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MEMORANDUM

To: Reporters and Editors
Re: Question for IRS commissioner on the tax gap
Da: Wednesday, Feb. 14, 2007

Sen. Chuck Grassley, ranking member of the Finance Committee and a senior member of the Budget Committee, today asked IRS Commissioner Mark Everson a series of questions to pinpoint the most effective means of closing the tax gap. The exchange came at a Budget Committee hearing on the tax gap, which is the amount of taxes due but uncollected. Some senators and House members cite tax gap collection as a way to pay for Alternative Minimum Tax relief and other priorities. Grassley has worked and continues to work to close the tax gap but also points out that there is no simple solution for closing the tax gap, and the answer is not simply providing more IRS funding. The text of Grassley's questions to Everson follows here. The hearing video is available at <http://budget.senate.gov/republican/NewHearings&Testi.htm>. Grassley will submit the questions he did not have time to ask at the hearing to Everson to answer for the hearing record.

Commissioner Everson, the tax gap is not a new issue. According to the GAO, the voluntary compliance rate has ranged from around 81 percent to 84 percent over the past three decades. In the Finance Committee, we take the tax gap very seriously, because it's not fair to the vast majority of taxpayers that pay their taxes on time. We have had several hearings to examine the size, sources, and solutions to the tax gap, and we have enacted several steps to reduce the tax gap, such as boosting the IRS' whistleblower program and authorizing the private debt collection program. But we need to do more. Dozens of factors contribute to the tax gap and dozens of solutions are needed to close it. I am completely in support of taking appropriate measures to close the tax gap – and I will work aggressively toward enacting legislative changes to help close it -- but it has to be done with care to be effective. There are no easy solutions.

There seems to be a general consensus that potential solutions to the tax gap fall into three categories: (1) Additional and more efficient enforcement by the IRS; (2) additional enforcement tools for the IRS, such as information reporting and withholding; and (3) changes to our tax base that reduce the complexity of our current system, including reforming or eliminating some tax expenditures, as recommended by the Joint Committee on Taxation in a report called "Options to Improve Tax Compliance and Reform Tax Expenditures". I would note that some of the JCT staff's recommendations have been enacted, but there are many other proposals in that report that have not

been enacted, such as repealing the deduction for interest on home equity loans, modifying the social security tax and self-employment tax rules, and moving to a territorial system for foreign business income. Others have suggested even more fundamental reform, like shifting to a consumption tax. Many of these changes, of course, would create winners and losers, making them controversial.

I have six questions for you Mr. Commissioner, and I'd like to ask them all first, then have you answer each of them.

(1) Do you agree that IRS enforcement, information reporting or withholding, and changes to the tax base are the three general categories of tax gap solutions, and how much tax gap reduction do you think is achievable in each of these categories?

(2) On enforcement, of course JCT and CBO don't score revenue from changes in enforcement. But last year, you testified before this committee that the tax gap could be reduced by \$50 billion to \$100 billion without changing the way the Government interacts with taxpayers. The largest portion of the tax gap is under-reporting by small businesses, which would seem to involve high volume and low dollars. So I find it hard to believe that going after the bulk of the tax gap with IRS enforcement would not result in a much more intrusive IRS. Is your \$50 billion to \$100 billion figure on top of the \$55 billion that the IRS includes in its net tax gap estimate of \$290 billion? In other words have you already gotten a lot of the \$50 billion you spoke of last year through direct and indirect enforcement efforts?

(3) How would the IRS have to change its enforcement practices to actually close the tax gap, how much more intrusive would the IRS be in the lives of taxpayers, and what kind of time frame should Congress expect for the resulting revenues to come in to the Treasury?

(4) The President's budget contains proposals that would expand information reporting for credit card transactions, broker transactions, payments to corporations, and cost basis for securities transactions. Some members on the other side of the aisle have criticized these proposals as not going far enough, because they only bring in about 1 percent of the tax gap. So, how could these proposals be strengthened, and what other types of income should be considered for expanded information reporting or withholding?

(5) In your view, what role should tax reform and simplification play in reducing the tax gap?

(6) What role should the private debt collection program play in going after the tax gap?