-adjusted dollars since 2010, resulting in the elimination of 22 percent of our staff.[8] Because labor costs account for about 70 percent of the IRS's budget, measures to reduce the IRS workforce were instituted, including a hiring freeze from 2011 - 2018. The amount of funding and staff allocated to enforcement activities has declined by about 30 percent since 2010. In this regard, the CBO determined that experienced Revenue Agents, who handle complex enforcement examinations, fell by 35 percent and Revenue Officers, who manage difficult collection matters, dropped by 48 percent. The disruptions stemming from the 2020 coronavirus pandemic have further reduced the ability of the IRS to enforce tax laws.

The loss of more than 17,000 enforcement employees since FY2010 led to a significant reduction in the number of examinations and the number of follow-ups on discrepancies between returns and third-party data, as well as an increase in assessments that were not collected and unfiled returns that were not secured. Enhancements in IRS technology are clearly helpful in offsetting some portion of the declining enforcement workforce, but we must acknowledge that such enhancements are hard pressed to significantly offset the increased sophistication of taxpayers and their transactions operating in a digital world economy coupled with the overall complexity of tax law.

According to the CBO, the number of examinations since FY2010 dropped by about 40 percent even as the number of returns filed grew by 5 percent. CBO estimates that increasing the IRS's funding for examinations and collections by $20 billion over 10 years would increase revenues by $61 billion and that increasing such funding by $40 billion over 10 years would increase revenues by $103 billion. CBO's estimates only capture the direct effect of enforcement activities. The IRS's enforcement activities also have an indirect, deterrent effect on the Tax Gap by discouraging taxpayers from making misstatements on their returns.

On April 9, 2021, the Biden Administration released its proposal for topline discretionary funding that included an additional increase of $417 million in funding for tax enforcement as part of a multiyear tax initiative that would increase tax compliance and increase revenues. Almost every Presidential budget request going back over the past decade has requested additional, targeted funding to increase enforcement in the high-income/high-wealth and other important areas. If received, these funds would increase enforcement activities while also providing resources for the support costs that make enforcement activities possible and provide a significant return on investment (ROI) for our country.

"[8] Trends in the Internal Revenue Service's Funding and Enforcement," Congressional Budget Office, July 2020, Publication 56467

Much has been written about the return on investment (ROI) for IRS funding generally.[9] The ROI is often computed by dividing the total enforcement revenue collected by the IRS in any given year by the total IRS budget for that year. This method may understate the actual return and fail to measure what the IRS would do with additional enforcement funding that could be targeted at specific areas of identified non-compliance, rather than a general investment into general IRS enforcement operations. However, *any* stated ROI is likely understated because it does not reflect the effect that visible, enhanced enforcement has on deterring non-compliance.

We are currently taking measures to position the IRS to significantly increase staffing, in the event Congress were to appropriate the necessary funding. A $1 billion investment targeted in enforcement could accommodate approximately 4,875 additional front-line enforcement staff plus supporting managers, Appeals Officers, Taxpayer Advocate staff, Office of Chief Counsel staff and staff in Operations Support. This investment would begin to restore the base in field examination and collection, address priorities in large corporate/partnership/pass-thru/and high income/high wealth areas and protect revenue while enhancing deterrence through additional operations involving Criminal Investigations and tax-exempt organizations. This would only be the beginning and is significantly less than the more than 17,000 enforcement employees lost over the last decade.

Almost 20% of the overall IRS workforce is presently eligible to retire and almost 40% are eligible to retire over the next several years. It would be challenging to absorb more than 4,875 front-line enforcement staff in a single year in addition to replacing attrition. Although an incremental approach building to significantly increased enforcement staffing over several years may be more manageable, the IRS *must* presently position itself to be able to quickly and appropriately increase enforcement staffing in the event Congress were to appropriate the necessary funding. Investments in targeted IRS enforcement efforts designed to reduce the Tax Gap are important to every American.

Tax Gap Enforcement Efforts

The IRS uses the Tax Gap data to help it decide where to deploy its resources, both to minimize burden on compliant taxpayers (e.g., we would rather not audit someone who paid fully and timely) and to concentrate on reaching noncompliant taxpayers. Thanks to the help of artificial intelligence, advanced data, and analytic strategies, we have enhanced our capabilities to identify areas of noncompliance in ways that were not remotely possible just a few years ago. With that said, there is room to further modernize these efforts, and the IRS has requested funding to do that. Likewise, the IRS has requested modernization funding that will allow it to make better use of the data we already collect.

“[9] Shrinking the Tax Gap: Approaches and Revenue Potential,” Natasha Sarin and Lawrence H. Summers, Tax Notes, November 18, 2019 (“Extrapolating from the CBO and Treasury data suggest that $1 of investment in the IRS leads to $11 of additional revenue, which suggest that a $1.1 trillion increase in tax collections — shrinking the tax gap by around 15 percent — could be achieved by increasing IRS outlays by $100 billion.”).

Yet, we cannot devote all of our resources to just the deepest pockets of non-compliance. It is important that the IRS have a presence "in every neighborhood" so to speak, for if the IRS were to stop auditing one segment of the population non-compliance in that segment would be more at risk to increase. That is because tax enforcement has both a direct effect on those taxpayers we audit, but also an indirect "deterrence" effect on taxpayers generally. Research has shown that taxpayers are more likely to comply when it appears that there is a recognizable chance they will be caught if they "cheat," and that the consequences for "cheating" will be costly.

We sometimes receive criticism for not deploying sufficient resources to a specific issue or type of taxpayer. Such criticism ignores the importance of maintaining meaningful audit coverage across *all* segments of society, compliance issues, etc. With that coverage requirement in mind, and after considering all the options, including the tax dollars involved, the IRS determines the best *overall* solution for tax administration by devoting our limited enforcement resources across numerous areas with significant perceived non-compliance.

With technological advances, we are now able to identify instances of noncompliance that would not have been possible just a few years ago. Enforcement supports the efforts of compliant taxpayers. To do this, we are exercising our best efforts with limited experienced personnel covering taxpayer compliance from several angles. Since 2018, we have shifted significant examination resources and technology to increase our focus on high-income/high-wealth taxpayers. We have also initiated a Compliance Initiative Project to ensure that we continue to maintain a high rate of audit coverage of taxpayers at the highest income category using examiners across each of our operating divisions. Our examination personnel are conducting audits of high-income/high-wealth taxpayers at an examination rate far higher than any other category of individual filers.

The previously referenced research study entitled "Tax Evasion at the Top of the Income Distribution: Theory and Evidence" produced by IRS researchers and their academic partners strongly supports our efforts to recruit and retain experienced, sophisticated, and specialized examiners to conduct the examinations of the high-income and high-wealth individuals and their related entities. During the past year, we successfully brought onboard many experienced external tax professionals to increase our examination focus on pass-through entities associated with high-income and high-wealth individuals.

Examination Enhancements

Over the past two years, we have shifted significant examination resources and technology to increase our focus on high-income and high-wealth taxpayers and the most egregious matters. When it comes to underreporting, our most highly trained and experienced Revenue Agents with substantial accounting skills are almost entirely focused on tax returns that include complex issues, such as high-income taxpayers, pass-through entities, multi-national taxpayers involving international tax issues, large pension plans and private foundations.

Within our Examination functions, high-income taxpayers can be selected for compliance efforts through many return-selection programs. For example, a high-income taxpayer could be selected through the Discriminate Function (DIF) scoring method; as a related return through a partnership examination; or through a campaign, the Global High Wealth (GHW) program (described below), offshore compliance work, international individual compliance activity, review of foreign tax credits, or corporate officer compliance checks. We also have new compliance programs addressing virtual currencies including crypto collectibles and non-fungible digital assets, including Non-Fungible Tokens (NFTs), often referred to as ERC721 or ERC1155 tokens, that are unique or limited in quantity and are treated similar to vintage baseball cards, rare coins or original works of art. These compliance programs will also address Return Preparer non-filers; Form 8300 (reporting of cash transactions of $10,000 or more) non-filers and others.

A few impactful current enforcement programs include:

- **Global High Wealth and Examinations of High Income/High Wealth Taxpayers.** As noted in a recent Closer Look article[10], high income/high wealth taxpayers, including high-income non-filers (HINF), continue to be a high priority for the IRS. As reported in the IRS's most recently published Data Book (2019), the exam coverage rate (closed and in-process) for Tax Year 2015[11] of taxpayers with incomes of $10 million or more is about 8.16% (down from almost 23% in 2010). The rate for taxpayers with incomes between $5-10 million was 4.39%; for those with income between $1-5 million was about 2.39%; for those with income between $500,000- $1 million was about 1.13%; and for those with income between $200,000-$500,000 was about 0.55%.The IRS receives more third-party information (Forms W-2's, Forms 1099, etc.) for taxpayers with income between $200,000-$1 million than for those above $1 million. Audit rates for the highest income taxpayers are higher than for any other category of individual filers, and we expect to see that trend generally continue as the timeframe expires within which we can conduct and close examinations for tax years following 2015.

  The Global High Wealth (GHW) program was created to take a holistic approach in addressing the high wealth taxpayer population to look at the complete financial picture of high-wealth individuals and the enterprises they control. Its scope includes individual taxpayers (Form 1040) who have income or wealth in the tens of millions of dollars. A GHW enterprise case consists of a key case, generally an individual income tax return, and related income tax returns where the individual has a controlling interest and significant compliance risk is deemed to exist. Controlling interest can include significant ownership of, or significant influence over, an entity

[10] How the IRS Prioritizes Compliance Work on High Income Non-Filers Through National and International Efforts, December 3, 2020.

[11] Tax Year 2015 is the last year for which we know the actual audit rates, because the IRS can still open audits for more recent years, so the date for more recent years is not yet complete.

or multiple entities within the enterprise. The enterprise case may include interests in partnerships, trusts, subchapter S corporations, C corporations, other foreign entities, a relationship with private foundations, large gifts, etc. The cases also typically require involvement of cross-border and financial products experts, engineers, and appraisers to conduct the examination.

- **Office of Fraud Enforcement.** Within the past two years, we launched our Office of Fraud Enforcement (OFE) where technical advisors provide fraud policy and operations support to all IRS operations. Damon Rowe, the Executive Director of the OFE, is a longtime IRS Criminal Investigation (IRS-CI) veteran. OFE has expanded fraud awareness Service-wide by holding "Fraud Bootcamps" (advanced technical training) to more than 12,000 front line examiners, Managers and Chief Counsel personnel during the first quarter of 2021. Compliance examiners have a commitment to general fraud awareness and each Operating Division provides quarterly or more frequent non-taxpayer specific reports to the Commissioner regarding their activities in this area. As an example of their efforts, OFE has a new project "Operation Hidden Treasure" focused on the development of various signatures associated with the hidden ownership of virtual currencies to better enable the IRS to pursue undisclosed taxable transactions. A substantial portion of the OFE caseload involves high-income/high-wealth individuals and their controlled entities.

- **Office of Promoter Investigations.** Within the past year, we have created an Office of Promoter Investigations (OPI) focused on taxpayers and the promoters of abusive tax avoidance transactions, including abusive Syndicated Conservation Easements, abusive Micro-Captive insurance arrangements, virtual currencies, offshore transactions, and other transactions. Substantially all of these transactions are engaged in by high-income/high-wealth individuals. OPI coordinates Service-wide enforcement activities most often interacting with our LB&I division, our SBSE division, our TEGE division, the Office of Chief Counsel, OFE and, when appropriate, Criminal Investigation (IRS-CI).

For these efforts to remain highly impactful going forward, IRS must continue and expand focused examinations and, to do so, we need to onboard many additional experienced, specialized examiners. Further, all examiners must receive the appropriate resources and ongoing training to enable them to perform at the highest levels. Additional resources will allow us to expand the nature and scope of these examinations.

Collection Enhancements

As to underpayment, our Collection operation resolves unpaid balances using the Notice stream, and then conducts enforcement through liens, levies, and seizures. They also help taxpayers identify tools such as installment agreements to keep them in compliance. Revenue officers are the IRS Collection personnel who work the more complex and higher dollar inventory. While their field activities have been somewhat curtailed during the pandemic, they normally contact taxpayers in person at their home or business. Our automated programs, the Automated Underreporter (AUR) and Automated Collection System (ACS), are generally effective in focusing on taxpayers with less complex delinquencies.

Due to attrition, there are some locations where there is an imbalance between available high priority case inventory and the Revenue Officer staffing needed to work it. In FY 2020, we began a “Revenue Officer Compliance Sweep” (ROCS) initiative to address this problem. ROCS typically focus on a geographic area. A team of Revenue Officers spends several days in an area contacting high priority individual and business balance due or delinquent return taxpayers. Cases selected for the ROCS initiative typically involve high-income individual taxpayer cases and business cases where payroll taxes are going unpaid. To increase the impact, we promote our strategy through the national media to address HINF delinquencies and improve future voluntary compliance.

During the pandemic, the ROCS have mostly been conducted virtually, with Revenue Officers contacting taxpayers by telephone. We are continuing to conduct ROCS using appointment letters to initiate contact with taxpayers in 33 different states. We estimate between 2,200 and 2,700 high priority cases will be worked as part of this effort, many of which include high-income/high-wealth individuals as part of the overall high priority taxpayer population. Many of these ROCS will specifically focus on attempting to contact and resolve approximately 600 high-income individual non-filer cases in 20 different states. Additional resources will allow us to expand the nature and scope of these Collection division programs.

“Operation Surround Sound” represents a coordinated effort among our Collection Division, Exam, OFE and, when appropriate, Criminal Investigation to identify and pursue the most egregious High-Income Non-Filers (HINFs) from their sweeps. High-income taxpayers with balances due receive high prioritization for enforcement action. For taxpayers who fail to file a return, we have programs that address their compliance through notices as well as field presence. All High-Income Non-Filers (HINFs) for tax years 2016, 2017 and 2018 received a notice, and we intend to continue selecting all HINF cases for tax years 2019 and beyond.

Criminal Investigation Division

Most investigations conducted by IRS-CI involve high-income individuals and their advisors. Our Nationally Coordinated Investigations Unit (NCIU) supplements case development by identifying, promoting, and supporting innovative investigations, delivering high-impact investigations, and addressing emerging issues to advance the mission of the IRS and IRS-CI. During the past year, IRS-CI has conducted approximately 450 undercover investigations, many focused on high-income individuals and their advisors. If completion of a criminal investigation leads to an indictment by the Department of Justice, the publicity surrounding the indictment often has a deterrent effect helpful to tax administration.

Over the last year, IRS-CI has also been combatting COVID-19 fraud related to the Economic Impact Payments, Paycheck Protection Program (PPP) and Employee Retention Credit. The agency has investigated more than 350 tax and money laundering cases nationwide totaling $440 million. These investigations covered a broad range of criminal activity, including fraudulently obtained loans, credits and payments meant for American workers, families, and small businesses. Additional resources will allow us to expand the nature and scope of these IRS-CI investigations.

Mitigating the Tax Gap Through Legislative and Other Considerations

While tax enforcement is necessary and, from a financial perspective, worthwhile, significant mitigation of the Tax Gap will also require policy and other changes. Proposals for legislative expansions of IRS authority, reduced complexity, increased information reporting, as well as policy changes that improve IRS access to relevant data, have historically included:

- Giving IRS clear statutory authority to regulating return preparers and require they have a minimum knowledge of the tax code, to improve the accuracy of the returns they prepare.
- Expanded electronic filing for individuals, corporations, partnerships, and tax-exempt organizations to provide tax return information in a more uniform electronic form, which will enhance the ability of the IRS to more productively focus its audit activities, lessening audits of compliant taxpayers and overall taxpayer burden.
- Expanding the scope of information returns.[12]
- Requiring early filing and electronic submission of all information returns.
- Requiring withholding on certain Form 1099 income, especially 1099-MISC and 1099-NEC (non-employee compensation).
- Providing IRS with greater flexibility to correct specific errors on taxpayer returns, such as math errors or taxpayer identification numbers, with appropriate safeguards, where information doesn't match information in government databases would also avoid burdensome audits.
- Requiring all payers to obtain and maintain TINs (Form W-9) for all information documents subject to back-up withholding and expand TIN matching.
- Simplifying worker classification rules.
- Making repeated willful failure to file a tax return a felony.

Narrowing the Tax Gap

Investment in the IRS's service, enforcement and compliance efforts is extremely important in reducing the overall Tax Gap. Multi-year, consistent, adequate funding helps us deliver meaningful services to taxpayers, conduct critical enforcement initiatives, and support long-

[12]Shrink the Tax Gap Program - Updated Financial Analysis to Fit a Legislative Timetable, March 14, 2021 ("The primary driver of shrinking the tax gap will be the improved voluntary compliance from enhanced information reporting, supported by modernized technology and enforcement. Approximately 68% of our estimate of the revenue gain is from enhanced voluntary compliance and improved accuracy of filing.") https://shrinkthetaxgap.com/

term IT modernization efforts that help improve compliance. We remain committed to ensuring that the tax system is enforced fairly, taxpayers receive the nature and quality of services they deserve and that no one at any income level feels safe cheating on their taxes.

In addition to the need for the IRS to run a balanced enforcement program, the Tax Gap – and the underlying components – illustrate that the agency also needs to continue focusing on solid, meaningful taxpayer service to help people understand and meet their filing and reporting obligations.

Enforcement alone will not narrow the Tax Gap, and the efforts necessary to raise compliance levels are resource intensive for the IRS and can be intrusive to taxpayers. We know that more withholding and reporting works, which is why we need legislation. But, we recognize that enhanced record keeping and reporting, although necessary, may be perceived by some as an overly burdensome approach to the Tax Gap, and we are committed to working with our partners to carefully balance the need with the burden.

Greater investments in technology can help us properly assist compliant taxpayers, allow us to make better use of the data we already have and that we may receive in the future. Modernization of our systems coupled with technological advances in artificial intelligence, data and analytics will continue to enhance services to compliant taxpayers and make tax avoidance by others more visible and more difficult.

Resource challenges, retirements, implementation of major new federal tax programs and law changes, and the pandemic have placed additional restraints on our resources. However, the entire IRS workforce remains dedicated to delivering a fair and equitable tax system that benefits all Americans. Every IRS employee proudly serves our nation, we want to do more and we are hopeful you will continue to help us help others . . . ONE IRS, ONE COUNTRY.

Best to all,

Chuck