

## Making the Internal Revenue Service Work

Jonathan Barry Forman  
*University of Oklahoma*

Roberta F. Mann  
*University of Oregon School of Law*

Follow this and additional works at: <https://scholarship.law.ufl.edu/fttr>

---

### Recommended Citation

Forman, Jonathan Barry and Mann, Roberta F. () "Making the Internal Revenue Service Work," *Florida Tax Review*: Vol. 17, Article 11.

Available at: <https://scholarship.law.ufl.edu/fttr/vol17/iss1/11>

This Article is brought to you for free and open access by UF Law Scholarship Repository. It has been accepted for inclusion in Florida Tax Review by an authorized editor of UF Law Scholarship Repository. For more information, please contact [jessicaejoseph@law.ufl.edu](mailto:jessicaejoseph@law.ufl.edu).

# FLORIDA TAX REVIEW

Volume 17

2015

Number 10

## MAKING THE INTERNAL REVENUE SERVICE WORK\*

by

Jonathan Barry Forman\*\* & Roberta F. Mann\*\*\*

### ABSTRACT

*This is an Article about how to redesign the federal tax system so that the Internal Revenue Service (IRS) can administer it more effectively given that Congress is only willing to let the IRS have around 82,000 employees and a \$12 billion budget. As the IRS Oversight Board and the National Taxpayer Advocate have frequently emphasized, the*

---

\* Copyright © 2015, Jonathan Barry Forman & Roberta F. Mann. This Article was presented at the 107th Annual Conference on Taxation of the National Tax Association in Santa Fe, New Mexico, November 15, 2014, and at the 2015 Annual Meeting of the Law and Society Association in Seattle, Washington, May 28, 2015. Thanks to Gerald E. Auten, Joshua Blank, Bryan T. Camp, George W. Connelly, Jr., Danshera Louise Cords, Pete Davis, Janice M. Hedemann, Allen Lerman, Martin J. McMahon, Jr., Alan H. Plumley, Eric A. San Juan, Lon Smith, and Frank Wolpe.

\*\* Alfred P. Murrah Professor of Law, University of Oklahoma; B.A. 1973, Northwestern University; M.A. (Psychology) 1975, University of Iowa; J.D. 1978, University of Michigan; M.A. (Economics) 1983, George Washington University; Professor in Residence at the Internal Revenue Service Office of Chief Counsel, Washington, D.C. for the 2009-2010 academic year; Tax Counsel to the late U.S. Senator Daniel Patrick Moynihan, 1983-1984; Trial Attorney, Civil Trial Section, Northern Region, Tax Division, U.S. Department of Justice, 1979-1983; Judicial Clerk to the Honorable Robert J. Yock, U.S. Court of Claims, Trial Division (now the U.S. Court of Federal Claims), 1978-1979.

\*\*\* Mr. & Mrs. L. L. Stewart Professor of Business Law, University of Oregon School of Law; B.S. (Psychology) 1980, Arizona State University; M.B.A. 1982, Arizona State University; J.D. 1987, Arizona State University; LL.M. 1995, Georgetown University Law Center. From 1987 to 1997, Mann served in various capacities at the National Office of the Internal Revenue Service Office of Chief Counsel. In 1997 and 1998, Mann served on the staff of the Joint Committee of Taxation.

*United States underinvests in the IRS. Underinvesting means that taxpayer services are suffering and that tax enforcement has been significantly weakened.*

*With budget deficits for “as far as the eye can see” and the recent IRS troubles with tax-exempt political organizations, the prospects for increased funding for the IRS are remote. In this Article, we consider a variety of approaches that would make it easier for the IRS to raise and collect revenue, and we offer a number of recommendations for legislative and administrative changes. For example, we recommend simplifying the tax system, enhancing third-party reporting, and streamlining the tax-filing and dispute-resolution procedures.*

*In short, this Article discusses how the tax system should be designed so that it can work with a modestly-funded tax administrator. Part II of this Article provides an overview of the federal tax system, and Part III of this Article provides an overview of tax administration. Part IV of this Article discusses the key problems with current tax administration. Finally, Part V of this Article offers a number of recommendations for change, including some that would require legislation and some that could be achieved administratively.*

#### TABLE OF CONTENTS

<b>I.</b>	<b>INTRODUCTION</b> .....	728
<b>II.</b>	<b>FEDERAL TAXES</b> .....	730
	A. <i>An Overview</i> .....	730
	B. <i>The Income Tax on Individuals</i> .....	731
	C. <i>Social Insurance Taxes</i> .....	734
	1. <i>Social Security and Medicare Taxes</i> .....	734
	2. <i>Unemployment Compensation Taxes</i> .....	735
	D. <i>The Corporate Income Tax</i> .....	735
	E. <i>Estate and Gift Taxes</i> .....	736
	F. <i>Other Taxes and Revenues</i> .....	736
	G. <i>Other Tax Reporting Entities</i> .....	737
<b>III.</b>	<b>TAX ADMINISTRATION</b> .....	737
	A. <i>Government Players</i> .....	737
	1. <i>Congress</i> .....	737
	2. <i>The Executive Branch</i> .....	738
	a. <i>Internal Revenue Service</i> .....	738
	i. <i>Collecting Revenue</i> .....	739
	ii. <i>Administering Tax Expenditures</i> .....	739

	b.	<i>Other Department of Treasury Offices ...</i>	742
	c.	<i>Department of Justice .....</i>	743
	d.	<i>White House and Other Agencies .....</i>	743
	3.	<i>The Courts.....</i>	744
B.		<i>The Current Tax Administration.....</i>	747
	1.	<i>Returns.....</i>	747
	2.	<i>Voluntary Compliance and the Tax Gap .....</i>	748
	3.	<i>Enforcement.....</i>	752
	a.	<i>Math Error.....</i>	752
	b.	<i>Document Matching.....</i>	752
	c.	<i>Examinations .....</i>	753
	d.	<i>Appeals within the IRS.....</i>	754
	e.	<i>Collection Activities.....</i>	755
	f.	<i>Revenue Collected by Enforcement Activities .....</i>	755
	4.	<i>Litigation.....</i>	756
	5.	<i>Guidance and Other Activities.....</i>	757
	6.	<i>A Summary of the IRS Budget and Staffing Levels.....</i>	759
	7.	<i>A Closer Look at the Tax Gap and Compliance ..</i>	761
<b>IV.</b>		<b>KEY PROBLEMS WITH CURRENT TAX ADMINISTRATION .....</b>	<b>763</b>
A.		<i>The Internal Revenue Service is Significantly Underfunded .....</i>	763
B.		<i>The Tax Code is Increasingly Complex .....</i>	772
	1.	<i>Endless Legislation Adds to Complexity.....</i>	772
	2.	<i>The IRS has Increasing Responsibilities.....</i>	774
	a.	<i>An Increasing Number of Tax Expenditures .....</i>	774
	b.	<i>A More Detailed Example: Energy-related Tax Expenditure.....</i>	775
	i.	<i>Incentives for Renewable Energy.....</i>	776
	ii.	<i>Energy Tax Incentives for Consumers.....</i>	779
C.		<i>The Tax Controversy Process is Unnecessarily Complicated.....</i>	779
<b>V.</b>		<b>RECOMMENDATIONS FOR CHANGE.....</b>	<b>781</b>
A.		<i>Changes that would Require Congressional Action .....</i>	782
	1.	<i>Simplify the Tax System .....</i>	782
	a.	<i>Fundamentally Revamp the Tax System .</i>	784
	b.	<i>Modified Revamp: Simplify or Repeal Certain Provisions.....</i>	787
	2.	<i>Improve the Legislative Process .....</i>	789

	a.	<i>A Permanent Loophole Closing Commission</i> .....	789
	b.	<i>Make Congress Write the Details</i> .....	790
	3.	<i>Enhance Third-Party Information Reporting</i> .....	792
	4.	<i>Simplify the Tax Penalty System</i> .....	794
	5.	<i>Increase Transparency to Increase Compliance</i> .	797
	6.	<i>Streamline Dispute Procedures</i> .....	798
	7.	<i>Give the IRS more authority to Regulate Tax Practitioners and Preparers</i> .....	800
	8.	<i>Do Not Expand Private Debt Collection</i> .....	801
B.		<i>Administrative Actions that Could be Taken by Treasury or IRS or Both</i> .....	803
	1.	<i>Issue Simplifying Regulations</i> .....	803
	2.	<i>Move to a Return-free System</i> .....	804
	3.	<i>Improve the IRS's Allocation of Resources</i> .....	806
	a.	<i>Shift Resources from Guidance to Enforcement</i> .....	807
	b.	<i>Shift Audit Sources</i> .....	809
	c.	<i>Expand the Compliance Assurance Process (CAP) Program</i> .....	812
	4.	<i>Expand Alternative Dispute Resolution and the Use of IRS Appeals</i> .....	812
	5.	<i>Change the IRS Mission</i> .....	813
VI.		<b>CONCLUSION</b> .....	815

## I. INTRODUCTION

This Article is about how to redesign the federal tax system so that the IRS can administer it more effectively given that Congress is only willing to let the IRS have around 82,000 employees and a \$12 billion budget.<sup>1</sup> As the IRS Oversight Board and the National Taxpayer Advocate have frequently emphasized, the U.S. underinvests in the IRS. Underinvesting means that

---

1. U.S. DEP'T OF TREASURY, THE BUDGET IN BRIEF FY 2016, at 61 (2015), [http://www.treasury.gov/about/budget-performance/budget-in-brief/Documents/FY\\_2016\\_BiB\\_complete.pdf](http://www.treasury.gov/about/budget-performance/budget-in-brief/Documents/FY_2016_BiB_complete.pdf) (showing for Fiscal Year 2015, an appropriation of \$10.945 billion, a total program operation level budget [including user fees] of \$11.976 billion, and total full-time equivalent employment of 82,203) [hereinafter BUDGET IN BRIEF 2016]. See also Consolidated and Further Continuing Appropriations Act, 2015, Pub. L. No. 113-235, div. E, tit. I, 128 Stat. 2130, 2336-40 (2014); Associated Press, *IRS Head Says Budget Cuts Could Delay Tax Refunds*, N.Y. TIMES, Dec. 18, 2014, <http://www.nytimes.com/aponline/2014/12/18/us/politics/ap-us-irs-delayed-refunds.html>.

taxpayer services are suffering and that tax enforcement has been significantly weakened.<sup>2</sup>

With budget deficits for “as far as the eye can see”<sup>3</sup> and the recent IRS troubles with tax-exempt political organizations,<sup>4</sup> the prospects for increased funding for the IRS are remote. In this Article, we consider a variety of approaches that would make it easier for the IRS to raise and collect revenue, as well as offer a number of recommendations for legislative and administrative changes. For example, we recommend simplifying the tax system, enhancing third-party reporting, and streamlining the tax-filing and dispute-resolution procedures.

In short, this Article discusses how the tax system should be designed so that it can work with a modestly-funded tax administrator.<sup>5</sup> Part II of this Article provides an overview of the federal tax system and Part III of this Article provides an overview of tax administration. Part IV of this Article discusses the key problems with current tax administration. Finally, Part V of this Article offers a number of recommendations for change, including some that would require legislation and some that could be achieved administratively.

---

2. See, e.g., IRS OVERSIGHT BD., FY 2015 IRS BUDGET RECOMMENDATION SPECIAL REPORT 8 (May 2014) [hereinafter FY 2015 IRS BUDGET RECOMMENDATION SPECIAL REPORT]; NAT'L TAXPAYER ADVOCATE, ANNUAL REPORT TO CONGRESS vol. 1, at viii (2014), <http://www.taxpayeradvocate.irs.gov/userfiles/file/2014-Annual-Report/Volume-One.pdf> (“the IRS’s inflation-adjusted budget has declined by about 17 percent between Fiscal Years (FYs) 2010 and 2015”) [hereinafter 2014 ANNUAL REPORT TO CONGRESS]; NAT'L TAXPAYER ADVOCATE, ANNUAL REPORT TO CONGRESS vol. 1, at 20, 21 (2013), <http://www.taxpayeradvocate.irs.gov/userfiles/file/2013FullReport/Volume-1.pdf> [hereinafter 2013 ANNUAL REPORT TO CONGRESS].

3. The quote is generally attributed to David A. Stockman, a budget director under President Ronald Reagan. Helen Dewar, *Budget Called Vital: Stockman Issues Blunt Warning*, WASH. POST, Apr. 19, 1983, at A1. See also CONG. BUDGET OFFICE, THE BUDGET AND ECONOMIC OUTLOOK: 2015 TO 2025, at 2 tbl.1 (2015), <https://www.cbo.gov/sites/default/files/cbofiles/attachments/49892-Outlook2015.pdf> (showing projected budget deficits over the next ten years).

4. See, e.g., Editorial, *The Real Internal Revenue Scandal*, N.Y. TIMES, July 6, 2014, at SR10, <http://www.nytimes.com/2014/07/06/opinion/sunday/the-real-internal-revenue-scandal.html>; S. REP. NO. 114–119 (2015) (The Internal Revenue Service’s Processing of 501(c)(3) and 501(c)(4) Applications for Tax-Exempt Status Submitted by “Political Advocacy” Organizations from 2010–2013).

5. We recognize that impairing the functioning of the tax system may indeed be the goal of some members of Congress, but reconciling the political process is beyond the scope of this article. See *infra* note 241 and accompanying text.

## II. FEDERAL TAXES

### A. An Overview

The federal government raises virtually all of its revenue from individual income taxes, Social Security payroll taxes, corporate income taxes, estate and gift taxes, and excise taxes on selected goods and services.<sup>6</sup> Table 1 shows the various sources of federal revenues since 1940,<sup>7</sup> and Figure 1 shows a fuller picture of the relative portion of federal revenues coming from each source since 1940.<sup>8</sup> What is most striking is that the federal government has increased its reliance on individual income taxes and payroll taxes and decreased its reliance on corporate income taxes, excise taxes, and other sources of revenue.

**Table 1. Federal Revenues by Source, 1940–2015**

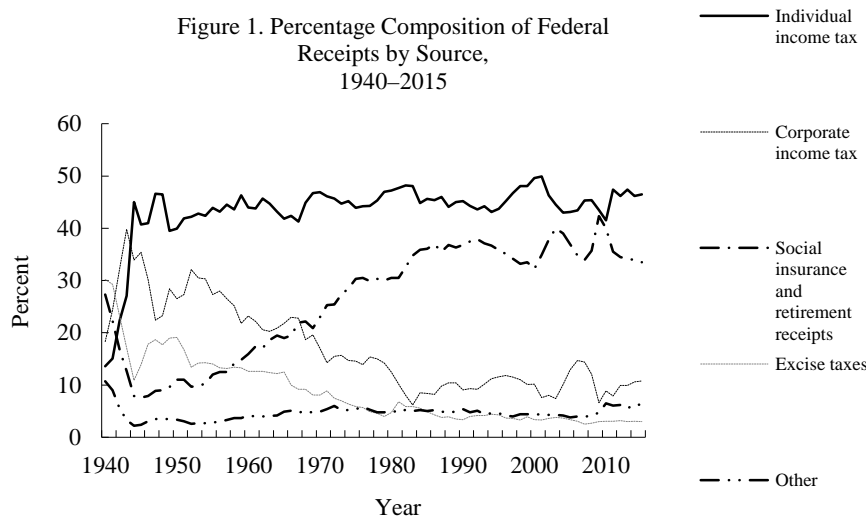
<i>Fiscal year</i>	<i>Individual income taxes</i>	<i>Corporate income taxes</i>	<i>Social insurance and retirement receipts</i>	<i>Excise taxes</i>	<i>Other</i>	<i>Total receipts</i>
<i>in millions of dollars</i>						
1940	892	1,197	1,785	1,977	698	6,548
1960	40,715	21,494	14,683	11,676	3,923	92,492
1980	244,069	64,600	157,803	24,329	26,311	517,112
2000	1,004,462	207,289	652,852	68,865	91,750	2,025,218
2010	895,549	191,437	864,814	66,909	140,997	2,162,706
2015 estimate	1,478,076	341,688	1,065,012	95,898	195,398	3,176,072
<i>percent composition of receipts by source</i>						
1940	13.6	18.3	27.3	30.2	10.7	100.0
1960	44.0	23.2	15.9	12.6	4.2	100.0
1980	47.2	12.5	30.5	4.7	5.1	100.0
2000	49.6	10.2	32.2	3.4	4.5	100.0
2010	41.5	8.9	40.0	3.1	6.5	100.0
2015 estimate	46.5	10.8	33.5	3.0	6.2	100.0

6. See, e.g., STAFF OF THE J. COMM. ON TAX'N, JCX-70-15, OVERVIEW OF THE FEDERAL TAX SYSTEM AS IN EFFECT FOR 2015, at 20 tbl.A-3 (Mar. 30, 2015), [https://www.jct.gov/publications.html?func=download&id=4763&chk=4763&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4763&chk=4763&no_html=1) [hereinafter OVERVIEW OF FED. TAX SYSTEM 2015].

7. OFF. OF MGMT. & BUDGET, HISTORICAL TABLES, tbls.2.1 & 2.2, available at <http://www.whitehouse.gov/omb/budget/historicals> (last visited Aug. 13, 2015) [hereinafter OMB, HISTORICAL TABLES]. See also I.R.S., Pub. No. 55B, DATA BOOK, 2014, at 15–16 tbl.6 (Mar. 2015), [http://www.irs.gov/file\\_source/pub/irs-soi/14databk.pdf](http://www.irs.gov/file_source/pub/irs-soi/14databk.pdf) [hereinafter 2014 IRS DATA BOOK].

8. OMB, HISTORICAL TABLES, *supra* note 7, at tbl.2.2.

Figure 1. Percentage Composition of Federal Receipts by Source, 1940–2015



#### B. *The Income Tax on Individuals*

The largest of the federal taxes is the income tax imposed on individuals. For example, the individual income tax raised more than \$1.6 trillion in Fiscal Year 2014 and 147.4 million individual income tax returns were filed that year.<sup>9</sup>

The federal income tax is imposed on a taxpayer's taxable income.<sup>10</sup> Taxpayers file returns as unmarried individuals, heads of household, married couples filing joint returns, or married couples filing separate returns.<sup>11</sup>

As a starting point, taxpayers first determine the amount of their gross income.<sup>12</sup> Gross income includes all income from whatever source derived, including (but not limited to) the wages, salary, tips, gains, dividends, interest, rents, and royalties received by taxpayers during the taxable year.<sup>13</sup> The U.S. Supreme Court interpreted the term gross income broadly to include all "undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion."<sup>14</sup>

9. *Id.*; I.R.S., *SOI Tax Stats – Tax Stats at a Glance*, <http://www.irs.gov/uac/SOI-Tax-Stats-Tax-Stats-at-a-Glance> (last updated Aug. 11, 2015) [hereinafter *SOI Tax Stats*].

10. I.R.C. §§ 1, 63; OVERVIEW OF FED. TAX SYSTEM 2015, *supra* note 6, at 2.

11. I.R.C. §§ 1, 2, 6012, 6013.

12. I.R.C. § 61.

13. *Id.*

14. *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955).



At the same time, however, there are numerous statutory exclusions from gross income.<sup>15</sup> For example, gifts, inheritances,<sup>16</sup> and life insurance proceeds<sup>17</sup> received by a taxpayer are expressly excluded from gross income, as are certain scholarships,<sup>18</sup> fringe benefits,<sup>19</sup> interest earned on State and local bonds,<sup>20</sup> and most Social Security benefits.<sup>21</sup> Also of note, economic gains are not taxed until the underlying property has been sold and the gain is realized.<sup>22</sup>

From gross income, taxpayers subtract certain deductions to get to taxable income.<sup>23</sup> A majority of taxpayers simply claim a standard deduction and their personal exemptions.<sup>24</sup> Of the almost 145 million individual income tax returns filed for the 2012 tax year, almost 92 million (more than 63 percent) claimed the standard deduction.<sup>25</sup> For the 2015 tax year, the standard deduction amounts are \$12,600 for married couples filing joint returns, \$9,250 for heads of household, \$6,300 for unmarried individuals, and \$6,300 for married individuals filing separate returns.<sup>26</sup> The personal exemption for the 2015 tax year amount is \$4,000.<sup>27</sup>

The remaining individual taxpayers claim certain itemized deductions in lieu of the standard deduction.<sup>28</sup> Also, certain other deductions are allowed without regard to whether the taxpayer chooses to itemize.<sup>29</sup> The tax rate structure is progressive: taxpayers with higher taxable income will pay tax at progressively higher tax rates.<sup>30</sup> Tax rates are imposed by brackets, which vary

---

15. See, e.g., I.R.C. §§ 101 *et seq.*

16. I.R.C. § 102.

17. I.R.C. § 101.

18. I.R.C. § 117.

19. I.R.C. §§ 106, 119, 132.

20. I.R.C. § 103.

21. I.R.C. § 86.

22. I.R.C. § 1001. See, e.g., David M. Schizer, *Realization as Subsidy*, 73 N.Y.U. L. REV. 1549, 1551 (1998).

23. See, e.g., I.R.C. §§ 161 *et seq.*

24. I.R.C. § 63(b).

25. I.R.S., Pub. No. 1304, *Individual Income Tax Returns 2012*, at 2 tbl.A (2014), [http://www.irs.gov/file\\_source/pub/irs-soi/12inalcr.pdf](http://www.irs.gov/file_source/pub/irs-soi/12inalcr.pdf) [hereinafter *Individual Income Tax Returns 2012*]. Authors generated calculation from data in IRS publication (91,780,792 ÷ 144,928,472 = 0.63328). *Id.* at 2 tbl.A, 4 tbl.A.

26. I.R.C. § 63(c); Rev. Proc. 2014–61 § 3.14, 2014–47 I.R.B. 860, 866 (Standard Deduction).

27. I.R.C. § 151(d); Rev. Proc. 2014–61, *supra* note 26, § 3.24 (Personal Exemption).

28. I.R.C. § 63(a), (d), (e).

29. I.R.C. § 62. So called “above the line” deductions may be taken by taxpayers regardless of whether they choose to itemize or not.

30. I.R.C. § 1.

depending on the taxpayer's filing status (married, head of household, or single).<sup>31</sup> In 2015, there are seven ordinary tax brackets: 10, 15, 25, 28, 33, 35, and 39.6 percent.<sup>32</sup> Long-term capital gains and dividend income are generally subject to lower tax rates.<sup>33</sup> The amount that a taxpayer must actually pay (or alternatively will receive as a refund) is equal to the taxpayer's regular tax liability minus her allowable tax credits.<sup>34</sup> For example, certain low-income taxpayers can claim the refundable earned income tax credit.<sup>35</sup> Additionally, many taxpayers with children can claim the partially refundable child tax credit and the nonrefundable dependent care credit.<sup>36</sup>

Some individuals must also pay the alternative minimum tax, which is payable when it exceeds the individual's regular income tax liability.<sup>37</sup> The tax is imposed at rates of 26 and 28 percent on alternative minimum taxable income in excess of an exemption amount.<sup>38</sup> In 2015, the exemption amounts are \$83,400 for married couples filing joint returns, \$53,600 for single individuals and heads of household, and \$41,700 for married individuals filing separate returns.<sup>39</sup>

Even this brief overview of individual income taxation illustrates the complexity faced by most, if not all, taxpayers. To be sure, some of this complexity is mitigated by the use of tax return software and return preparers.<sup>40</sup> In that regard, 55.5 percent of the 147.4 million individual tax returns filed for tax year 2013 were completed by a paid preparer.<sup>41</sup> We will return to a discussion of complexity later in this Article.<sup>42</sup>

---

31. *Id.*

32. *See, e.g.*, Rev. Proc. 2014–61, *supra* note 26, § 3.01.

33. I.R.C. § 1(h). There are four basic capital gains tax rates: 0, 15, 25, and 28 percent, plus a 20 percent rate for high-income taxpayers. *Id.* In addition, there is also a 3.8 percent surcharge on net investment income, which includes capital gains, dividends, and other investment income such as rents. I.R.C. § 1411.

34. I.R.C. §§ 21 *et seq.*

35. I.R.C. § 32.

36. I.R.C. §§ 21, 24.

37. I.R.C. § 55.

38. I.R.C. § 55(b).

39. I.R.C. § 55(d); Rev. Proc. 2014–61, *supra* note 26, § 3.11.

40. *See, e.g.*, NAT'L TAXPAYER ADVOCATE, 2012 ANNUAL REPORT TO CONGRESS vol. 1 at 3, 6 (2012), <http://www.taxpayeradvocate.irs.gov/2012-Annual-Report/downloads/Volume-1.pdf> [hereinafter 2012 ANNUAL REPORT TO CONGRESS].

41. *SOI Tax Stats*, *supra* note 9. *See also* U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-467T, PAID TAX RETURN PREPARERS: IN A LIMITED STUDY, PREPARERS MADE SIGNIFICANT ERRORS 1 (2014), <http://www.gao.gov/assets/670/662356.pdf> [hereinafter U.S. GOV'T ACCOUNTABILITY OFF., PAID TAX RETURN PREPARERS] (noting that paid preparers completed approximately 56 percent of all returns filed for the 2011 tax year).

42. *See infra* Part .IV.B.

C. *Social Insurance Taxes*

1. *Social Security and Medicare Taxes*

Social Security and Medicare taxes are levied on earnings in employment and self-employment covered by Social Security, with portions of the total tax allocated by law to the Old-Age and Survivors Insurance trust fund (OASI), the Disability Insurance trust fund (DI), and the Medicare Hospital Insurance trust fund.<sup>43</sup> For 2015, employees pay Social Security taxes of 7.65 percent on the first \$118,500 of wages and 1.45 percent of wages over \$118,500.<sup>44</sup> The lion's share of these payroll taxes is used to finance the OASI program (5.30 percent of wages), and the rest pay for DI (0.9 percent) and Medicare (1.45 percent).<sup>45</sup> Employers pay a matching Social Security tax of 7.65 percent of up to \$118,500 of wages for each covered employee.<sup>46</sup> Similarly, self-employed workers pay an equivalent Social Security tax of 15.3 percent on the first \$118,500 of self-employment earnings and 2.9 percent of self-employment earnings over that amount.<sup>47</sup>

Individuals are liable for an additional Medicare tax of 0.9 percent if their income exceeds a threshold of \$250,000 for married couples filing jointly, \$125,000 for married couples filing separately, or \$200,000 for single individuals, heads of household, and qualifying widow and widowers with a dependent child.<sup>48</sup>

---

43. I.R.C. §§ 3101–3128, 1401–1403; Soc. Sec. Admin., *Social Security & Medicare Tax Rates*, <http://www.ssa.gov/oact/progdata/taxRates.html> (last visited Aug. 13, 2015) [hereinafter Soc. Sec. Admin., *Social Security & Medicare Tax Rates*]; OVERVIEW OF FED. TAX SYSTEM 2015, *supra* note 6, at 14; H.R. WAYS & MEANS COMM., GREEN BOOK: BACKGROUND MATERIAL AND DATA ON PROGRAMS WITHIN THE JURISDICTION OF THE COMMITTEE ON WAYS AND MEANS ch. 1 (2014), <http://greenbook.waysandmeans.house.gov/2014-green-book> [hereinafter H.R. WAYS & MEANS COMM., GREEN BOOK].

44. See Soc. Sec. Admin., *Fact Sheet: 2015 Social Security Changes*, <http://www.ssa.gov/news/press/factsheets/colafacts2015.pdf> (last visited Aug. 13, 2015) [hereinafter Soc. Sec. Admin., *Fact Sheet: 2015*].

45. Soc. Sec. Admin., *Social Security & Medicare Tax Rates*, *supra* note 43.

46. Soc. Sec. Admin., *Fact Sheet: 2015*, *supra* note 44.

47. *Id.*

48. I.R.C. § 3102(f)(1); I.R.S., *Questions and Answers for the Additional Medicare Tax*, <http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Questions-and-Answers-for-the-Additional-Medicare-Tax> (last updated Mar. 5, 2015).

## 2. Unemployment Compensation Taxes

Unemployment compensation is a joint federal-state program that provides cash benefits to individuals who have recently become unemployed.<sup>49</sup> Benefits are financed through Federal Unemployment Tax Act (FUTA) taxes, a gross tax of 6.2 percent on the first \$7,000 paid annually by covered employers to each employee.<sup>50</sup>

### D. The Corporate Income Tax

The federal government also imposes an income tax on corporations.<sup>51</sup> The taxable income of a corporation generally is its gross income less allowable deductions.<sup>52</sup> Subject to the capitalization rules of sections 263 and 263A, allowable deductions include ordinary and necessary business expenditures such as salaries, wages, interest, depreciation, certain losses, advertising, and selling expenses, and other expenses.<sup>53</sup> Most large corporations pay tax at a 35 percent marginal tax rate.<sup>54</sup> Some corporations are also subject to an alternative minimum tax, which is payable in addition to all other tax liabilities, to the extent that it exceeds the corporation's regular income tax liability.<sup>55</sup> The alternative minimum tax is imposed at a flat rate of 20 percent on alternative minimum taxable income in excess of a \$40,000 exemption amount.<sup>56</sup>

Multinational corporations incorporated in the U.S. face taxation on their worldwide income, mitigated to some extent by the availability of the foreign tax credit and bilateral treaty provisions when applicable.<sup>57</sup>

---

49. I.R.C. § 3301; H.R. WAYS & MEANS COMM., GREEN BOOK, *supra* note 43; JULIE M. WHITTAKER & KATELIN P. ISAACS, CONGRESS. RESEARCH SERV. REP. NO. RL33362, UNEMPLOYMENT INSURANCE: PROGRAMS AND BENEFITS (Feb. 12, 2014), <https://www.fas.org/sgp/crs/misc/RL33362.pdf>.

50. H.R. WAYS & MEANS COMM., GREEN BOOK, *supra* note 43, at ch. 4.

51. I.R.C. § 11; OVERVIEW OF FED. TAX SYSTEM 2015, *supra* note 6, at 9; MARK P. KEIGHTLEY & MOLLY F. SHERLOCK, CONG. RESEARCH SERV. REP. NO. R42726, THE CORPORATE INCOME TAX SYSTEM: OVERVIEW AND OPTIONS FOR REFORM (Dec. 1, 2014), <https://www.hsdl.org/?view&did=760400> [hereinafter KEIGHTLEY & SHERLOCK, THE CORPORATE INCOME TAX SYSTEM].

52. I.R.C. § 63(a).

53. I.R.C. §§ 162, 163, 165, 167.

54. I.R.C. § 11(b)(1)(D) (providing a 35 percent tax rate for taxable income that exceeds \$10 million).

55. I.R.C. § 55.

56. I.R.C. § 55(d)(2).

57. *See, e.g.*, STAFF OF THE J. COMM. ON TAX'N, JCX-90-14, PRESENT LAW AND BACKGROUND RELATED TO PROPOSALS TO REFORM THE TAXATION OF INCOME OF MULTINATIONAL ENTERPRISES (July 21, 2014), [https://www.jct.gov/publications.html?func=download&id=4656&chk=4656&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4656&chk=4656&no_html=1).

Multinational corporations have been the subject of many recent news reports for their ability to avoid U.S. taxation by strategies such as inversions, transfer pricing, and earnings stripping;<sup>58</sup> and the U.S. Department of Treasury (Treasury) has taken some initial steps to curb some of these abusive transactions.<sup>59</sup>

*E. Estate and Gift Taxes*

The federal government also imposes estate and gift taxes on lifetime transfers and transfers at death.<sup>60</sup> In 2015, each taxpayer can give away up to \$5,430,000 of property tax free over her lifetime or at death.<sup>61</sup> Transfers in excess of \$5,430,000 are generally subject to an estate tax or a gift tax of up to 40 percent.<sup>62</sup> Transfers to a spouse are exempt from both taxes, and, for 2015, gifts of up to \$14,000 to others each year are exempt from the gift tax.<sup>63</sup>

*F. Other Taxes and Revenues*

The federal government also collects excise taxes on various consumer products and services such as alcoholic beverages, tobacco products, motor fuels, air transportation, and telephone service;<sup>64</sup> and the

---

58. See, e.g., Kevin Drawbaugh, *Burger King to save millions in U.S. taxes in 'inversion': study*, REUTERS, Dec. 11, 2014, <http://www.reuters.com/article/2014/12/11/us-usa-tax-burgerking-idUSKBN0JPOCI20141211>; David Gelles, *Businesses are Winning Cat-and-Mouse Tax Game*, N.Y. TIMES, Aug. 28, 2014, at B1, <http://dealbook.nytimes.com/2014/08/28/businesses-find-ways-to-avoid-corporate-taxes-but-a-fix-seems-unlikely/>. See generally DONALD J. MARPLES & JANE G. GRAVELLE, CONG. RESEARCH SERV., NO. R43568, CORPORATE EXPATRIATION, INVERSIONS, AND MERGERS: TAX ISSUES (Sept. 25, 2014), <http://www.fas.org/sgp/crs/misc/R43568.pdf> (explaining the corporate inversion strategy).

59. See Notice 2014-52, 2014-42 I.R.B. 712 (describing regulations that the IRS and the Treasury will issue with respect to inversions and related transactions).

60. I.R.C. §§ 2001 *et seq.*, 2501 *et seq.*; OVERVIEW OF FED. TAX SYSTEM 2015, *supra* note 6, at 13.

61. I.R.C. § 2010; Rev. Proc. 2014-61, *supra* note 26, § 3.33 (Unified Credit Against Estate Tax).

62. I.R.C. §§ 2001, 2501-2502.

63. I.R.C. §§ 2056, 2523; Rev. Proc. 2014-61, *supra* note 26, § 3.35 (Annual Exclusion for Gifts).

64. See, e.g., OMB, HISTORICAL TABLES, *supra* note 7, at tbl.2.4; OVERVIEW OF FED. TAX SYSTEM 2015, *supra* note 6, at 15; STAFF OF THE J. COMM. ON TAX'N, JCX-99-15, PRESENT LAW AND BACKGROUND INFORMATION ON FEDERAL EXCISE TAXES (July 13, 2015), [https://www.jct.gov/publications.html?func=download&id=4798&chk=4798&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4798&chk=4798&no_html=1) [hereinafter PRESENT LAW AND BACKGROUND INFORMATION ON FEDERAL EXCISE TAXES].

federal government also collects customs duties.<sup>65</sup>

### G. *Other Tax Reporting Entities*

In addition to the many taxpayers already described, the IRS also receives tax returns and provides guidance to numerous entities that are not subject to tax. In the business area, for example, partnerships file more than three million returns each year,<sup>66</sup> and S corporations file more than four million returns a year.<sup>67</sup> Nonprofit organizations, such as section 501(c)(3) charities, also file more than 360,000 returns each year.<sup>68</sup> Pension plans also file around 680,000 returns a year.<sup>69</sup>

## III. TAX ADMINISTRATION

### A. *Government Players*

Our tax laws are enacted by Congress and administered by the IRS with the assistance of many other agencies and entities.

#### 1. *Congress*

Tax legislation is typically crafted in the House Ways and Means Committee<sup>70</sup> and the Senate Finance Committee<sup>71</sup> with the assistance of the

---

65. See, e.g., OMB, HISTORICAL TABLES, *supra* note 7, at tbl.2.5.

66. See, e.g., I.R.S., *Partnership Returns, 2012*, [http://www.irs.gov/file\\_source/pub/irs-soi/12PartnershipsOneSheet.pdf](http://www.irs.gov/file_source/pub/irs-soi/12PartnershipsOneSheet.pdf) (more than 3.3 million information returns for 2012); *SOI Tax Stats*, *supra* note 9 (3,460,699 partnership returns for Tax Year 2013).

67. See, e.g., I.R.S., *Table 1--S Corporations: Total Receipts and Deductions, Portfolio Income, Rental Income, and Total Net Income, by Major Industry Tax Year 2012*, [http://www.irs.gov/file\\_source/pub/irs-soi/12co01s.xls](http://www.irs.gov/file_source/pub/irs-soi/12co01s.xls) (4,205,452 S corporation returns for Tax Year 2012); *SOI Tax Stats*, *supra* note 9 (4,205,452 S corporation returns for Tax Year 2012).

68. See, e.g., *SOI Tax Stats*, *supra* note 9 (367,277 nonprofit organization returns for Tax Year 2011).

69. For example, there were 676,622 private pension plans filing Forms 5500 (Annual Return/Report of Employee Benefit Plan) in 2012. U.S. DEP'T OF LABOR, EMP. BENEFITS SEC. ADMIN., PRIVATE PENSION PLAN BULLETIN 3 tbl.A1 (2015), <http://www.dol.gov/ebsa/pdf/2012pensionplanbulletin.pdf> [hereinafter DOL, PRIVATE PENSION PLAN BULLETIN].

70. U.S. H.R. Comm. on Ways & Means, *About*, <http://waysandmeans.house.gov/about/> (last visited Aug. 13, 2015).

71. U.S. S. Finance Comm., *Jurisdiction*, <http://www.finance.senate.gov/about/jurisdiction> (last visited Aug. 13, 2015).

Joint Committee on Taxation.<sup>72</sup> Legislative branch organizations like the Congressional Budget Office,<sup>73</sup> the U.S. Government Accountability Office (GAO),<sup>74</sup> and the Congressional Research Service also devote significant resources to tax law and policy.<sup>75</sup>

## 2. *The Executive Branch*

### a. *Internal Revenue Service*

The IRS is the bureau in the Treasury that administers and enforces the nation's internal revenue laws.<sup>76</sup> Within the IRS, the Chief Counsel of the Internal Revenue Service provides legal guidance and interpretive advice to the IRS, the Treasury, and taxpayers.<sup>77</sup> The Taxpayer Advocate Service is an independent organization within the IRS that helps taxpayers resolve problems with the IRS and recommends changes that will prevent those problems.<sup>78</sup> The IRS Oversight Board is an independent board that is supposed to oversee the IRS.<sup>79</sup> However as we go to press, "[t]he IRS Oversight Board does not currently have enough members confirmed by the U.S. Senate to make up a

---

72. J. Comm. on Tax'n, *About Us*, <https://www.jct.gov/about-us/overview.html> (last visited Aug. 13, 2015).

73. Cong. Budget Off., *Overview*, <http://www.cbo.gov/about/overview> (last visited Aug. 13, 2015).

74. U.S. Gov't Accountability Off., *About GAO*, <http://www.gao.gov/about/index.html> (last visited Aug. 13, 2015).

75. Library of Congress, Cong. Research Serv., *About CRS*, <http://www.loc.gov/crsinfo/about/> (last visited Aug. 13, 2015).

76. I.R.S., *About IRS*, <http://www.irs.gov/uac/About-IRS> (last visited Aug. 13, 2015).

77. I.R.C. § 7803(b) (describing duties for Chief Counsel for the IRS); I.R.S., *Office of Chief Counsel At-a-Glance*, <http://www.irs.gov/uac/Office-of-Chief-Counsel-At-a-Glance> (last updated Feb. 19, 2015); I.R.S., *A Great Place to Start and a Great Place to Build Your Career 2* (2011), [http://jobs.irs.gov/downloads/CC-Brochure411\\_2011\\_Rev.pdf](http://jobs.irs.gov/downloads/CC-Brochure411_2011_Rev.pdf). See also 2014 IRS DATA BOOK, *supra* note 7, at 69 tbl.30 (showing that the IRS had 1,454 attorneys at the end of Fiscal Year 2014, down from 1,523 attorneys at the end of Fiscal Year 2013); Marie Sapirie, *Stack Addresses IRS Budget Cuts, FATCA, and BEPS*, 146 TAX NOTES 317 (2015). See Roberta Mann, *Chief Counsel's Subtle Impact on Revenue: Regulations, Litigation, and Administrative Guidance*, 65 NAT'L TAX J. 889 (2012) [hereinafter Mann, *Chief Counsel's Subtle Impact on Revenue*] (more discussion on the role of Chief Counsel).

78. I.R.C. § 7803(c) (describing the duties of the Office of the Taxpayer Advocate); I.R.S., *Taxpayer Advocate Service*, <http://www.irs.gov/Advocate> (last updated Aug. 6, 2015); Taxpayer Advocate Serv., *About the Taxpayer Advocate Service (TAS)*, <http://www.taxpayeradvocate.irs.gov/About-TAS> (last visited Sept. 8, 2015).

79. I.R.C. § 7802; IRS Oversight Bd., *About Us*, <http://www.treasury.gov/IRSOB/about/Pages/default.aspx> (last visited Jan. 15, 2015).

quorum and as a result has suspended operations.”<sup>80</sup> In Fiscal Year 2015, the IRS has 82,203 full-time equivalent employees and an \$11.976 billion total program operating level budget.<sup>81</sup>

*i. Collecting Revenue*

For the most part, the job of the IRS is to collect almost all of the revenue that funds the federal government through the income, social insurance, estate & gift, excise, and other taxes already described in Part II. The organizational structure of the IRS has changed over time. At the 1913 inception of the Federal income tax, the Bureau of Internal Revenue was geographically organized by districts across the country.<sup>82</sup> In 1952, the first major reorganization of the IRS centralized most functions around the National Office.<sup>83</sup> In 1998, the current restructuring abolished the geographic districts: they were superseded by four operating divisions, now known as Wage & Investment, Large Business & International, Small Business/Self-Employed, and Tax-Exempt & Government Entities.<sup>84</sup> During Fiscal Year 2014, the IRS processed more than 199 million tax returns, and in the process, it collected more than \$3.1 trillion in revenue.<sup>85</sup>

*ii. Administering Tax Expenditures*

Congress also uses federal tax laws to shape economic and social welfare policy. Indeed, it has gotten to the point where the IRS has a dual mission: it must both promote tax compliance and it must administer a wide variety of economic and social welfare programs.<sup>86</sup>

---

80. IRS, Oversight Bd., <http://www.treasury.gov/irsob/Pages/default.aspx> (last visited Aug. 13, 2015).

81. BUDGET IN BRIEF 2016, *supra* note 1, at 61.

82. See, e.g., Joseph J. Thorndike, *Reforming the Internal Revenue Service: A Comparative History*, 53 ADMIN. L. REV. 717, 741 (2001).

83. *Id.* at 761–63; I.R.M. 1.1.2 (removed on June 2, 2015, updated I.R.M.).

84. I.R.M. 1.1.2, *supra* note 83; H.R. CONF. REP. 105–599, at 193–94 (1998), 1998 U.S.C.C.A.N. 288; I.R.S., *At-a-Glance: IRS Divisions and Principal Offices*, <http://www.irs.gov/uac/At-a-Glance:-IRS-Divisions-and-Principal-Offices> (last updated Mar. 27, 2015).

85. BUDGET IN BRIEF 2016, *supra* note 1, at 61; 2014 IRS DATA BOOK, *supra* note 7, at iii, 1.

86. See, e.g., Jeremiah Coder, *The New IRS: Expanding the Mission?*, 128 TAX NOTES 576 (2010) [hereinafter Coder, *The New IRS*]; NAT'L TAXPAYER ADVOCATE, 2010 ANNUAL REPORT TO CONGRESS vol. 1, at xii (2010), [http://www.irs.gov/pub/tas/execsummary\\_2010arc.pdf](http://www.irs.gov/pub/tas/execsummary_2010arc.pdf) [hereinafter 2010 ANNUAL REPORT TO CONGRESS].



In particular, the individual and corporate income taxes are replete with so-called tax expenditures.<sup>87</sup> For example, the Code uses accelerated depreciation and even expensing to encourage investments in certain machinery and other tangible property,<sup>88</sup> and the Code offers reduced tax rates for investments that result in capital gains or dividends.<sup>89</sup>

The IRS also administers some of the nation's largest welfare programs through the earned income and child tax credits.<sup>90</sup> Similarly, the IRS

---

87. The Congressional Budget and Impoundment Act of 1974 defines "tax expenditures" as:

those revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provide a special credit, a preferential rate of tax, or a deferral of tax liability . . .

Congressional Budget and Impoundment Act of 1974, Pub. L. No. 93-344, § 3(c), 88 Stat. 297, 299 (1974). *See, e.g.*, EXEC. OFF. OF THE PRES. AND OFF. OF MGMT. & BUDGET, ANALYTICAL PERSPECTIVES, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 2016 at 219 (2015), <http://www.whitehouse.gov/sites/default/files/omb/budget/fy2016/assets/spec.pdf> [hereinafter ANALYTICAL PERS., U.S. BUDGET 2016]; STAFF OF THE J. COMM. ON TAX'N, JCX-97-14, ESTIMATES OF FEDERAL TAX EXPENDITURES FOR FISCAL YEARS 2014-2018 (2014), <https://www.jct.gov/publications.html?func=startdown&id=4663>; U.S. GOV'T ACCOUNTABILITY OFF., GAO-13-167SP, TAX EXPENDITURES: BACKGROUND AND EVALUATION CRITERIA AND QUESTIONS (2013), <http://www.gao.gov/products/GAO-13-167SP>. *See also* Sen. Tom Coburn, TAX DECODER i (Dec. 2014) (discussing more than 165 tax expenditures costing over \$900 billion in Fiscal Year 2015 and more than \$5 trillion over the next five years).

88. I.R.C. §§ 168, 179. *See also* Cong. Budget Off., *Information on the Depreciation of Assets* (2013), <https://www.cbo.gov/sites/default/files/113th-congress-2013-2014/reports/44911-BaucusLetter%2011-21.pdf>; STAFF OF THE J. COMM. ON TAX'N, JCX-19-12, BACKGROUND AND PRESENT LAW RELATING TO COST RECOVERY AND DOMESTIC PRODUCTION ACTIVITIES (Feb. 27, 2012), [https://www.jct.gov/publications.html?func=download&id=4401&chk=4401&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4401&chk=4401&no_html=1).

89. I.R.C. § 1(h). *See also* CONG. BUDGET OFF., TAXING CAPITAL INCOME: EFFECTIVE MARGINAL TAX RATES UNDER 2014 LAW AND SELECTED POLICY OPTIONS (2014), [https://www.cbo.gov/sites/default/files/cbofiles/attachments/49817-Taxing\\_Capital\\_Income\\_0.pdf](https://www.cbo.gov/sites/default/files/cbofiles/attachments/49817-Taxing_Capital_Income_0.pdf); STAFF OF THE J. COMM. ON TAX'N, JCX-72-12, PRESENT LAW AND BACKGROUND INFORMATION RELATED TO THE TAXATION OF CAPITAL GAINS (Sept. 14, 2012), [https://www.jct.gov/publications.html?func=download&id=4485&chk=4485&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4485&chk=4485&no_html=1).

90. I.R.C. §§ 24, 32; URBAN-BROOKINGS TAX POL. CTR., *Tax Facts: Spending on the EITC, Child Tax Credit, and AFDC/TANF, 1975 - 2011*, <http://www.taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=266> (last visited Aug. 13, 2015); Jonathan P. Schneller, Adam S. Chilton & Joshua L. Boehm, *The*

administers numerous tax breaks for education, including the exclusion for certain scholarships, the deduction for student loan interest, and various education tax credits.<sup>91</sup> In addition, the IRS administers a wide variety of tax expenditures for energy.<sup>92</sup> More recently, with the enactment of the Patient Protection and Affordable Care Act (ACA),<sup>93</sup> the IRS acquired the responsibility of administering health insurance premium tax credits for individuals and a variety of other health care provisions.<sup>94</sup>

Table 2 shows the Office of Management and Budget's 2016 *Federal Budget* estimates of the revenue losses attributable to the 20 largest income tax benefits.<sup>95</sup> Since at least 2010, the sum of the estimated revenue loss due to tax expenditures has exceeded \$1 trillion a year.<sup>96</sup>

---

*Earned Income Tax Credit, Low-Income Workers, and the Legal Aid Community*, 3 COLUM. J. OF TAX L. 176, 176 (2012).

91. I.R.C. §§ 25A, 117, 221. See also STAFF OF THE J. COMM. ON TAX'N, JCX-7-14, BACKGROUND AND PRESENT LAW RELATING TO TAX BENEFITS FOR EDUCATION (June 20, 2014), [https://www.jct.gov/publications.html?func=download&id=4621&chk=4621&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4621&chk=4621&no_html=1); U.S. DEP'T OF TREASURY, REPORT TO CONGRESS ON COORDINATING THE AMERICAN OPPORTUNITY TAX CREDIT AND THE FEDERAL PELL GRANT (May 5, 2014), <http://www.treasury.gov/resource-center/tax-policy/Documents/Report-Coordinating-AOTC-Federal-Pell-Grant-5-5-2014.pdf>; U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2015-40-027, BILLIONS OF DOLLARS IN POTENTIALLY ERRONEOUS EDUCATION CREDITS CONTINUE TO BE CLAIMED FOR INELIGIBLE STUDENTS AND INSTITUTIONS (Mar. 25, 2015), <http://www.treasury.gov/tigta/auditreports/2015reports/201540027fr.pdf>.

92. See generally STAFF OF THE J. COMM. ON TAX'N, JCX-100-14, PRESENT LAW AND ANALYSIS OF ENERGY-RELATED TAX EXPENDITURES (Sept. 17, 2014), [https://www.jct.gov/publications.html?func=download&id=4667&chk=4667&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4667&chk=4667&no_html=1) [hereinafter PRESENT LAW AND ANALYSIS OF ENERGY-RELATED TAX EXPENDITURES]. See also *infra* Part IV.B.2.b.

93. Pub. L. No. 111-148, 124 Stat. 119 (2010).

94. See, e.g., I.R.C. § 36B; I.R.S., *Affordable Care Act Tax Provisions*, <http://www.irs.gov/uac/Affordable-Care-Act-Tax-Provisions> (last updated Sept. 1, 2015); I.R.S., *The Premium Tax Credit*, <http://www.irs.gov/Affordable-Care-Act/Individuals-and-Families/The-Premium-Tax-Credit> (last visited Aug. 13, 2015); Matthew R. Madera, *Information Reporting Under ACA Remains a Daunting Task*, 148 TAX NOTES 622 (August 10, 2015). The Supreme Court recently upheld the validity of the tax credits available to taxpayers purchasing health insurance on federally created insurance exchange markets. *King v. Burwell*, 135 S. Ct. 2480 (2015), *aff'g*, 759 F.3d 358 (4th Cir. 2014), and *rev'g*, *Halbig v. Burwell*, 758 F.3d 390 (D.C. Cir. 2014).

95. ANALYTICAL PERS., U.S. BUDGET 2016, *supra* note 87, at 216 tbl.14-3.

96. See, e.g., U.S. GOV'T ACCOUNTABILITY OFF., GAO-11-747T, TAX GAP: COMPLEXITY AND TAXPAYER COMPLIANCE (STATEMENT OF MICHAEL BROSTEK) 5 (2011), <http://www.gao.gov/assets/130/126530.pdf> [hereinafter TAX GAP: COMPLEXITY AND TAXPAYER COMPLIANCE]. While such totals of tax expenditures are useful for illustrative purposes, those totals need to be "interpreted carefully" since tax

**Table 2. The 20 Largest Income Tax Expenditures Ranked by Total Fiscal Year 2015–2024 Projected Revenue Effect (millions of dollars)**

<i>Provision</i>	<i>2015</i>	<i>2015-24</i>
Exclusion of employer contributions for health insurance and health care	206,430	2,673,780
Mortgage interest expense on owner-occupied homes	69,480	1,068,910
Capital gains (except agriculture, timber, iron ore, and coal)	85,360	1,047,140
Exclusion of net imputed rental income	78,810	956,320
Defined contribution employer plans	68,040	917,390
Deferral of income from controlled foreign corporations	64,560	811,980
Step-up basis of capital gains at death	63,440	801,340
Deductibility of nonbusiness State and local taxes other than on owner-occupied homes	47,490	660,280
Defined benefit employer plans	44,640	621,050
Deductibility of charitable contributions, other than education and health	44,280	606,750
Capital gains exclusion on home sales	36,930	513,160
Exclusion of interest on public purpose State and local bonds	31,070	485,110
Deduction for property taxes on real property	33,120	454,110
Exclusion of interest on life insurance savings	13,100	317,420
Self-Employed plans	25,480	395,950
Social Security benefits for retired workers	27,080	324,860
Treatment of qualified dividends	26,320	312,390
Accelerated depreciation of machinery and equipment	-12,260	306,810
Child credit	23,900	236,380
Individual Retirement Accounts	17,240	219,750

*b. Other U.S. Department of Treasury Offices*

Also within the Treasury, the Assistant Secretary (Tax Policy) is the senior advisor to the Secretary of the Treasury for analyzing, developing, and implementing federal tax policies and programs.<sup>97</sup> The Treasury Inspector General for Tax Administration (TIGTA) audits and inspects the IRS.<sup>98</sup>

---

expenditures are estimated one at a time, while holding the remaining tax system constant. *Id.* at 5 n.8. Thus, for example, the total of the tax expenditures in any given year does not necessarily reflect the amount of revenue that would be raised by repealing them all. *See also* Alan Cole, *Corporate and Individual Tax Expenditures*, TAX FOUNDATION (2015), <http://taxfoundation.org/article/corporate-and-individual-tax-expenditures> (finding \$1.339 trillion of tax expenditures in 2015).

97. U.S. DEP'T OF TREASURY, *About (Tax Policy)*, <http://www.treasury.gov/about/organizational-structure/offices/Pages/Tax-Policy.aspx> (last updated Apr. 16, 2014).

98. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., *About TIGTA*, <http://www.treasury.gov/tigta/about.shtml> (last updated Apr. 10, 2015).

c. *Department of Justice*

The U.S. Department of Justice, Tax Division, represents the U.S. in virtually all tax litigation in all federal courts other than the U.S. Tax Court.<sup>99</sup> The Tax Division has around 350 attorneys.<sup>100</sup> The civil sections of the Tax Division handle around 6,600 civil cases annually, and alone or in conjunction with Assistant United States Attorneys, the Tax Division handles between 1,300 and 1,800 criminal tax investigations annually.<sup>101</sup> The Tax Division estimates that its trial attorneys return \$12 to the Treasury for each dollar invested.<sup>102</sup> Finally, the U.S. Department of Justice's Office of the Solicitor General represents the United States in tax cases before the U.S. Supreme Court.<sup>103</sup>

d. *White House and Other Agencies*

The President of the U.S. often makes tax policy recommendations to the U.S. Department of Treasury and to Congress.<sup>104</sup> The Office of

---

99. U.S. DEP'T OF JUSTICE TAX DIV., FY 2016 OMB BUDGET 1 (2015), [http://www.justice.gov/sites/default/files/jmd/pages/attachments/2015/02/01/9.\\_tax\\_division\\_tax.pdf](http://www.justice.gov/sites/default/files/jmd/pages/attachments/2015/02/01/9._tax_division_tax.pdf) [hereinafter DOJ OMB BUDGET FY 2016]; see also U.S. DEP'T OF JUSTICE, *Tax Division Home*, <http://www.justice.gov/tax/>. For many years, some I.R.S. Chief Counsel attorneys were designated as Special U.S. Attorneys so that they could represent the IRS in bankruptcy proceedings in federal courts. I.R.M. 34.11.1.1, [http://www.irs.gov/irm/part34/irm\\_34-011-001.html](http://www.irs.gov/irm/part34/irm_34-011-001.html). Due to budget limitations, the IRS Office of Chief Counsel recently terminated that program. Keith Fogg, *End of SAUSA Program at Chief Counsel's Office*, PROCEDURALLY TAXING (June 3, 2015), <http://www.procedurallytaxing.com/end-of-sausa-program-at-chief-counsels-office/>.

100. U.S. DEP'T OF JUSTICE, *About the Division*, <http://www.justice.gov/tax/about-division> (last updated Apr. 15, 2015) [hereinafter U.S. DEP'T OF JUSTICE, *About the Tax Division*].

101. DOJ OMB BUDGET FY 2016, *supra* note 99, at 1.

102. *Id.*

103. U.S. Dep't of Justice, *Office of the Solicitor General*, <http://www.justice.gov/osg/> (last visited Aug. 13, 2015). See generally JASPER L. CUMMINGS JR., *THE SUPREME COURT, FEDERAL TAXATION, AND THE CONSTITUTION* (2013). In an empirical study of the Supreme Court's *certiorari* procedures, the researchers found that the Court follows the Solicitor General's recommendation on whether to grant *certiorari* in a majority of cases. David C. Thompson & Melanie F. Wachtell, *An Empirical Analysis of Supreme Court Certiorari Petition Procedures: The Call for Response and the Call for the Views of the Solicitor General*, 16 GEO. MASON L. REV. 237, 275 (2009).

104. See The White House, *Taxes*, <http://www.whitehouse.gov/issues/taxes> (last visited Aug. 13, 2015).

Management and Budget<sup>105</sup> and Council of Economic Advisors<sup>106</sup> often offer important assistance in the formulation of the President's tax and related budget recommendations. In recent years, the National Economic Council has served as a major tax policy player within the Executive Office of the President.<sup>107</sup> Other Executive Branch agencies may also play minor roles in the tax world.<sup>108</sup>

### 3. *The Courts*

Disputes between taxpayers and the U.S. government are ultimately resolved by the federal judicial system.<sup>109</sup> Many tax cases start after a taxpayer receives a notice from the IRS stating that there is a deficiency owed by the taxpayer.<sup>110</sup> The taxpayer can challenge that notice of deficiency by filing a

---

105. The White House, *Office of Management and Budget*, <http://www.whitehouse.gov/omb> (last visited Aug. 13, 2015).

106. The White House, *Council of Economic Advisors*, <http://www.whitehouse.gov/administration/eop/cea/> (last visited Aug. 13, 2015).

107. Nat'l Econ. Council, *Overview*, <http://www.whitehouse.gov/administration/eop/nec> (last visited Aug. 13, 2015).

108. For example, the U.S. Department of State is actively involved in international tax issues, treaties, and tax information exchange agreements. *See, e.g.,* U.S. Dep't of Treasury, *Resource Center: Treaties and Other International Documents*, <http://www.treasury.gov/resource-center/tax-policy/treaties/Pages/default.aspx>; STAFF OF THE J. COMM. ON TAX'N, JCS-17-79, TAX TREATIES: STEPS IN THE NEGOTIATION AND RATIFICATION OF TAX TREATIES AND STATUS OF PROPOSED TREATIES (May 21, 1979), [https://www.jct.gov/publications.html?func=download&id=3887&chk=3887&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=3887&chk=3887&no_html=1). Many other agencies also care about tax administration and tax policy. *See, e.g.,* U.S. Small Bus. Admin., *Filing & Paying Taxes*, <http://www.sba.gov/category/navigation-structure/starting-managing-business/starting-business/establishing-business/taxes> (last visited Aug. 13, 2015); JOHN O'HARE, MARY SCHMITT & JUDY XANTHOPOULOS, SMALL BUS. ADMIN. OFF. OF ADVOCACY, MEASURING THE BENEFIT OF FEDERAL TAX EXPENDITURES USED BY SMALL BUSINESS (Nov. 2013), <http://www.sba.gov/sites/default/files/rs415tot.pdf> (report developed under Contract No. SBAHQ-12-Q-0043 with Quantria Strategies); U.S. DEP'T OF HOUSING AND URBAN DEV., *Low Income Housing Tax Credit*, [http://portal.hud.gov/hudportal/HUD?src=/program\\_offices/fair\\_housing\\_equal\\_opp/lihtcmou](http://portal.hud.gov/hudportal/HUD?src=/program_offices/fair_housing_equal_opp/lihtcmou) (last visited Aug. 13, 2015) (explaining how low income housing tax credits work); Amy Burke, Arpit Misra & Steven Sheingold, U.S. DEP'T OF HEALTH & HUMAN SERV., OFF. OF THE ASSISTANT SEC'Y FOR PLANNING & EVALUATION, RESEARCH BRIEF, PREMIUM AFFORDABILITY, COMPETITION, AND CHOICE IN THE HEALTH INSURANCE MARKETPLACE, 2014 (June 18, 2014), <http://aspe.hhs.gov/health/reports/2014/premiums/2014mktplaceprembf.pdf> (examining the impact of health care premium tax credits on consumer costs).

109. *See generally* Admin. Off. of the U.S. Courts, *About Federal Courts*, <http://www.uscourts.gov/about-federal-courts> (last visited Aug. 13, 2015).

110. I.R.C. § 6212.

petition with the U.S. Tax Court without having first paid the tax.<sup>111</sup> Other cases start when a taxpayer pays the tax and then sues for a refund either in the U.S. District Court or in the U.S. Court of Federal Claims.<sup>112</sup> The U.S. Department of Justice also initiates many tax collection lawsuits in the U.S. District Courts.<sup>113</sup> Tax issues can also arise in the U.S. Bankruptcy Courts.<sup>114</sup>

The U.S. Tax Court was established by Congress under Article I of the U.S. Constitution.<sup>115</sup> The Court has 19 presidentially appointed judges who serve for a term of 15 years.<sup>116</sup> Jury trials are not available in the U.S. Tax Court.<sup>117</sup> Appeals generally go to the U.S. Court of Appeals where the taxpayer is located,<sup>118</sup> and then on to the U.S. Supreme Court if it grants *certiorari*.<sup>119</sup>

The U.S. District Courts are trial courts established by Congress under Article III of the U.S. Constitution.<sup>120</sup> District court judges are presidentially appointed and have lifetime tenure.<sup>121</sup> Jury trials are available.<sup>122</sup> There are 94 U.S. District Courts around the country,<sup>123</sup> and appeals go to 12 regional U.S.

---

111. I.R.C. § 6213; Leandra Lederman, “Civil”izing Tax Procedure: Applying General Federal Learning to Statutory Notices of Deficiency, 30 U.C. DAVIS L. REV. 183, 183 (1996).

112. I.R.C. § 7422; 28 U.S.C. §§ 1346, 1491 (2012).

113. E.g., I.R.C. §§ 7401–7410; U.S. Dep’t of Justice, *About the Tax Division*, *supra* note 100.

114. Admin. Off. of the U.S. Courts, *Court Role and Structure*, <http://www.uscourts.gov/about-federal-courts/court-role-and-structure> (last visited Aug. 13, 2015) [hereinafter Admin. Off. of the U.S. Courts, *Court Role and Structure*]. While historically these cases were often handled by IRS attorneys, they are now handled by Justice Department attorneys. *See supra* note 99.

115. I.R.C. § 7441; U.S. Tax Court, *About the Court*, <https://www.ustaxcourt.gov/about.htm> (last updated May 25, 2011) [hereinafter U.S. Tax Court, *About the Court*].

116. U.S. TAX COURT, *About the Court*, *supra* note 115.

117. *Id.*

118. *See, e.g.*, I.R.M. 36.2.5.8, [http://www.irs.gov/irm/part36/irm\\_36-002-005.html#d0e41](http://www.irs.gov/irm/part36/irm_36-002-005.html#d0e41); *Golsen v. Commissioner of Internal Revenue*, 54 T.C. 742 (1970), *aff’d on other grounds*, 445 F.2d 985 (10th Cir. 1971), *cert. denied*, 404 U.S. 940 (1971).

119. 28 U.S.C. § 1254 (2012); I.R.M. 36.2.2.1, [http://www.irs.gov/irm/part36/irm\\_36-002-002.html](http://www.irs.gov/irm/part36/irm_36-002-002.html).

120. *See* 28 U.S.C. § 1340 (2012); Fed. Judicial Ctr., *How the Federal Courts are Organized*, <http://www.fjc.gov/federal/courts.nsf/autoframe!openform&nav=menu1&page=/federal/courts.nsf/page/183> (last visited Aug. 13, 2015) [hereinafter Fed. Judicial Ctr., *How the Federal Courts are Organized*].

121. Fed. Judicial Ctr., *How the Federal Courts are Organized*, *supra* note 120.

122. 28 U.S.C. § 2402 (2012).

123. Admin. Off. of the U.S. Courts, *Court Role and Structure*, *supra* note 114.

Courts of Appeal,<sup>124</sup> and then on to the U.S. Supreme Court if it grants *certiorari*.<sup>125</sup>

The U.S. Bankruptcy Courts have exclusive jurisdiction over bankruptcy cases,<sup>126</sup> and the U.S. Bankruptcy Courts have the express jurisdiction to determine federal tax liabilities.<sup>127</sup> Bankruptcy judges are appointed by the U.S. Courts of Appeal to serve renewable fourteen-year terms as judicial officers of the applicable U.S. District Courts.<sup>128</sup> Appeals from U.S. Bankruptcy Court decisions may be taken to the applicable U.S. District Court, although five U.S. Courts of Appeal have instead established three-judge Bankruptcy Appellate Panels to hear those appeals.<sup>129</sup> Subsequent appeals go to the 12 regional U.S. Courts of Appeals,<sup>130</sup> and then on to the U.S. Supreme Court if it grants *certiorari*.<sup>131</sup>

The U.S. Court of Federal Claims is an Article I court that also has jurisdiction over tax refund suits.<sup>132</sup> The court has 16 presidentially appointed judges who serve for a term of 15 years.<sup>133</sup> Jury trials are not available in the U.S. Court of Federal Claims,<sup>134</sup> and appeals from the Court of Federal Claims decisions are heard by the U.S. Court of Appeals for the Federal Circuit (an

---

124. *Id.*

125. 28 U.S.C. § 1254 (2012).

126. Admin. Off. of the U.S. Courts, *Bankruptcy Cases*, <http://www.uscourts.gov/about-federal-courts/types-cases/bankruptcy-cases> (last visited Aug. 13, 2015).

127. 11 U.S.C. § 505 (2012).

128. 28 U.S.C. § 152 (2012); Fed. Judicial Ctr., *History of the Judiciary: Bankruptcy Judges*, [http://www.fjc.gov/history/home.nsf/page/judges\\_bank.html](http://www.fjc.gov/history/home.nsf/page/judges_bank.html) (last visited Aug. 13, 2015).

129. Admin. Off. of the U.S. Courts, *Appeals*, <http://www.uscourts.gov/about-federal-courts/types-cases/appeals> (last visited Aug. 13, 2015); Admin. Off. of the U.S. Courts, *Court Role and Structure*, <http://www.uscourts.gov/about-federal-courts/court-role-and-structure> (last visited Aug. 13, 2015).

130. *Id.*

131. 28 U.S.C. § 1254 (2012).

132. 28 U.S.C. §§ 1491 *et seq.* (2012); U.S. Court of Fed. Claims, *About the Court*, <http://www.uscfc.uscourts.gov/about-court> (last updated Feb. 19, 2014) [hereinafter U.S. COURT OF FED. CLAIMS, *About the Court*]. From August 1978 through August 1979, author Jonathan Barry Forman had the privilege of serving as a judicial clerk for the Honorable Robert J. Yock on this court (when it was the U.S. Court of Claims, Trial Division).

133. U.S. Court of Fed. Claims, *About the Court*, *supra* note 132.

134. U.S. COURT OF FED. CLAIMS, THE PEOPLE'S COURT 4, [http://www.uscfc.uscourts.gov/sites/default/files/court\\_info/Court\\_History\\_Brochure.pdf](http://www.uscfc.uscourts.gov/sites/default/files/court_info/Court_History_Brochure.pdf) (last visited Aug. 13, 2015).

Article III court),<sup>135</sup> and then on to the U.S. Supreme Court if it grants *certiorari*.<sup>136</sup>

*B. The Current Tax Administration*

*1. Returns*

The U.S. has a voluntary self-reporting tax system; while various statutes require taxpayers to file returns and pay their tax liabilities, taxpayers generally calculate their own tax liability and file the appropriate tax returns.<sup>137</sup> For example, married couples filing jointly generally filed a joint income tax return for the 2014 tax year if they had more than \$20,300 of gross income.<sup>138</sup>

Table 3 shows the number of federal tax returns filed with the IRS for Fiscal Year 2014.<sup>139</sup> Of note, Table 3 does not include the almost 2.3 billion 1099s, and other third-party information returns that the IRS receives,<sup>140</sup> nor does it include the roughly 680,000 Forms 5500 (Annual Return/Report of Employee Benefit Plan) which are filed by pension plans through the electronic EFAST2 filing system jointly administered by U.S. Department of Labor, the IRS, and the Pension Benefit Guaranty Corporation.<sup>141</sup>

---

135. 28 U.S.C. § 1295 (2012); U.S. Court of Appeals for the Fed. Circuit, *Court Jurisdiction*, <http://www.cafc.uscourts.gov/the-court/court-jurisdiction> (last visited Aug. 13, 2015).

136. 28 U.S.C. § 1254.

137. *See, e.g.*, STAFF OF THE J. COMM. ON TAX'N, JCX-34-14, PRESENT LAW AND BACKGROUND RELATED TO THE REGULATION ON CONDUCT OF PAID TAX RETURN PREPARERS 2 (Apr. 4, 2014), [https://www.jct.gov/publications.html?func=download&id=4580&chk=4580&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4580&chk=4580&no_html=1); I.R.S., THE TRUTH ABOUT FRIVOLOUS TAX ARGUMENTS 1–5 (2014), [http://www.irs.gov/file\\_source/pub/irs-utl/friv\\_tax.pdf](http://www.irs.gov/file_source/pub/irs-utl/friv_tax.pdf); Bryan T. Camp, 'Loving' Return Preparer Regulation, 140 TAX NOTES 457 (July 30, 2013); J. T. Manhire, *What Does Voluntary Tax Compliance Mean?: A Government Perspective*, 164 U. PA. L. REV. ONLINE (forthcoming 2015), <http://ssrn.com/abstract=2601613>.

138. I.R.S., PUB. NO. 17, TAX GUIDE FOR INDIVIDUALS 6 tbl.1-1 (2015), [http://www.irs.gov/file\\_source/pub/irs-pdf/p17.pdf](http://www.irs.gov/file_source/pub/irs-pdf/p17.pdf).

139. 2014 IRS DATA BOOK, *supra* note 7, at 4 tbl.3.

140. *Id.* at 37, 38 tbl.14 (noting that the IRS received almost 2.3 billion third-party information returns in Fiscal Year 2014). In addition, the IRS also eventually receives information on the millions of W-2 forms that are filed with the Social Security Administration. *See, e.g.*, I.R.S., Form W-2, Wage and Tax Statement (2015), <http://www.irs.gov/pub/irs-pdf/fw2.pdf>; Soc. Sec. Admin., *Employer W-2 Filing Instructions & Information*, <http://www.socialsecurity.gov/employer/> (last visited Aug. 12, 2015).

141. U.S. Dep't of Labor, *EFAST2 Filing—Welcome*, <http://www.efast.dol.gov/welcome.html> (last visited Aug. 13, 2015); DOL, PRIVATE PENSION PLAN BULLETIN, *supra* note 69, at 3 tbl.A1.



**Table 3. Number of Returns Filed, by Type of Return, Fiscal Year 2014**  
(Numbers are in thousands)

<i>Type of Return</i>	<i>Number</i>
<b>United States, total</b>	<b>239,875</b>
<b>Income taxes, total</b>	<b>185,540</b>
C or other corporation	2,221
S corporation, Form 1120-S	4,643
Partnership, Form 1065	3,799
Individual	147,445
Forms 1040, 1040-A, 1040-EZ	146,568
Forms 1040-C, 1040-NR, 1040NR-EZ, 1040-PR, 1040-SS	877
Individual estimated tax, Form 1040-ES	23,608
Estate and trust, Form 1041	3,206
Estate and trust estimated tax, Form 1041-ES	618
<b>Employment taxes</b>	<b>30,066</b>
<b>Estate tax</b>	<b>34</b>
<b>Gift tax, Form 709</b>	<b>335</b>
<b>Excise taxes</b>	<b>987</b>
<b>Tax-exempt organizations</b>	<b>1,467</b>
<b>Supplemental documents</b>	<b>21,446</b>

In processing those 240 million tax returns in Fiscal Year 2014, the IRS collected almost \$3.1 trillion in revenue,<sup>142</sup> and it issued \$373.5 billion in refunds.<sup>143</sup> In its efforts to combat refund fraud, the IRS routinely suspends or rejects suspicious returns. For example, in Fiscal Year 2013, the IRS suspended or rejected more than 5.7 million suspicious returns and worked with victims of identity fraud to close more than 899,000 cases.<sup>144</sup>

## 2. *Voluntary Compliance and the Tax Gap*

Most taxpayers voluntarily pay their taxes on time without enforcement actions by the IRS.<sup>145</sup> According to a study by the IRS, 83.1 percent of the true tax liability was voluntarily paid on time without

142. See *supra* note 85 and accompanying text.

143. 2014 IRS DATA BOOK, *supra* note 7, at 1.

144. I.R.S., PUB. NO. 55-B, 2013 DATA BOOK iii (Mar. 2014), [http://www.irs.gov/file\\_source/pub/irs-soi/13databk.pdf](http://www.irs.gov/file_source/pub/irs-soi/13databk.pdf).

145. See, e.g., 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 3, 8; 2013 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 5 (“The U.S. tax system is built on voluntary compliance. The IRS estimates that it collects 85.5 percent of all tax owed. Of that amount, 98 percent is paid timely and voluntarily. Only two percent derives from late and enforced collection actions.” [footnotes omitted]).

enforcement activities for the 2006 tax year, about the same as for the 2001 tax year.<sup>146</sup> Every percentage point of compliance is significant, as a one percentage point drop in compliance would cost the government around \$30 billion per year.<sup>147</sup>

Taxpayers who do not comply generally fall into several identifiable categories—primarily individuals with business income and large corporations.<sup>148</sup> The gross tax gap is the difference between a taxpayer's true tax liability and the amounts paid on time.<sup>149</sup> The net tax gap is "the amount of true tax liability that is not paid on time and is not collected."<sup>150</sup> The difference between the gross tax gap and the net tax gap reflects IRS enforcement activities, as well as other payments made late without enforcement (such as just before the extended due date or with a voluntary amended or delinquent return).<sup>151</sup> The gross tax gap for 2006, the most recent year for which analysis is complete, was \$450 billion.<sup>152</sup> The net tax gap for 2006 was \$385 billion, reflecting \$65 billion of additional collections.<sup>153</sup> All

---

146. IR-2012-4, *IRS Releases New Tax Gap Estimates; Compliance Rates Remain Statistically Unchanged From Previous Study* (Jan. 6, 2012), <http://www.irs.gov/uac/IRS-Releases-New-Tax-Gap-Estimates;-Compliance-Rates-Remain-Statistically-Unchanged-From-Previous-Study>.

147. Jeremy Scott, *From the Editor: The Precarious State of Voluntary Compliance*, 144 TAX NOTES 893 (Aug. 25, 2014) (reporting on the remarks of IRS Commissioner John Koskinen); William Hoffman, *Koskinen Warns of House IRS Budget's Impact in 2015*, 144 TAX NOTES 919 (Aug. 25, 2014) [hereinafter Hoffman, *Koskinen Warns of House IRS Budget's Impact in 2015*]; Claire Berlin, Nat'l Soc. of Accountants, *IRS Commissioner Koskinen Criticizes Congress at NSA Annual Meeting*, Nov. 13, 2014, <http://connect.nsacct.org/blogs/claire-berlin/2014/11/13/irs-commissioner-koskinen-criticizes-congress-at-nsa-annual-meeting>. Actually, the IRS's 2006 tax gap estimated that a one percentage point drop in compliance cost the government \$26.6 billion for the 2006 Tax Year. I.R.S., *Tax Gap "Map"*, [http://www.irs.gov/file\\_source/pub/newsroom/tax\\_gap\\_map\\_2006.pdf](http://www.irs.gov/file_source/pub/newsroom/tax_gap_map_2006.pdf) (last visited May 3, 2015) (\$26.6 billion per percentage point = \$2,210 billion tax paid voluntarily & timely for tax year 2006 ÷ 83.1 percent). See also Eric Kroh, *U.S. Seen in Danger of Tumbling Over 'Compliance Cliff'*, 144 TAX NOTES 909 (Aug. 25, 2014).

148. See *infra* notes 161–162 and accompanying text (regarding IRS Tax Gap "Map").

149. I.R.S., *Tax Gap for Tax Year 2006: Overview 1* (Jan. 6, 2012), [http://www.irs.gov/file\\_source/pub/newsroom/overview\\_tax\\_gap\\_2006.pdf](http://www.irs.gov/file_source/pub/newsroom/overview_tax_gap_2006.pdf); JAMES M. BICKLEY, CONG. RESEARCH SERV. REP. NO. R42739, *TAX GAP, TAX COMPLIANCE, AND PROPOSED LEGISLATION IN THE 112TH CONGRESS 1* (Sept. 20, 2012), <http://fas.org/sgp/crs/misc/R42739.pdf>.

150. I.R.S., *Tax Gap for Tax Year 2006: Overview*, *supra* note 149.

151. *Id.*

152. *Id.*

153. *Id.*

in all, of the revenue the IRS collects, 98 percent is paid timely and voluntarily, and only two percent comes from late and enforcement actions.<sup>154</sup>

The tax gap is made up of underreporting, underpaying, and non-filing.<sup>155</sup> Underreporting is by far the largest proportion of the tax gap—\$376 billion (83.6 percent) in 2006.<sup>156</sup> Some \$235 billion (62.5 percent) of the 2006 underreported tax gap was due to the individual income tax.<sup>157</sup> The 2006 tax gap analysis showed that the compliance rate is much higher for income subject to third-party reporting and withholding. For example, wage income is subject to third-party reporting and mandatory withholding,<sup>158</sup> and Figure 2 shows that wages had a tiny net misreporting percentage of just one percent in 2006.<sup>159</sup> Figure 2 also shows that the next best category consists of amounts subject to third-party reporting but no withholding, such as domestic dividends,<sup>160</sup> with a net misreporting percentage of eight percent.

---

154. 2013 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 5.

155. *IRS Releases New Tax Gap Estimates; Compliance Rates Remain Statistically Unchanged From Previous Study*, *supra* note 146.

156. *Id.*; BICKLEY, TAX GAP, TAX COMPLIANCE, AND PROPOSED LEGISLATION IN THE 112TH CONGRESS, *supra* note 149, at 2.

157. *IRS Releases New Tax Gap Estimates; Compliance Rates Remain Statistically Unchanged From Previous Study*, *supra* note 146, at 2.

158. I.R.C. §§ 3401 *et seq.*; I.R.S., PUB. NO. 15 (CIRCULAR E), EMPLOYER'S TAX GUIDE 20 (2014), [http://www.irs.gov/file\\_source/pub/irs-pdf/p15.pdf](http://www.irs.gov/file_source/pub/irs-pdf/p15.pdf).

159. I.R.S., *Tax Gap for Tax Year 2006: Overview*, *supra* note 149, at 1–2, 3 chart 1. *See also* Mark D. Phillips, *Individual Income Tax Compliance and Information Reporting: What Do the U.S. Data Show?*, 67(3) NAT'L TAX J. 531 (2014).

160. *See, e.g.*, I.R.C. § 6042; I.R.S., Form 1099-DIV, Dividends and Distributions, <http://www.irs.gov/pub/irs-pdf/f1099div.pdf> (last visited Aug. 13, 2015).

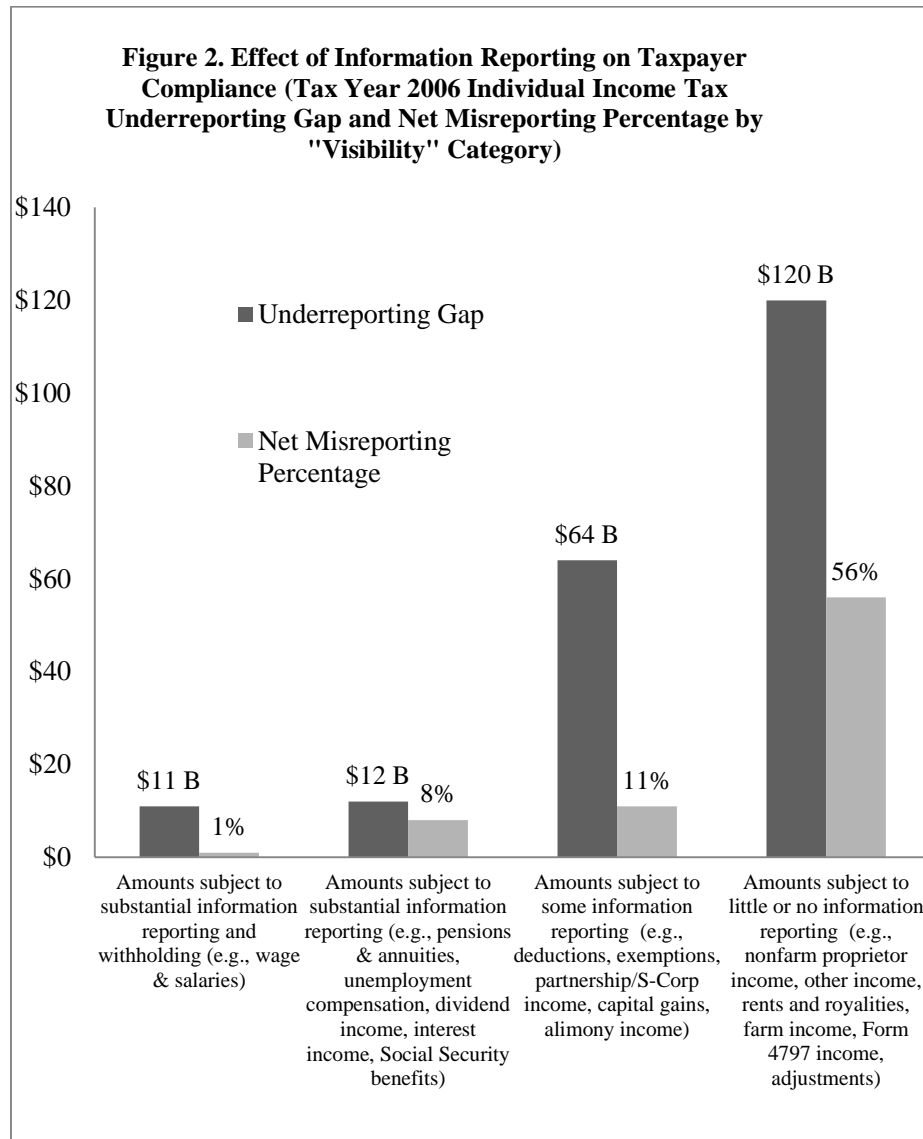


Figure 2 also shows that amounts subject to little or no information reporting by third parties (let alone withholding), such as business income, have a net misreporting percentage of 56 percent. For individuals, 52 percent of the underreporting was attributable to such business income.<sup>161</sup> For

161. Author-calculated percentage from IRS, *Tax Gap "Map"*, *supra* note 147 (52% = \$122 billion underreported business income tax liability ÷ \$235 billion total underreported individual income tax liability).

corporations, 72 percent of the underreporting was attributable to large corporations, defined as corporations with assets of \$10 million or more.<sup>162</sup>

### 3. *Enforcement*

The IRS has a number of programs to ensure compliance with the tax filing, reporting, and payment requirements.<sup>163</sup>

#### a. *Math Error*

The IRS's Math Error program corrects any obvious math errors as returns are processed.<sup>164</sup> Once a taxpayer has filed a return, the IRS evaluates and processes it. In the routine processing of tax returns, the IRS checks for mathematical and clerical errors before refunds are paid.<sup>165</sup> For example, in 2014, the IRS sent more than 1.7 million notices to taxpayers for "math errors" identified on their 2013 returns.<sup>166</sup>

#### b. *Document Matching*

The IRS also collects information on taxpayers from employers, financial institutions, and other third parties and compiles that data in its Information Returns Processing (IRP) system.<sup>167</sup> Then, the Automated Underreporter (AUR) program matches that data against the information that taxpayers reported on their returns in order to identify returns with potentially underreported income or unwarranted deductions or tax credits.<sup>168</sup> In some cases, a notice is sent to the taxpayer asking for an explanation of the discrepancy, while other cases are referred for an audit.<sup>169</sup> The Automated

---

162. Author-calculated percentage from *id.* (72% = \$48 billion underreported corporate income tax liability of large corporations ÷ \$67 billion total underreported corporate income tax liability).

163. *See, e.g.*, U.S. GOV'T ACCOUNTABILITY OFF., GAO-13-151, TAX GAP: IRS COULD SIGNIFICANTLY INCREASE REVENUES BY BETTER TARGETING ENFORCEMENT RESOURCES 3-5 (2012), <http://www.gao.gov/assets/660/650521.pdf> [hereinafter TAX GAP: IRS COULD SIGNIFICANTLY INCREASE REVENUES].

164. *Id.* at 4.

165. *Id.* The Math Error program also disallows various benefits under certain circumstances.

166. 2014 IRS DATA BOOK, *supra* note 7, at 37, 39 tbl.15.

167. TAX GAP: IRS COULD SIGNIFICANTLY INCREASE REVENUES, *supra* note 163, at 4.

168. *Id.*

169. *Id.*

Substitute for Return (ASFR) program uses that IRP third-party data to identify non-filers and to create substitute returns for them.<sup>170</sup>

c. *Examinations*

The IRS may conduct an audit of a taxpayer's accounts and financial information to make sure that information is being reported correctly.<sup>171</sup> Correspondence Examinations are formal audits that are handled through correspondence between the taxpayer and the IRS examiner.<sup>172</sup> Field Examinations are face-to-face audits involving meetings between the taxpayer and the IRS examiner.<sup>173</sup> Face-to-face audits can also take place at an IRS office,<sup>174</sup> although for statistical purposes these office audits appear to be included in IRS statistics as field audits.<sup>175</sup>

In Fiscal Year 2014, the IRS examined 1,384,365 returns, about 0.7 percent of the 189,656,600 returns considered that year.<sup>176</sup> There were 401,340 field examinations and 983,025 correspondence examinations,<sup>177</sup> and altogether the IRS recommended additional taxes of more than \$31.2 billion.<sup>178</sup>

Roughly 0.9 percent of individual income tax returns were examined in Fiscal Year 2014, including 7.5 percent of returns with more than \$1,000,000 of income.<sup>179</sup> The IRS also examined 1.3 percent of corporate income tax returns that year, including, for example, 30.1 percent of

170. *Id.* at 4–5. See also I.R.M. 4.12.1, [http://www.irs.gov/irm/part4/irm\\_04-012-001.html](http://www.irs.gov/irm/part4/irm_04-012-001.html).

171. I.R.S., *IRS Audits*, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/IRS-Audits> (last updated May 18, 2015).

172. TAX GAP: IRS COULD SIGNIFICANTLY INCREASE REVENUES, *supra* note 163, at 5.

173. *Id.*

174. I.R.S., *IRS Audits*, *supra* note 171.

175. This is our inference from what is written in the 2014 IRS DATA BOOK, *supra* note 7, at 22: “IRS conducted the majority of FY 2014 audits, 71 percent, via correspondence. The remaining 29 percent were conducted in the field.”

176. *Id.* at 23 tbl.9a. See also I.R.S., *Fiscal Year 2014 Enforcement and Service Results*, [http://www.irs.gov/file\\_source/PUP/newsroom/FY-2014%20Enforcement%20and%20Service%20Results%20--%20web%20version.pdf](http://www.irs.gov/file_source/PUP/newsroom/FY-2014%20Enforcement%20and%20Service%20Results%20--%20web%20version.pdf) (last visited Aug. 13, 2015) [hereinafter I.R.S., *Fiscal Year 2014 Enforcement and Service Results*] (reporting slightly different numbers).

177. 2014 IRS DATA BOOK, *supra* note 7, at 23 tbl.9a.

178. *Id.* at 24 tbl.9a (\$31,240,521,000).

179. *Id.* at 23. See also I.R.S., *Fiscal Year 2014 Enforcement and Service Results*, *supra* note 176, at 2; Lisa Rein, *In Dallas, the IRS says it can't chase tax cheats who owe less than \$1 million*, WASH. POST, Apr. 8, 2015, <http://www.washingtonpost.com/blogs/federal-eye/wp/2015/04/08/in-dallas-the-irs-says-it-cant-chase-tax-cheats-who-owe-less-than-1-million/>.

corporations with between \$1 and \$5 billion of assets and 84.2 percent of corporations with \$20 billion or more in assets.<sup>180</sup> The IRS also examined 0.36 percent of Subchapter S corporations and 0.43 percent of partnerships.<sup>181</sup> In addition, the IRS examined 20,971 returns of tax-exempt organizations, employee retirement plans, government entities, and tax-exempt bonds.<sup>182</sup>

*d. Appeals within the IRS*

When taxpayers disagree with IRS decisions to assess additional tax or take collection action, taxpayers are generally entitled to an administrative review with the Office of Appeals (Appeals), an independent organization within the IRS.<sup>183</sup> Appeals handles around 115,000 cases a year.<sup>184</sup> Most of the cases arise as a result of IRS examination or collection activities.<sup>185</sup> In a typical case, the taxpayer gets to Appeals after an audit by filing a protest to the 30-day letter that she receives from the IRS.<sup>186</sup> Also, filing a petition in the U.S. Tax Court will generally result in the taxpayer's case being referred to Appeals if it has not already considered the dispute,<sup>187</sup> and many IRS collection actions also lead to Appeals.<sup>188</sup>

---

180. 2014 IRS DATA BOOK, *supra* note 7, at 23 tbl.9a. *See also* I.R.S., *Fiscal Year 2014 Enforcement and Service Results*, *supra* note 176, at 3 (showing that the IRS examined 12.23 percent of the returns of large corporations, defined as those with \$10 million or more in assets).

181. I.R.S., *Fiscal Year 2014 Enforcement and Service Results*, *supra* note 176, at 3.

182. 2014 IRS DATA BOOK, *supra* note 7, at 34 tbl.13.

183. *See, e.g.*, I.R.M. pt. 8 (Appeals), [http://www.irs.gov/irm/part8/irm\\_08-001-001.html](http://www.irs.gov/irm/part8/irm_08-001-001.html); I.R.S., *Appeals . . . Resolving Tax Disputes*, <http://www.irs.gov/Individuals/Appeals-Resolving-Tax-Disputes> (last updated Apr. 20, 2015); U.S. GOV'T ACCOUNTABILITY OFF., GAO-06-396, TAX ADMINISTRATION: OPPORTUNITIES TO IMPROVE COMPLIANCE DECISIONS AND SERVICE TO TAXPAYERS THROUGH ENHANCEMENTS TO APPEALS' FEEDBACK PROJECT 1 (2006), <http://www.gao.gov/assets/250/249414.pdf>.

184. *See, e.g.*, 2014 IRS DATA BOOK, *supra* note 7, at 51 tbl.21 (showing that Appeals received 113,608 cases and closed 115,472 cases in Fiscal Year 2014).

185. *See id.*

186. *See, e.g.*, I.R.S., *Letters and Notices Offering an Appeal Opportunity*, <http://www.irs.gov/Individuals/Letters-and-Notices-Offering-an-Appeal-Opportunity> (last updated Sept. 1, 2015); I.R.S., PUB. NO. 556, EXAMINATION OF RETURNS, APPEAL RIGHTS, AND CLAIMS FOR REFUND 5 (2013), [http://www.irs.gov/file\\_source/pub/irs-pdf/p556.pdf](http://www.irs.gov/file_source/pub/irs-pdf/p556.pdf) [hereinafter I.R.S., EXAMINATION OF RETURNS, APPEAL RIGHTS, AND CLAIMS FOR REFUND].

187. I.R.S., EXAMINATION OF RETURNS, APPEAL RIGHTS, AND CLAIMS FOR REFUND, *supra* note 186, at 9; I.R.M. 8.4.1, [http://www.irs.gov/irm/part8/irm\\_08-004-001.html](http://www.irs.gov/irm/part8/irm_08-004-001.html).

188. *See, e.g.*, I.R.S., PUB. NO. 1660, COLLECTION APPEAL RIGHTS (2012), [http://www.irs.gov/file\\_source/pub/irs-pdf/p1660.pdf](http://www.irs.gov/file_source/pub/irs-pdf/p1660.pdf); I.R.M. 8.22.4, <http://www.irs.gov>.

*e. Collection Activities*

While most taxpayers pay the taxes that are shown on their returns or subsequently assessed after the IRS reviews their returns,<sup>189</sup> the IRS also endeavors to collect taxes that have been reported or assessed but not paid voluntarily. In Fiscal Year 2014, for example, the IRS filed 535,580 federal tax liens and served 1,995,987 notices of levy on third parties.<sup>190</sup>

Noncompliance with the tax laws can also result in civil and criminal penalties.<sup>191</sup> For example, in Fiscal Year 2014, the IRS assessed more than 40.3 million civil penalties and initiated 4,297 criminal investigations.<sup>192</sup>

Also in Fiscal Year 2014, taxpayers submitted around 68,000 offers in compromise in settlement of their outstanding tax liabilities, and the IRS accepted around 27,000 of those offers.<sup>193</sup> The IRS is authorized to accept the taxpayer's offer in compromise of less than the amount due if: 1) there is doubt as to the amount of the tax liability; 2) there is doubt as to the collectability of the tax liability; or 3) requiring payment in full would either create economic hardship or would be unfair because of exceptional circumstances.<sup>194</sup>

*f. Revenue Collected by Enforcement Activities*

Table 4 summarizes how much revenue the IRS has collected in recent years as a result of its various enforcement activities.<sup>195</sup>

---

gov/irm/part8/irm\_08-022-004.html.

189. See *supra* note 146 and accompanying text.

190. 2014 IRS DATA BOOK, *supra* note 7, at 43 tbl.16. A federal tax lien gives the IRS a claim to all of a taxpayer's property. See, e.g., I.R.C. §§ 6321 *et seq.*; I.R.S., *Understanding a Federal Tax Lien*, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Understanding-a-Federal-Tax-Lien> (last updated Sept. 15, 2015). A levy is an administrative action by the IRS to seize property to satisfy a tax debt. See, e.g., I.R.C. §§ 6331 *et seq.*; I.R.S., *Levy*, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Levy> (last updated Sept. 10, 2015).

191. Civil penalties include Code sections 6651, 6662, and 6663. Criminal penalties include: I.R.C. §§ 7201, 7206.

192. 2014 IRS DATA BOOK, *supra* note 7, at 44 tbl.17, 46 tbl.18. In Fiscal Year 2014, the civil penalties assessed came to almost \$25.6 billion. *Id.* at 41.

193. *Id.* at 41.

194. Reg. § 301.7122-1.

195. I.R.S., *Fiscal Year 2014 Enforcement and Service Results*, *supra* note 176, at 1.



**Table 4. Enforcement Revenue Collected, FY2005–FY2014**  
(billions of dollars)

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Collection	26.6	28.2	31.8	31.1	26.9	29.1	31.10	30.44	31.40	33.20
Examination	13.8	13.0	15.2	15.8	12.6	16.9	12.40	10.20	9.83	12.51
Appeals	3.9	4.3	8.3	4.8	4.8	6.7	6.50	4.20	6.83	6.47
Document Matching	3.1	3.3	3.9	4.7	4.6	4.9	5.20	5.27	5.29	4.97
<b>Total</b>	<b>47.3</b>	<b>48.7</b>	<b>59.2</b>	<b>56.4</b>	<b>48.9</b>	<b>57.6</b>	<b>55.20</b>	<b>50.20</b>	<b>53.35</b>	<b>57.15</b>

#### 4. *Litigation*

Taxpayers who disagree with IRS decisions may be able to take their cases to the U.S. Tax Court, a U.S. District Court, or the U.S. Court of Federal Claims.<sup>196</sup> When a taxpayer receives a notice of deficiency from the IRS, the taxpayer usually has 90 days to file a petition in the U.S. Tax Court.<sup>197</sup> When a taxpayer receives an adverse determination after a collection due process hearing at IRS Appeals, the taxpayer has 30 days to file an appeal to the U.S. Tax Court.<sup>198</sup> The U.S. Tax Court handles more than 30,000 cases a year.<sup>199</sup> As already mentioned, appeals generally go to the U.S. Court of Appeals where the taxpayer is located and then on to the U.S. Supreme Court.<sup>200</sup>

Alternatively, taxpayer claims for the refund of any tax paid can be brought in the appropriate U.S. District Court or in the U.S. Court of Federal Claims.<sup>201</sup> These trial courts hear refund suits only after the taxpayer has paid the tax and filed a claim for refund with the IRS.<sup>202</sup> The U.S. Department of Justice also initiates numerous civil and criminal cases in the U. S. District Courts.<sup>203</sup> As already mentioned, there are 94 U.S. District Courts around the

196. I.R.S., EXAMINATION OF RETURNS, APPEAL RIGHTS, AND CLAIMS FOR REFUND, *supra* note 186, at 9. *See supra* Part III.A.

197. I.R.C. § 6213 (or 150 days if the notice is addressed to a person outside the United States).

198. I.R.C. § 6330(d)(1); Danshera Cords, *How Much Process is Due? I.R.C. Sections 6320 and 6330 Collection Due Process Hearings*, 29 VT. L. REV. 51, 51 (2004). *See also* Leslie Book, *The Collection Due Process Rights: A Misstep or Step in the Right Direction*, 41 HOUS. L. REV. 1145 (2004).

199. 2014 IRS DATA BOOK, *supra* note 7, at 63 tbl.27 (showing that the Chief Counsel of the IRS received 34,346 U.S. Tax Court cases in Fiscal Year 2014).

200. *See supra* notes 118–119 and accompanying text.

201. I.R.S., PUB. NO. 5, YOUR APPEAL RIGHTS AND HOW TO PREPARE A PROTEST IF YOU DON'T AGREE 2 (1999), <http://www.irs.gov/pub/irs-pdf/p5.pdf> [hereinafter I.R.S., YOUR APPEAL RIGHTS AND HOW TO PREPARE A PROTEST IF YOU DON'T AGREE]. *See also supra* note 112 and accompanying text.

202. I.R.S., YOUR APPEAL RIGHTS AND HOW TO PREPARE A PROTEST IF YOU DON'T AGREE, *supra* note 201, at 2.

203. U.S. DEP'T OF JUSTICE, *About the Tax Division*, *supra* note 100.

country, where the appeals go to 12 regional U.S. Courts of Appeal, and then to the U.S. Supreme Court.<sup>204</sup> Also, as already mentioned, the U.S. Court of Federal Claims is a court of national jurisdiction located in Washington, D.C., and appeals go the U.S. Court of Appeals for the Federal Circuit, and then on to the Supreme Court.<sup>205</sup>

The IRS Office of Chief Counsel handles the U.S. Tax Court litigation,<sup>206</sup> while the U.S. Department of Justice Tax Division handles most affirmative and defensive tax litigation in the remaining federal courts,<sup>207</sup> with the U.S. Department of Justice Office of the Solicitor General handling all the Supreme Court cases.<sup>208</sup> The Tax Division typically handles around 6,600 civil tax cases, 700 tax appeals, and alone or with the Assistant U.S. Attorneys, the Tax Division works between 1,300 and 1,800 criminal tax cases each year.<sup>209</sup>

Pertinent here, the IRS's Low-Income Taxpayer Clinic program provides grants to independently operated low-income taxpayer clinics (LITCs) throughout the U.S.<sup>210</sup> Section 7526(b)(1)(B)(i) requires that at least 90 percent of the taxpayers represented by a LITC have incomes that do not exceed 250 percent of the federal poverty level.<sup>211</sup> In 2013, LITCs provided representation in more than 18,000 cases and held more than 25,000 direct consultations with taxpayers.<sup>212</sup> In 2014, the IRS awarded about \$10 million in grants to LITCs in 47 States and the District of Columbia.<sup>213</sup>

##### 5. *Guidance and Other Activities*

The IRS also provides guidance and other assistance for taxpayers. For example, the IRS updates almost all of its forms and publications each year.<sup>214</sup> Also, along with the Office of Chief Counsel and the Treasury Office of Tax Policy, the IRS is actively involved in issuing regulations, revenue rulings, revenue procedures, and other formal guidance.<sup>215</sup> The IRS also issues

---

204. *See supra* notes 123–125 and accompanying text.

205. *See supra* notes 132–136 and accompanying text.

206. *See, e.g.*, I.R.M. 35.5.1.1, [http://www.irs.gov/irm/part35/irm\\_35-005-001.html](http://www.irs.gov/irm/part35/irm_35-005-001.html).

207. U.S. DEP'T OF JUSTICE, *About the Tax Division*, *supra* note 100.

208. *See supra* note 103 and accompanying text.

209. *See supra* note 101 and accompanying text.

210. *See, e.g.*, TAXPAYER ADVOCATE SERV., LOW INCOME TAXPAYER CLINICS: PROGRAM REPORT 4 (Dec. 2014), <http://www.irs.gov/pub/irs-pdf/p50666.pdf>.

211. *Id.* at 7.

212. *Id.* at 10.

213. *Id.* at 11, 22 app. A.

214. *See, e.g.*, I.R.S., Forms & Publications, <http://www.irs.gov/Forms-&-Pubs> (last updated June 11, 2015) [hereinafter I.R.S., Forms & Publications].

215. *See, e.g.*, I.R.M. pt. 32, [http://www.irs.gov/irm/part32/irm\\_32-001-001.html](http://www.irs.gov/irm/part32/irm_32-001-001.html).

private letter rulings (PLRs) to taxpayers on qualifying issues.<sup>216</sup> While the IRS collects a fee for PLRs, which varies depending on the requesting taxpayer's category, it is unclear whether the PLR fees cover the administrative costs of issuing PLRs.<sup>217</sup>

In addition, the IRS communicates directly with millions of taxpayers and their representatives. In Fiscal Year 2014, for example, there were 437.1 million visits to the [irs.gov](http://irs.gov) website, and 69.4 million taxpayers got assistance through its toll-free telephone hotline or at walk-in sites.<sup>218</sup> The IRS Taxpayer Advocate Service also provided post-filing taxpayer assistance to some 220,000 taxpayers that year.<sup>219</sup>

In addition to dealing with revenue-generating taxpayers, the IRS also provides formal guidance to employee retirement plans, tax-exempt organizations, and the issuers of tax-exempt bonds.<sup>220</sup> The IRS also routinely issues determination letters on employee retirement plans and reviews and approves applications for tax-exempt status by charities and other tax-exempt organizations.<sup>221</sup>

Finally, the IRS also has to manage and safeguard a vast amount of taxpayer information, while at the same time, making that information available to its employees, to taxpayers when it is needed to resolve disputes, and even to third-parties when it is needed to establish eligibility for tax benefits, student loans, and many other benefits.<sup>222</sup> Pertinent here, during the

---

216. See, e.g., Rev. Proc. 2015-1, 2015-1 I.R.B. 1; I.R.M. 32.3.2 (Letter Rulings), [http://www.irs.gov/irm/part32/irm\\_32-003-002.html](http://www.irs.gov/irm/part32/irm_32-003-002.html).

217. Rev. Proc. 2015-1, *supra* note 216. PLR user fees range from \$2,200 to \$28,300, with discounts for substantially identical requests. *Id.* at 79 app. A.

218. 2014 IRS DATA BOOK, *supra* note 7, at 47.

219. *Id.* at 50 tbl.20 (showing that the Taxpayer Advocate Service received 216,697 cases in Fiscal Year 2014 and closed 222,974 cases that year).

220. See, e.g., *id.* at 55, tbl.22.

221. See, e.g., *id.* at 56 tbl.23, 57 tbl.24, 58 tbl.25. See also U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2015-10-025, STATUS OF ACTIONS TAKEN TO IMPROVE THE PROCESSING OF TAX-EXEMPT APPLICATIONS INVOLVING POLITICAL CAMPAIGN INTERVENTION (Mar. 27, 2015), <http://www.treasury.gov/tigta/auditreports/2015reports/201510025fr.pdf>. Note that the IRS recently announced that it is going to significantly reduce the scope of its determination letter program for individually designed pension plans. See *infra* note 481 and accompanying text.

222. For example, federal tax information for students and their parents are often required on the Free Application for Federal Student Aid (FAFSA) form that most applicants for financial aid fill out. See, e.g., FEDERAL STUDENT AID, *FAFSA: Applying for Aid*, <https://studentaid.ed.gov/sa/fafsa/filling-out> (last viewed Aug. 13, 2015). Along the same lines, taxpayers with unpaid debts for overdue child support, state income taxes, or student loans can see their refunds offset. See, e.g., I.R.S., IRS Tax Tip 2013-60, *Six Facts on Tax Refunds and Offsets* (Apr. 22, 2013), <http://www.irs.gov/uac/Newsroom/Six-Facts-on-Tax-Refunds-and-Offsets>.

2015 filing season, hackers used the IRS's "Get Transcript" system to steal personal information from some 104,000 taxpayers.<sup>223</sup>

#### 6. *A Summary of the IRS Budget and Staffing Levels*

At bottom, it is the IRS that is America's tax administrator, although it receives some help from other agencies. Accordingly, it makes sense to take a closer look at the IRS's budget and staffing levels. In the Fiscal Year 2015, the IRS total full-time equivalent employment of 82,203, had an appropriation of \$10.945 billion, and had a total program operation level budget (including user fees) of \$11.976.<sup>224</sup>

Table 5 shows more detail about how the IRS allocates its budget a typical year.<sup>225</sup> Pertinent here, Congress appropriates separate amounts for distinct categories of IRS activity (i.e., Taxpayer Services, Enforcement, Operations Support, and Business Systems Modernization), and funds generally cannot be shifted from one appropriation to another.<sup>226</sup> However,

---

223. Lisa Rein & Jonnelle Marte, *Hackers stole personal information from 104,000 taxpayers, IRS says*, WASH. POST (May 26, 2015), <http://www.washingtonpost.com/blogs/federal-eye/wp/2015/05/26/hackers-stole-personal-information-from-104000-taxpayers-irs-says/>; Emmarie Huetteman, *Chief Says I.R.S. Struggles to Stay Ahead of Online Attackers*, N.Y. TIMES, June 2, 2015, at B5, [http://www.nytimes.com/2015/06/03/business/chief-says-irs-struggles-to-stay-ahead-of-online-attackers.html?emc=edit\\_th\\_20150603&nl=todaysheadlines&nid=16486715&\\_r=0](http://www.nytimes.com/2015/06/03/business/chief-says-irs-struggles-to-stay-ahead-of-online-attackers.html?emc=edit_th_20150603&nl=todaysheadlines&nid=16486715&_r=0); I.R.S., *Written Testimony of Commissioner Koskinen on Unauthorized Attempts to Access Taxpayer Data before Senate Finance Committee* (June 2, 2015), <http://www.irs.gov/uac/Written-Testimony-of-Commissioner-Koskinen-on-Unauthorized-Attempts-to-Access-Taxpayer-Data-before-Senate-Finance-Committee>. See also U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-405, *IRS NEEDS TO ADDRESS CONTROL WEAKNESSES THAT PLACE FINANCIAL AND TAXPAYER DATA AT RISK* (2014), <http://www.gao.gov/products/GAO-14-405> (noting weaknesses in the IRS's information security control); U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., *MANAGEMENT AND PERFORMANCE CHALLENGES FACING THE INTERNAL REVENUE SERVICE FOR FISCAL YEAR 2015*, at 3 (Oct. 15, 2014), [http://www.treasury.gov/tigta/management/management\\_fy2015.pdf](http://www.treasury.gov/tigta/management/management_fy2015.pdf) ("Computer security has been problematic for the IRS since 1997.").

224. BUDGET IN BRIEF 2016, *supra* note 1, at 61 tbl.

225. 2014 IRS DATA BOOK, *supra* note 7, at 65 tbl.28. See also BUDGET IN BRIEF 2016, *supra* note 1, at 61 tbl. (showing similar information for Fiscal Year 2014 [actual] and Fiscal Years 2015 and 2016 [estimates]).

226. See, e.g., Consolidated and Further Continuing Appropriations Act, 2015, Pub. L. No. 113-235, div. E, tit. I, 128 Stat. 2130, 2336-40 (2014).

the IRS has does have discretion over the allocation of user fees.<sup>227</sup> Table 6 shows how the IRS allocates its staff in a typical year.<sup>228</sup>

**Table 5. Costs Incurred by Budget Activity, Fiscal Year 2014**  
(thousands of dollars)

<i>Budget activity</i>	<i>Total</i>	<i>Personnel compensation and benefits</i>	<i>Other</i>
<b>Total obligations against appropriated funds</b>	<b>11,591,007</b>	<b>8,554,261</b>	<b>3,036,746</b>
<b>Taxpayer Services</b>			
<b>Total</b>	<b>2,345,229</b>	<b>2,173,414</b>	<b>171,815</b>
Prefiling Taxpayer Assistance and Education	628,940	563,633	65,307
Filing and Account Services	1,716,289	1,609,781	106,508
<b>Enforcement</b>			
<b>Total</b>	<b>4,944,885</b>	<b>4,683,916</b>	<b>260,969</b>
Investigations	604,070	563,126	40,944
Examinations and Collections	4,169,169	3,952,501	216,668
Regulatory	171,646	168,289	3,357
<b>Operations Support</b>			
<b>Total</b>	<b>4,054,808</b>	<b>1,625,556</b>	<b>2,429,252</b>
Infrastructure	874,938	588	874,350
Shared Services and Support	1,137,127	719,377	417,750
Information Services	2,042,743	905,591	1,137,152
<b>Business Systems Modernization</b>	<b>246,085</b>	<b>71,375</b>	<b>174,710</b>

227. See, e.g., U.S. H.R. COMM. ON WAYS & MEANS MAJORITY STAFF REP., DOING LESS WITH LESS: IRS'S SPENDING DECISIONS HARM TAXPAYERS 3 (Apr. 22, 2015), <http://waysandmeans.house.gov/wp-content/uploads/2015/07/4.21.15-Tax-Filing-Report.pdf> [hereinafter U.S. H.R. COMM. ON WAYS & MEANS MAJORITY STAFF REP., DOING LESS WITH LESS]; U.S. GOV'T ACCOUNTABILITY OFF., GAO-15-624, IRS 2016 BUDGET: IRS IS SCALING BACK ACTIVITIES AND USING BUDGET FLEXIBILITIES TO ABSORB FUNDING CUTS 12–13 (2015), <http://www.gao.gov/assets/680/670968.pdf> [hereinafter GAO, IRS IS SCALING BACK ACTIVITIES].

228. 2014 IRS DATA BOOK, *supra* note 7, at 69 tbl.30. See also GAO, IRS IS SCALING BACK ACTIVITIES, *supra* note 227, at 30 tbl.5.

**Table 6. Personnel Summary by Employment Status, Budget Activity, and Selected Personnel Type, Fiscal Year 2014**

<i>Employment status, budget activity, and selected personnel type</i>	<i>Average positions realized</i>	<i>Number of employees at close of fiscal year</i>
<b>Internal Revenue Service, total</b>	<b>84,133</b>	<b>78,121</b>
<b>Employment status:</b>		
Full-time permanent	82,406	76,126
Other	1,727	1,995
<b>Budget activity:</b>		
Examinations and Collections	37,608	37,266
Filing and Account Services	23,972	17,925
Information Services	6,711	7,258
Prefiling Taxpayer Assistance & Education	5,449	5,594
Shared Services and Support	5,097	5,195
Investigations	3,581	3,608
Regulatory	1,239	1,201
Business Systems Modernization	476	74
<b>Selected personnel type:</b>		
Revenue Agents	11,659	11,422
Seasonal Employees	10,030	4,100
Customer Service Representatives	8,837	8,820
Tax Examiners	8,416	8,496
Revenue Officers	4,439	4,353
Special Agents	2,437	2,454
Tax Technicians	1,418	1,357
Attorneys	1,473	1,454
Appeals Officers	761	758

### 7. A Closer Look at the Tax Gap and Compliance

All in all, the IRS is amazingly effective at collecting revenue, despite the relatively low level of its audits and other enforcement and collection efforts. For example, in Fiscal Year 2014, the IRS—with a budget of just \$11.6 billion—collected around \$3.1 trillion dollars, and that worked out to a cost of \$0.38 for every \$100 collected that year.<sup>229</sup> Put differently, that is an average

229. 2014 IRS DATA BOOK, *supra* note 7, at 63, 68 tbl.29.

return on investment of about 264 to one: for every \$1 spent on IRS operations, \$264 was collected.<sup>230</sup>

To be sure, the tax revenue paid voluntarily costs little to deposit (although determining the correct amounts to refund can require significant efforts). The presence of IRS educational, enforcement, and collection activities seems to inspire voluntary compliance, although the degree to which this is true is unclear.<sup>231</sup> Changes in audit coverage are generally believed to affect voluntary compliance by altering taxpayers' perceived risks of being audited: the higher the risk of being audited, the less likely a taxpayer is to evade taxes.<sup>232</sup> This view is consistent with the classic economic theory of tax evasion, which holds that a rational taxpayer will evade taxes if the expected savings from tax evasion exceed the expected penalty for non-compliance.<sup>233</sup>

Accordingly, it would almost certainly make sense to increase the IRS's budget significantly, and it is no wonder that IRS Commissioner John A. Koskinen called the recent Fiscal Year 2015 budget cuts "a tax cut for tax cheats."<sup>234</sup> Unfortunately, however, we do not think that IRS budget increases are very likely, even in the long run.<sup>235</sup> In the short run, the appropriations bill working its way through the House of Representatives would cut the IRS's Fiscal Year 2016 budget by \$838 million from its Fiscal Year 2015 levels.<sup>236</sup> One member of the House Appropriations Committee concluded that "these

---

230. Authors' computation from *id.* ( $264.37 = \$3,064,301,358,000$  gross collections  $\div$   $\$11,591,007,000$  operating costs; following I.R.S., IR-2013-3, *National Taxpayer Advocate Delivers Annual Report to Congress; Focuses on Tax Reform, IRS Funding and Identity Theft* (Jan. 9, 2013), <http://www.irs.gov/uac/Newsroom/National-Taxpayer-Advocate-Delivers-2012-Annual-Report-to-Congress> (finding a return on investment of 214 to one for Fiscal Year 2012)).

231. Recall that 83.1 percent of tax liabilities are voluntarily paid on time, and that a one percentage point drop in compliance would cost the government around \$30 billion per year. *See supra* notes 146–147 and accompanying text.

232. Pertinent here, the GAO has noted that the voluntary tax compliance of taxpayers who were not examined could be affected by resource reallocation. TAX GAP: IRS COULD SIGNIFICANTLY INCREASE REVENUES, *supra* note 163, at 12. However, the indirect effects of enforcement activities are difficult to estimate, and no empirical evidence exists as to whether overall voluntary compliance would increase or decrease as a result of specific resource reallocations. *Id.*

233. *See, e.g.,* Michael G. Allingham & Agnar Sandmo, *Income Tax Evasion: A Theoretical Analysis*, 1 J. OF PUB. ECON. 323 (1972).

234. Associated Press, *IRS Head Says Budget Cuts Could Delay Tax Refunds*, *supra* note 1.

235. *See infra* Part IV.A.

236. *Full Committee Markup – FY 2016 Financial Services and General Government Appropriations Bill* (June 17, 2015) (opening statement of Rep. Hal Rogers, Chairman, H. Comm. on Appropriations), <http://docs.house.gov/meetings/AP/AP00/20150617/103644/HMKP-114-AP00-20150617-SD002.pdf>.

actions will help the IRS clean up its act so it can operate more efficiently and protect the rights of the American people.”<sup>237</sup>

While spending more on enforcement would almost certainly raise far more revenue than it costs, increasing enforcement might also increase the burdens on compliant taxpayers.<sup>238</sup> For example, audits are burdensome for both compliant and noncompliant taxpayers, and even now many audits result in no-change findings.<sup>239</sup> Our politicians are loath to increase enforcement budgets to maximize revenues, as they want to balance their desire for revenue with the political costs of inflicting pain on compliant taxpayers.<sup>240</sup> Some even ascribe nefarious motives to Congress’s recent IRS budget cuts. For example, Jared Bernstein, former chief economist to Vice-President Joseph Biden, considers the IRS budget cuts to be “a different way to shrink government, accommodate tax evasion, and even undermine the implementation of health reform.”<sup>241</sup>

#### IV. KEY PROBLEMS WITH CURRENT TAX ADMINISTRATION

##### A. *The Internal Revenue Service is Significantly Underfunded*

The IRS is seriously underfunded. At the outset, Table 7 shows how IRS costs and personnel changed from Fiscal Year 2005 through Fiscal Year 2014.<sup>242</sup> Pertinent here, the number of individual income tax returns filed

---

237. *Id.*

238. See, e.g., U.S. GOV’T ACCOUNTABILITY OFF., GAO/T-GGD-97-186, TAXPAYER RIGHTS AND BURDENS DURING AUDITS OF THEIR TAX RETURNS (STATEMENT OF JAMES WHITE) (1997), <http://www.gao.gov/assets/110/107079.pdf>.

239. See, e.g., U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2012-30-062, THE RECOMMENDED ADJUSTMENTS FROM S CORPORATION AUDITS ARE SUBSTANTIAL, BUT THE NUMBER OF NO-CHANGE AUDITS IS A CONCERN (June 21, 2012), <http://www.treasury.gov/tigta/auditreports/2012reports/201230062fr.pdf> (expressing concern that 62 percent of the S corporation returns audited after selection by the Discriminant Index Function system were closed as a no-change).

240. For example, the National Taxpayer Advocate argues that “the government has a moral and practical imperative to make the tax compliance process as painless as possible.” 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 5. On the other hand, the real or perceived “pain” of the IRS’s enforcement activities undoubtedly contributes to the overall deterrent effect of that enforcement: people want to avoid that pain, as well as any additional tax and penalties due.

241. Jared Bernstein, *Why the GOP really wants to defund IRS*, WASH. POST (July 1, 2014), <http://www.washingtonpost.com/posteverything/wp/2014/07/01/why-the-gop-really-wants-to-defund-irs/?hpid=z11> [hereinafter Bernstein, *Why the GOP really wants to defund IRS*]. See also Associated Press, *IRS Head Says Budget Cuts Could Delay Tax Refunds*, *supra* note 1.

242. 2014 IRS DATA BOOK, *supra* note 7, at 68 tbl.29. Inflation-adjusted operating costs calculated by author using the BUREAU OF LABOR STATISTICS, *CPI*



increased by 11 percent from Fiscal Year 2005 to Fiscal Year 2014 (from 132.8 million returns to 147.8 million), and the number of business entity returns increased by 18 percent over that period (from 8.8 million returns to 10.4 million).<sup>243</sup>

**Table 7. Costs, Personnel, and U.S. Population, FY2005–FY2014**

<i>Fiscal year</i>	<i>Operating Costs (thousands of dollars)</i>	<i>Operating Costs (adjusted to 2014, thousands of dollars)</i>	<i>Number of Employees (full-time equivalent position realized)</i>	<i>U.S. population (thousands)</i>
2005	\$10,397,837	\$12,603,903	94,282	296,972
2006	\$10,605,845	\$12,454,292	91,717	299,835
2007	\$10,764,736	\$12,290,807	92,017	302,807
2008	\$11,307,223	\$12,432,835	90,647	305,554
2009	\$11,708,604	\$12,920,140	92,577	308,189
2010	\$12,353,344	\$13,411,606	94,711	310,390
2011	\$12,358,877	\$13,007,042	94,709	312,649
2012	\$12,059,409	\$12,434,542	90,280	314,908
2013	\$11,597,560	\$11,785,694	86,974	317,132
2014	\$11,591,007	\$11,591,007	84,133	319,804

Despite the IRS's ever-increasing responsibilities, its budget was slashed—by about 17 percent in real dollars between Fiscal Years 2010 and 2015.<sup>244</sup> For example, although President Obama requested \$12.861 billion for the IRS in Fiscal Year 2014, Congress appropriated just \$11.290 billion.<sup>245</sup> Worse still, President Obama's call for \$12.476 billion for the IRS in Fiscal

---

*Inflation Calculator*, [http://www.bls.gov/data/inflation\\_calculator.htm](http://www.bls.gov/data/inflation_calculator.htm) (last visited Aug. 13, 2015).

243. 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 9, 10.

244. *Id.* at vol. 1, at viii. See also GAO, IRS IS SCALING BACK ACTIVITIES, *supra* note 227, at 2 (noting that the IRS's annual appropriations have declined by \$1.2 billion [9.9 percent] since fiscal year 2010), 28 tbl.4 (showing the IRS budgets enacted for fiscal years 2009–2015 and the fiscal year 2016 budget request); FY 2015 IRS BUDGET RECOMMENDATION SPECIAL REPORT, *supra* note 2, at 8 (noting that the IRS saw its budget fall in nominal terms in three of the prior four fiscal years); Bryan Camp, *Overlooked costs of IRS budget cuts will hit taxpayers hardest*, THE CONVERSATION (Apr. 14, 2015), <https://theconversation.com/overlooked-costs-of-irs-budget-cuts-will-hit-taxpayers-hardest-39762>.

245. FY 2015 IRS BUDGET RECOMMENDATION SPECIAL REPORT, *supra* note 2, at 8 fig.1.

Year 2015<sup>246</sup> was met—three months into the fiscal year—with an appropriation of just \$10.95 billion, a three percent cut from Fiscal Year 2014.<sup>247</sup> President Obama’s request for \$12.931 billion for the IRS in Fiscal Year 2016<sup>248</sup> will almost certainly be pared by Congressional efforts to cut spending in general, and IRS spending in particular.<sup>249</sup>

---

246. *Id.*

247. BUDGET IN BRIEF 2016, *supra* note 1, at 61; Consolidated and Further Continuing Appropriations Act, 2015, Pub. L. No. 113–235, div. E, tit. I, 128 Stat. 2130, 2336–40 (2014); Rachael Bade, *Republicans seek to cripple IRS*, POLITICO (Dec. 11, 2014), <http://www.politico.com/story/2014/12/republicans-irs-regulations-113484.html> [hereinafter Bade, *Republicans seek to cripple IRS*]; Catherine Rampell, *As Congress cripples the IRS, tax rates are likely to rise*, WASH. POST (Dec. 15, 2014), [http://www.washingtonpost.com/opinions/catherine-rampell-as-congress-cripples-the-irs-tax-rates-are-likely-to-rise/2014/12/15/a7a30754-8476-11e4-b9b7-b8632ae73d25\\_story.html?wpisrc=nl\\_opin&wpmm=1](http://www.washingtonpost.com/opinions/catherine-rampell-as-congress-cripples-the-irs-tax-rates-are-likely-to-rise/2014/12/15/a7a30754-8476-11e4-b9b7-b8632ae73d25_story.html?wpisrc=nl_opin&wpmm=1); *IRS 2015 Budget Cut Is ‘Troubling Development,’ Koskinen Says*, 2014 TAX NOTES TODAY 243–12 (Dec. 17, 2014) [hereinafter *IRS 2015 Budget Cut Is ‘Troubling Development’*]; Matthew R. Madara, *IRS Facing 5 Percent Budget Cut From 2014 Levels, Olson Warns*, 145 TAX NOTES 1093 (Dec. 8, 2014); Stephen K. Cooper, *House Passes Omnibus Spending Bill; Senate Approval Expected*, 145 TAX NOTES 1195 (Dec. 15, 2014). *See also* William Hoffman, *IRS Budget Cuts ‘Will Be Visible’ in 2015*, Koskinen Warns, 145 TAX NOTES 1208 (Dec. 15, 2014); Daniel Nasaw & Brian McGill, *Funding Bill: The Losers*, WALL ST. J. (Dec. 10, 2014), <http://blogs.wsj.com/washwire/2014/12/10/funding-bill-the-losers>; Marc Heller, *Spending Bill Puts Squeeze, Restrictions on IRS for 2015*, 238 DAILY TAX REPORT (BNA), Dec. 11, 2014, at G-4.

248. BUDGET IN BRIEF 2016, *supra* note 1, at 61; *Internal Revenue Service Operations and the President’s Budget for Fiscal Year 2016, Hearing Before the Senate Committee on Finance*, 114th Cong. (Mar. 18, 2015) (statement of Commissioner of I.R.S. John A. Koskinen), <http://www.finance.senate.gov/imo/media/doc/2015%20JAK%20testimony%20SFC020315%20-%20FINAL.pdf>; *FY 2016 Budget Hearing – Internal Revenue Service*, 114th Cong. (Feb. 3, 2015) (statement of Commissioner of I.R.S. John A. Koskinen), <http://docs.house.gov/meetings/AP/AP23/20150318/103111/HHRG-114-AP23-Wstate-KoskinenJ-20150318.pdf> [hereinafter FY 2016 Statement of Commissioner John Koskinen].

249. *See, e.g.*, Kat Lucero, *Senate Appropriators Adopt Bill Cutting IRS Funding 4.3 Percent*, 148 TAX NOTES 387 (July 27, 2015); Eric Yoder, *House plan would cut IRS budget*, WASH. POST, June 10, 2015, <http://www.washingtonpost.com/blogs/federal-eye/wp/2015/06/10/house-plan-would-cut-irs-budget/> (“A bill to be considered by a House Appropriations subcommittee on Thursday would provide \$10.1 billion for the IRS, \$838 million below the current level and \$2.8 billion below President Obama’s request for the 2016 fiscal year.”) Rachael Bade, *Republicans take aim at IRS Budget*, POLITICO (June 10, 2015), <http://www.politico.com/story/2015/06/gop-irs-budget-118835.html> (“House GOP appropriators on Wednesday proposed chopping IRS resources almost [eight] percent, reducing the agency budget to \$10.1

Even before the Fiscal Year 2015 budget cut, the IRS was operating at the lowest budget level in ten years (adjusted for inflation); it had already absorbed more than one billion dollars in budget cuts since 2010; and it had reduced the number of employees by 17,000 since then.<sup>250</sup> In that regard, Figure 3 shows how recent IRS budget cuts have led to significant declines in IRS staffing for key enforcement occupations.<sup>251</sup> In response to the Fiscal Year 2015 budget cuts, the IRS implemented a hiring freeze, ceased most overtime pay, and further cut its travel budget.<sup>252</sup> The IRS expects to lose another 3000 full-time employees in Fiscal Year 2015.<sup>253</sup> All in all, the IRS is losing its

---

billion.”); David van den Berg, *Chaffetz Blasts IRS Requests for More Money for IT*, 2015 TAX NOTES TODAY 107–2 (June 4, 2015).

250. William Hoffman, *Koskinen Denies IRS Service Cuts Are a Protest Over Its Budget*, 146 TAX NOTES 339 (Jan. 19, 2015); Bade, *Republicans seek to cripple IRS*, *supra* note 247. See also I.R.S., *Prepared Remarks of John A. Koskinen Commissioner, Internal Revenue Service, Before the National Press Club* (Mar. 31, 2015), <http://www.irs.gov/uac/Newsroom/Commissioner-Koskinen-Speech-before-the-National-Press-Club>; U.S. GOV’T ACCOUNTABILITY OFF., GAO-14-534R, INTERNAL REVENUE SERVICE: ABSORBING BUDGET CUTS HAS RESULTED IN SIGNIFICANT STAFFING DECLINES AND UNEVEN PERFORMANCE 2 (2014), <http://www.gao.gov/assets/670/662681.pdf> [hereinafter U.S. GOV’T ACCOUNTABILITY OFF., INTERNAL REVENUE SERVICE: ABSORBING BUDGET CUTS]; U.S. GOV’T ACCOUNTABILITY OFF., GAO-14-605, IRS 2015 BUDGET: LONG-TERM STRATEGY AND RETURN ON INVESTMENT DATA NEEDED TO BETTER MANAGE BUDGET UNCERTAINTY AND SET PRIORITIES 1 (2014), <http://www.gao.gov/assets/670/664083.pdf> [hereinafter U.S. GOV’T ACCOUNTABILITY OFF., IRS 2015 BUDGET]; Bernstein, *Why the GOP really wants to defund IRS*, *supra* note 241; CHUCK MARR & JOEL FRIEDMAN, CTR. ON BUDGET & POL. PRIORITIES, CUTS IN IRS BUDGET HAVE COMPROMISED TAXPAYER SERVICE AND WEAKENED ENFORCEMENT (June 25, 2014), <http://www.cbpp.org/files/6-25-14tax.pdf> (estimating that the IRS cut its staff by 11 percent from 2011 to 2014) [hereinafter Marr & Friedman, *Cuts in IRS Budget Have Compromised Taxpayer Service and Weakened Enforcement*].

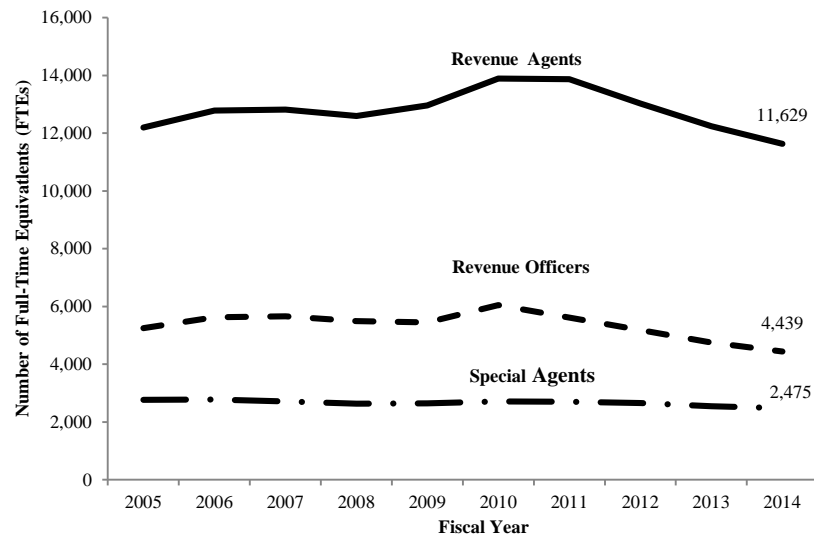
251. I.R.S., *Fiscal Year 2014 Enforcement and Service Results*, *supra* note 176, at 1. See also FY 2015 IRS BUDGET RECOMMENDATION SPECIAL REPORT, *supra* note 2, at 14 fig.6; U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2014-30-080, DECLINING RESOURCES HAVE CONTRIBUTED TO UNFAVORABLE TRENDS IN SEVERAL KEY AUTOMATED COLLECTION SYSTEM BUSINESS RESULTS (Sept. 18, 2014), <http://www.treasury.gov/tigta/auditreports/2014reports/201430080fr.pdf>; GAO, IRS IS SCALING BACK ACTIVITIES, *supra* note 227 (examining the effects of recent budget cuts on three IRS business units).

252. William Hoffman & Tom Kasprzak, *Omnibus Prompts IRS Hiring Freeze, Travel Cuts*, 145 TAX NOTES 1323 (Dec. 22, 2014). See also William Hoffman, *Year in Review: Koskinen’s Tough Job Likely to Get Tougher in 2015*, 146 TAX NOTES 18 (Jan. 7, 2015); *Koskinen Outlines How 2015 Budget Cuts Will Affect IRS Employees*, 2015 TAX NOTES TODAY 9–18 (Jan. 13, 2015) (reprinting a message of budget gloom from IRS Commissioner John A. Koskinen to IRS employees).

253. FY 2016 Statement of Commissioner John Koskinen, *supra* note 248.

most experienced workers, and the IRS is finding it harder and harder to replace them.<sup>254</sup> Budget cuts also make it harder for the IRS to manage and modernize its information technology.<sup>255</sup> All in all, the IRS is “doing less with less.”<sup>256</sup>

**Figure 3. Staffing for Key Enforcement Occupations**



While the IRS has been able to use increased electronic filing of tax returns, web-based services, and automation to become more efficient, those improvements have not been enough to offset the recent cuts in the IRS’s budget and personnel.<sup>257</sup> Unquestionably, the declines in personnel and resources have led to a decrease in the number of returns examined, and most examinations are now conducted by correspondence (rather than in face-to-

254. See, e.g., William Hoffman, *Almost Half of IRS Leadership Gone Since 2011, Koskinen Says*, 147 TAX NOTES 33 (Apr. 6, 2015).

255. See, e.g., U.S. GOV’T ACCOUNTABILITY OFF., *GAO-15-297, INFORMATION TECHNOLOGY: MANAGEMENT NEEDS TO ADDRESS REPORTING OF IRS INVESTMENTS’ COST, SCHEDULE, AND SCOPE INFORMATION* (2015), <http://www.gao.gov/assets/670/668665.pdf>.

256. William Hoffman, *IRS Reducing Services to Cope With Budget Cuts, GAO Says*, 148 TAX NOTES 511, 511 (Aug. 3, 2015).

257. Budget cuts have also contributed to a lower morale among IRS employees. See, e.g., Devin Leonard & Richard Rubin Hoffman, *IRS: An Emotional Audit: IRS Workers Are Miserable and Overwhelmed*, 68 DAILY TAX REP. (BNA), Apr. 9, 2015, at G2; *Year in Review: Koskinen’s Tough Job Likely to Get Tougher in 2015*, supra note 252; Pete Kasperowicz, *The Next Big Problem at the IRS: Low Worker Morale*, THE BLAZE (July 23, 2014), <http://www.theblaze.com/stories/2014/07/23/the-next-big-problem-at-the-irs-low-worker-morale/>.

face audits).<sup>258</sup> In that regard, Table 8 shows how recent budget cuts have led to a decline in the audit rates of large corporations (those with assets of more than \$10 million).<sup>259</sup> As already mentioned, 72 percent of the corporate tax underreporting was attributable to large corporations.<sup>260</sup>

**Table 8. Examination - Large Corporation Return Closures and Coverage Rates, by Fiscal Year (corporations with assets \$10 Million and Higher)**

	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
Total Returns Examined	10,829	10,578	9,644	9,406	9,536	10,207	10,459	10,752	9,876	7,858
Returns Filed in Prior CY	54,091	56,877	57,357	61,641	65,546	61,570	59,291	60,489	62,347	64,261
Coverage	20.0%	18.6%	16.8%	15.3%	14.5%	16.6%	17.6%	17.78%	15.84%	12.23%

Moreover, according to the IRS Oversight Board, “[u]ncertainty in the budget process and limited funding [have] hindered the IRS in addressing its long term strategic goals and initiatives.”<sup>261</sup> The IRS Oversight Board emphasized that:

Congress has increasingly called upon the IRS to implement the tax-related portions of new legislation. Although the IRS

258. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2014-30-062, TRENDS IN COMPLIANCE ACTIVITIES THROUGH FISCAL YEAR 2013, at 13–15 (Sept. 12, 2014), <http://www.treasury.gov/tigta/auditreports/2014reports/201430062fr.pdf> [hereinafter U.S. TREASURY, TRENDS IN COMPLIANCE ACTIVITIES 2013]. See *supra* Part III.B.3.c.

259. I.R.S., *Fiscal Year 2014 Enforcement and Service Results*, *supra* note 176, at 4. See also Marie Sapirie, *Business Tax Return Examinations Drop*, 146 TAX NOTES 1211 (Mar. 9, 2015); Transactional Records Access Clearinghouse (TRAC), *Audit Rates for Largest Corporations with Assets of \$250 Million or More*, <http://trac.syr.edu/tracirs/highlights/current/auditrateG.html> (last visited Aug. 9, 2015).

260. See *supra* note 162 and accompanying text.

261. FY 2015 IRS BUDGET RECOMMENDATION SPECIAL REPORT, *supra* note 2, at 5. See also IRS OVERSIGHT BD., FY2014 IRS BUDGET RECOMMENDATION SPECIAL REPORT (2013), [http://www.treasury.gov/IRSOB/reports/Documents/IRSOB\\_FY14%20IRS%20Budget\\_Web061413.pdf](http://www.treasury.gov/IRSOB/reports/Documents/IRSOB_FY14%20IRS%20Budget_Web061413.pdf) [hereinafter IRS OVERSIGHT BD., FY2014 BUDGET REPORT]; U.S. GOV’T ACCOUNTABILITY OFF., IRS 2015 BUDGET, *supra* note 250, at 15; IRS OVERSIGHT BD., FY2013 IRS BUDGET RECOMMENDATION SPECIAL REPORT (2012), [http://www.treasury.gov/IRSOB/reports/Documents/\\_IRSOB%20FY13%20BUDGET%20REPORT.pdf](http://www.treasury.gov/IRSOB/reports/Documents/_IRSOB%20FY13%20BUDGET%20REPORT.pdf); IRS OVERSIGHT BD., ANNUAL REPORT TO CONGRESS 2013 (2014), [http://www.treasury.gov/IRSOB/reports/Documents/IRSOB\\_Annual%20Report%202013.pdf](http://www.treasury.gov/IRSOB/reports/Documents/IRSOB_Annual%20Report%202013.pdf).

has been tasked with more and more responsibilities, it has not received sufficient funding to carry them out.<sup>262</sup>

The IRS Oversight Board's concern about the underfunding of the IRS has been echoed by many other government officials. Indeed, the National Taxpayer Advocate has repeatedly argued that underfunding is one of the most serious problems facing the IRS,<sup>263</sup> and the Internal Revenue Service Advisory Council has also expressed concern.<sup>264</sup>

Similarly, the Treasury Inspector General for Tax Administration (TIGTA) has also found that key examination and collection statistics showed declines from 2012 to 2013 as the result of budget cuts.<sup>265</sup> Examinations of individual tax returns declined by approximately five percent, and collection activities such as taxpayer liens, levies, and property seizures declined approximately 33 percent.<sup>266</sup> TIGTA's analysis of IRS data also showed that reduced funding affected key customer service efforts.<sup>267</sup> Customer service trends showed that the level of service—defined as the relative success rate of taxpayers calling the IRS toll-free assistance lines—declined from 70 percent

---

262. FY 2015 IRS BUDGET RECOMMENDATION SPECIAL REPORT, *supra* note 2, at 11.

263. *See, e.g.*, 2013 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at ix, 21; NAT'L TAXPAYER ADVOCATE, 2011 ANNUAL REPORT TO CONGRESS (2012) at vol. 1, at 3, <http://www.taxpayeradvocate.irs.gov/userfiles/file/IRS%20TAS%20ARC%202011%20VOL%201.pdf> [hereinafter 2011 ANNUAL REPORT TO CONGRESS]; 2011 ANNUAL REPORT TO CONGRESS, *supra*, at vol. 2, at 1, [http://www.irs.gov/file\\_source/pub/tas/irs\\_tas\\_arc\\_2011\\_vol\\_2.pdf](http://www.irs.gov/file_source/pub/tas/irs_tas_arc_2011_vol_2.pdf).

264. *See, e.g.*, I.R.S. ADVISORY COUNCIL, 2014 PUBLIC REPORT 9 (2014), [http://www.irs.gov/file\\_source/PUP/taxpros/2014-IRSAC-Full-Report.pdf](http://www.irs.gov/file_source/PUP/taxpros/2014-IRSAC-Full-Report.pdf); I.R.S. ADVISORY COUNCIL, 2013 PUBLIC REPORT 7–12 (2013), <http://www.irs.gov/pub/irs-utl/2013%20IRSAC%20Full%20Report.pdf>; I.R.S. ADVISORY COUNCIL, 2011 PUBLIC REPORT 9 (2011), [http://www.irs.gov/pub/irs-utl/irsac\\_2011\\_report\\_for\\_irs.gov\\_revised\\_12-12-11.pdf](http://www.irs.gov/pub/irs-utl/irsac_2011_report_for_irs.gov_revised_12-12-11.pdf).

265. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2014-10-025, IMPLEMENTATION OF FISCAL 2013 SEQUESTRATION BUDGET REDUCTIONS (June 12, 2014), <http://www.treasury.gov/tigta/auditreports/2014reports/201410025fr.pdf> [hereinafter U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., IMPLEMENTATION OF FISCAL 2013 SEQUESTRATION BUDGET REDUCTIONS]. *See also* U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2015-30-035, REDUCED BUDGETS AND COLLECTION RESOURCES HAVE RESULTED IN DECLINES IN TAXPAYER SERVICE, CASE CLOSURES, AND DOLLARS COLLECTED i (May 8, 2015), <http://www.treasury.gov/tigta/auditreports/2015reports/201530035fr.pdf> (“Since Fiscal Year 2010, decreases in the budget have resulted in the reduction of 21 percent of Automated Collection Service (ACS) contact representatives and 28 percent of Field Collection revenue officers.”).

266. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., IMPLEMENTATION OF FISCAL 2013 SEQUESTRATION BUDGET REDUCTIONS, *supra* note 265, at 6.

267. *Id.* at 9.

in 2009 to just 61 percent in 2013.<sup>268</sup> The average telephone call wait time nearly doubled from 8.8 minutes to 16.8 minutes over the period from Fiscal Year 2009 to mid-March 2014.<sup>269</sup>

Things are certainly not going to get any better on the customer service front. In December of 2014, IRS Commissioner John A. Koskinen noted that that “only about 50 percent of the taxpayers who call can reach us on the phone” and “some 24 million Americans may not be able to reach us for help.”<sup>270</sup> With the Fiscal Year 2015 cuts now in place, the level of phone service could be as low as 43 percent, and the IRS may handle up to 1.9 million fewer pieces of correspondence than it did in FY 2014.<sup>271</sup> Worse still, IRS budget cuts are likely to hit low-income and unsophisticated taxpayers especially hard.<sup>272</sup> All in all, National Taxpayer Advocate Nina E. Olson believes that “taxpayer service has reached unacceptably low levels and is getting worse.”<sup>273</sup>

Many in the private sector also lament the underfunding of the IRS.<sup>274</sup> For example, in a letter to members of the House and Senate Appropriations

---

268. *Id.* at 9 fig.4. See also *FY16 Treasury Department Budget, Hearing Before the Subcommittee on Financial Services and General Government of the Senate Committee on Appropriations*, 114th Cong. (2015) (statement of the Treasury Inspector General for Tax Administration Russell George), <http://www.appropriations.senate.gov/sites/default/files/hearings/FSGG%20Inspector%20General%20for%20Tax%20Administration%20George%20Testimony%20030315.pdf>; U.S. GOV'T ACCOUNTABILITY OFF., GAO-15-420R, INTERNAL REVENUE SERVICE: OBSERVATIONS ON IRS'S OPERATIONS, PLANNING, AND RESOURCES (2015), <http://www.gao.gov/assets/670/668769.pdf>; U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-133, 2013 TAX FILING SEASON: IRS NEEDS TO DO MORE TO ADDRESS THE GROWING IMBALANCE BETWEEN THE DEMAND FOR SERVICES AND RESOURCES (2013), <http://www.gao.gov/assets/660/659777.pdf>.

269. U.S. GOV'T ACCOUNTABILITY OFF., INTERNAL REVENUE SERVICE: ABSORBING BUDGET CUTS, *supra* note 250, at 2.

270. *IRS 2015 Budget Cut Is Troubling Development*, *supra* note 247.

271. 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at ix.

272. Low-income taxpayers may also suffer if the budget cuts result in a decline in grants for the Low-Income Taxpayer Clinics that help serve them.

273. 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 3; see also William Hoffman, *IRS Must Balance Service With Technology*, *TPC Panelists Say*, 147 TAX NOTES 143 (Apr. 13, 2015).

274. See, e.g., Henry J. Aaron, *You Get What You Pay For: Lessons From the IRS Scandal*, YAHOO! FINANCE, May 31, 2013, <http://finance.yahoo.com/blogs/the-exchange/pay-lessons-irs-scandal-234428300.html>; Bernstein, *Why the GOP really wants to defund IRS*, *supra* note 241; Marr & Friedman, *Cuts in IRS Budget Have Compromised Taxpayer Service and Weakened Enforcement*, *supra* note 250; Catherine Rampell, *Stop starving the beast of the IRS*, WASH. POST (July 1, 2014), [http://www.washingtonpost.com/opinions/catherine-rampell-stop-starving-the-beast-of-the-irs/2014/07/01/d3f819d6-008f-11e4-8fd0-3a663dfa68ac\\_story.html](http://www.washingtonpost.com/opinions/catherine-rampell-stop-starving-the-beast-of-the-irs/2014/07/01/d3f819d6-008f-11e4-8fd0-3a663dfa68ac_story.html); George

Committees, the Chair of the Section of Taxation of the American Bar Association wrote that “the recent trend of funding reductions for the [IRS] is negatively impacting its ability to properly serve taxpayers and enforce the tax laws that Congress enacts.”<sup>275</sup> The American Institute of Certified Public Accountants has expressed similar concerns.<sup>276</sup>

Pulitzer Prize-winning journalist David Cay Johnston has noted that “it makes no economic sense to trim the ranks of auditors who generate [revenues of] more than 100 times their annual salaries.”<sup>277</sup> Professor Diane Fahey notes that since the first enactment of the income tax, financial elites who recognized that restricting government funding would reduce the federal

---

Yin, *The Most Critical Issue Facing Tax Administration Today -- And What to Do About It* (Virginia Law and Econ. Research Paper No. 2014-11, June 27, 2014), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2459592](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2459592) [hereinafter Yin, *The Most Critical Issue Facing Tax Administration Today -- And What to Do About It*]; George K. Yin, *Saving the IRS*, 143 TAX NOTES 589 (May 5, 2014); *Transcript Available of Tax Analysts' Panel on the IRS Budget*, 2012 TAX NOTES TODAY 58-56 (Mar. 23, 2012) (transcript of a March 23, 2012 panel discussion cosponsored by Tax Analysts and Georgetown University Law Center on budgetary challenges facing the IRS with speakers including Lisa Zarlenga of Treasury's Office of Tax Counsel, National Taxpayer Advocate Nina E. Olson, and former IRS Commissioner Fred T. Goldberg, Jr.).

275. Michael Hirschfeld, Chair, Section of Taxation, American Bar Association, *Letter to various members of the U.S. Senate and House Appropriations committees* (Feb. 10, 2014), <http://www.americanbar.org/content/dam/aba/administrative/taxation/policy/021014comments.pdf>. See also Armando Gomez, *Investing in the Tax System (From the Chair)*, 34 A.B.A. SECTION OF TAXATION NEWS QUARTERLY 3 (Winter 2015), <http://www.americanbar.org/content/dam/aba/publishing/newsquarterly/15win/gomez-ftc-investing-in-the-tax-system-nq-winter-2015.pdf>.

276. Jeffrey A. Porter, Chair, AICPA Tax Executive Committee, *Letter to various members of the U.S. Senate and House Appropriations committees* (Sept. 4, 2013), <http://www.aicpa.org/Advocacy/Tax/DownloadableDocuments/2013-9-04-Appropriations-AICPA-Position-on-IRS-Budget.pdf>. See also *Written Statement of the American Institute of Certified Public Accountants for the record of the February 5, 2014 Hearing of the House Committee on Ways and Means Subcommittee on Oversight on the State of the Internal Revenue Service* (Feb. 19, 2014), <http://www.aicpa.org/Advocacy/Tax/TaxLegislationPolicy/DownloadableDocuments/AICPA-WRITTEN-STATEMENT-FEB-5-2014-hwmc-OVERSIGHTsubcomte2%2018%2014.pdf>.

277. David Cay Johnston, *Honey, they shrunk the IRS*, REUTERS (Jan. 17, 2012), <http://blogs.reuters.com/david-cay-johnston/2012/01/17/honey-they-shrunk-the-irs> (“The highest-paid IRS auditors make \$71 an hour. Based on a 2,080-hour work year, that works out to around \$19 million of lost revenue annually for every senior corporate auditor position cut from the payroll.”). See also David Cay Johnston, *The Cost of Shrinking IRS Budget*, 147 TAX NOTES 1043 (June 1, 2015); David Cay Johnston, *The Tax Policy Budget Shrinks*, 139 TAX NOTES 211 (Apr. 8, 2013).



government's influence and power have acted to undermine the income tax and the government's ability to collect it.<sup>278</sup> Whatever the motivation for the recent budget cuts was, the IRS has a big job to do and less and less money to do it with. Many observers expected that the IRS would have a "miserable" 2015 filing season (for 2014 tax returns).<sup>279</sup> As it turned out, however, the 2015 tax filing season went pretty smoothly, although because of budget cuts, the IRS was "unable to provide adequate levels of taxpayer service."<sup>280</sup> In that regard, however, Republicans in Congress generally believe that the IRS could provide better customer service if it did a better job of allocating its resources.<sup>281</sup>

## B. *The Tax Code is Increasingly Complex*

### 1. *Endless Legislation Adds to Complexity*

Much of the complexity in tax administration comes from Congress constantly tinkering with, and adding to, the Internal Revenue Code. The

---

278. Diane L. Fahey, *The Movement to Destroy the Income Tax and the IRS: Who is Doing It and How They are Succeeding*, 15 FLA. TAX REV. 157, 159 (2014).

279. Jeanne Sahadi, "Miserable" tax season could be worst in years, CNN MONEY (Jan. 5, 2015), <http://money.cnn.com/2015/01/05/pf/taxes/tax-filing-irs/>; Ashlea Ebeling, *IRS Commissioner Predicts Miserable 2015 Tax Filing Season*, FORBES (Nov. 4, 2014), <http://www.forbes.com/sites/ashleaebeling/2014/11/04/irs-commissioner-predicts-miserable-2015-tax-filing-season/>; William Hoffman, *Koskinen, Olson Share Fears Over 2015 Filing Season*, 145 TAX NOTES 636 (Nov. 10, 2014); Hoffman, *Koskinen Warns of House IRS Budget's Impact in 2015*, *supra* note 147. *But see* Christopher Bergin, *Worst Filing Season in 30 Years? Probably Not*, 146 TAX NOTES 551 (Jan. 26, 2015).

280. *2015 Tax Filing Season, Hearing Before the House Committee on Ways and Means Subcommittee on Oversight*, 114th Cong. (statement of Commissioner of IRS John A. Koskinen), <http://www.irs.gov/uac/Written-Testimony-of-IRS-Commissioner-Koskinen-before-the-House-Ways-and-Means-Committee>. *See also* NAT'L TAXPAYER ADVOCATE, FISCAL YEAR 2016 OBJECTIVES REPORT TO CONGRESS (2015) at vol. 1, at 8, [http://www.taxpayeradvocate.irs.gov/Media/Default/Documents/2016-JRC/Volume\\_1.pdf](http://www.taxpayeradvocate.irs.gov/Media/Default/Documents/2016-JRC/Volume_1.pdf); William Hoffman, *IRS IT Delivers, Phones Not So Much, as Filing Season Ends*, 147 TAX NOTES 251 (Apr. 20, 2015).

281. Kat Lucero, *House Panel Criticizes IRS for Mismanagement of Resources*, 147 TAX NOTES 387 (Apr. 27, 2015); U.S. H.R. COMM. ON WAYS & MEANS MAJORITY STAFF REPORT, DOING LESS WITH LESS, *supra* note 227 (criticizing IRS spending decisions). *See also* Chris Edwards, *IRS Budget Cuts and Tax Filing*, CATO AT LIBERTY, (Apr. 8, 2015), <http://www.cato.org/blog/irs-budget-cuts-tax-filing>.

Internal Revenue Code already includes nearly four million words.<sup>282</sup> There were more than 15,000 tax code changes between 1986 and 2010,<sup>283</sup> and more than 4,680 changes from 2000 to 2012.<sup>284</sup> Late-in-the-year tax legislation adds significant burdens on the IRS to prepare forms in time for the filing season.<sup>285</sup> In addition, numerous federal tax provisions expire each year,<sup>286</sup> and inflation adjustments integral to many tax provisions require the IRS to change many of its publications every year.<sup>287</sup> Pertinent here, dozens of tax provisions that expired at the end of 2013 were ultimately restored by Congress retroactively for the 2014 tax year, but not until the end of December of that year.<sup>288</sup>

---

282. 2012 ANNUAL REPORT TO CONGRESS, *supra* note 40, at vol. 1, at 3, 6. See also U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-652R, DIFFERENCES IN DEFINITIONS AND RULES IN THE TAX CODE (2014), <http://www.gao.gov/assets/670/664890.pdf> (noting that definitions for the same or similar terms can differ from one Code provision to another). To be sure, a shorter tax code would not necessarily be less complex.

283. THE PRESIDENT'S ECON. RECOVERY ADVISORY BD., THE REPORT ON TAX REFORM OPTIONS: SIMPLIFICATION, COMPLIANCE, AND CORPORATE TAXATION 3 (2010), [http://www.whitehouse.gov/sites/default/files/microsites/PERAB\\_Tax\\_Reform\\_Report.pdf](http://www.whitehouse.gov/sites/default/files/microsites/PERAB_Tax_Reform_Report.pdf) [hereinafter THE PRESIDENT'S ECON. RECOVERY ADVISORY BD., THE REPORT ON TAX REFORM OPTIONS: SIMPLIFICATION, COMPLIANCE, AND CORPORATE TAXATION].

284. 2012 ANNUAL REPORT TO CONGRESS, *supra* note 40, at vol. 1, at 6.

285. See, e.g., U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2013-40-124, LATE LEGISLATION DELAYED THE FILING OF TAX RETURNS AND ISSUANCE OF REFUNDS FOR THE 2013 FILING SEASON (Sept. 30, 2013), <http://www.treasury.gov/tigta/auditreports/2013reports/201340124fr.pdf>. See also Seth H. Giertz & Jacob Feldman, *The Costs of Tax Policy Uncertainty and the Need for Tax Reform*, 138 TAX NOTES 951 (Feb. 25, 2013).

286. See, e.g., STAFF OF THE J. COMM. ON TAX'N, JCX-1-15, LIST OF EXPIRING FEDERAL TAX PROVISIONS 2014–2025 (2015), [https://www.jct.gov/publications.html?func=download&id=4683&chk=4683&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4683&chk=4683&no_html=1) [hereinafter STAFF OF THE J. COMM. ON TAX'N, LIST OF EXPIRING FEDERAL TAX PROVISIONS 2014–2025]. See also IRS Commissioner John A. Koskinen, *Letter to the Chairman of the Senate Finance Committee* (Oct. 6, 2014) (urging Congress to act “expeditiously” on whether to extend the tax provisions that expired at the end of 2013 so as not to delay the 2015 tax filing season [for 2014 tax returns]), 2014 TAX NOTES TODAY 195–25 (Oct. 6, 2014); Victor Fleischer, *Commentary, Tax Extenders*, 67 TAX L. REV. 613 (2014).

287. See, e.g., I.R.S., Forms & Publications, *supra* note 214.

288. See, e.g., Tax Increase Prevention Act of 2014, Pub. L. No. 113–295, 128 Stat. 4010 (2014) (signed by the President Dec. 19, 2014); STAFF OF THE J. COMM. ON TAX'N, JCX-107-14R, ESTIMATED REVENUE EFFECTS OF H.R. 5771, THE “TAX INCREASE PREVENTION ACT OF 2014,” SCHEDULED FOR CONSIDERATION BY THE HOUSE OF REPRESENTATIVES ON DECEMBER 3, 2014 (Dec. 3, 2014), [https://www.jct.gov/publications.html?func=download&id=4677&chk=4677&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4677&chk=4677&no_html=1).

Our complex tax system imposes a wide range of recordkeeping, planning, computational, and filing requirements on taxpayers.<sup>289</sup> The cost of complying with the personal and corporate tax systems alone is at least one percent of gross domestic product, and the economic efficiency costs are estimated to be even larger, on the order of five percent of gross domestic product (GDP).<sup>290</sup>

Of course, some taxpayers choose more complicated tax situations, for example, by participating in partnerships with special allocations or engaging in estate tax planning through a variety of trust vehicles. Although we need not feel sorry for taxpayers who choose more complicated tax situations to minimize their tax liabilities, we do need to acknowledge that those more complicated situations also impose additional burdens on the IRS.

## 2. *The IRS has Increasing Responsibilities*

Despite the declining funding provided to the IRS,<sup>291</sup> Congress frequently increases the IRS's responsibilities by calling on it to implement the tax-related portions of major new legislation and by increasing the number and complexity of tax provisions. For example, in recent years, the IRS has been called upon to implement the tax-related portions of both the Patient Protection and Affordable Care Act (ACA) and the Foreign Account Tax Compliance Act (FATCA).<sup>292</sup>

### a. *An Increasing Number of Tax Expenditures*

As already mentioned, in addition to having provisions that raise

---

289. Most notably, taxpayers are generally required to file annual income tax returns. I.R.C. § 6012.

290. TAX GAP: COMPLEXITY AND TAXPAYER COMPLIANCE, *supra* note 96, at 5. See also William Hoffman, *Compliance Costs Up to \$1.5 Trillion, Heritage Panelists Say*, 145 TAX NOTES 896 (Nov. 24, 2014); STAFF OF THE J. COMM. ON TAX'N, JCX-49-15, COMPLEXITY IN THE FEDERAL TAX SYSTEM (2015), [https://www.jct.gov/publications.html?func=download&id=4738&chk=4738&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4738&chk=4738&no_html=1).

291. See *supra* Part IV.A.

292. IRS OVERSIGHT BD., FY2014 BUDGET REPORT, *supra* note 261, at 7; U.S. TREASURY, TRENDS IN COMPLIANCE ACTIVITIES 2013, *supra* note 258, at 4–5; U.S. TREASURY INSPECTOR GENERAL FOR TAX ADMIN., REF. NO. 2015-43-030, AFFORDABLE CARE ACT: ASSESSMENT OF INTERNAL REVENUE SERVICE PREPARATIONS TO ENSURE COMPLIANCE WITH MINIMUM ESSENTIAL COVERAGE AND SHARED RESPONSIBILITY PAYMENT REQUIREMENTS (Mar. 30, 2015), <http://www.treasury.gov/tigta/auditreports/2015reports/201543030fr.pdf> (stating the IRS will be unable to ensure that all taxpayers claiming the personal tax credit bought health insurance through an exchange as required).

revenue, the Internal Revenue Code includes numerous tax expenditures that are designed to promote a variety of economic and social welfare goals.<sup>293</sup> Over the years, the number of tax expenditures has increased markedly, and new one are added almost every year.<sup>294</sup> For example, to bolster the residential real estate market during the 2008 financial crisis, Congress enacted a complicated new first-time homebuyer credit,<sup>295</sup> which presented significant challenges for both the IRS and taxpayers.<sup>296</sup> The problem is that administering provisions like the first-time homebuyer credit forces the IRS to divert resources from its core work of collecting revenue.<sup>297</sup>

*b. A More Detailed Example: Energy-related Tax Expenditures*

The responsibilities for administering economic and social welfare programs can be quite significant. For example, consider the IRS's responsibility for providing guidance and enforcement for various energy-

---

293. See *supra* notes 86–96 and accompanying text.

294. See, e.g., William McBride, *A Brief History of Tax Expenditures*, TAX FOUNDATION (2013), <http://taxfoundation.org/article/brief-history-tax-expenditures>; STAFF OF THE J. COMM. ON TAX'N, JCX-15-11, BACKGROUND INFORMATION ON TAX EXPENDITURE ANALYSIS AND HISTORICAL SURVEY OF TAX EXPENDITURE ESTIMATES 16 fig. 1 (Feb. 28, 2011), [https://www.jct.gov/publications.html?func=download&id=3740&chk=3740&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=3740&chk=3740&no_html=1); Allison Rogers & Eric Toder, *Trends in Tax Expenditures, 1985-2016*, TAX POLICY CTR. (2011), <http://www.taxpolicycenter.org/UploadedPDF/412404-Tax-Expenditure-Trends.pdf>; CONG. RESEARCH SERV., TAX EXPENDITURES: COMPENDIUM OF BACKGROUND MATERIAL ON INDIVIDUAL PROVISIONS, SEN. REP. NO. 45 (2d Sess. 2012), <http://www.gpo.gov/fdsys/pkg/CPRT-112SPRT77698/pdf/CPRT-112SPRT77698.pdf>.

295. I.R.C. § 36 (added by the Housing and Economic Recovery Act of 2008, Pub. L. No. 110–289, § 3011(a), 122 Stat. 2654, 2888 (2008)).

296. See, e.g., *Filing Season Update: Current IRS Issues, Hearing Before the Senate Committee on Finance*, 111th Cong. 5-10 (2010) (statement of National Taxpayer Advocate Nina E. Olson), <http://www.finance.senate.gov/imo/media/doc/041510notest1.pdf>.

297. *Id.* at 10; U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2010-41-128, RECOVERY ACT: VERIFYING ELIGIBILITY FOR CERTAIN NEW TAX BENEFITS WAS A CHALLENGE FOR THE 2010 FILING SEASON (Sept. 30, 2010), <http://www.treasury.gov/tigta/auditreports/2010reports/201041128fr.pdf>. The IRS also had some work to do in connection with the 2009 “Cash for Clunkers” program. See, e.g., NAT'L AUTOMOTIVE DEALERS ASSOC., Automotive Alert 1, *Consumer Assistance to Recycle and Save (CARS) Act of 2009: Taxability of Payments to Dealerships* (2009), [https://www.nada.org/NR/rdonlyres/877BB9FB-3381-4715-9AC5-CAABF6E31969/0/IRS\\_MVTA\\_Alert\\_CARS\\_Payments\\_072009.pdf](https://www.nada.org/NR/rdonlyres/877BB9FB-3381-4715-9AC5-CAABF6E31969/0/IRS_MVTA_Alert_CARS_Payments_072009.pdf) (discussing the tax treatment of the CARS tax credits).

related tax expenditures.<sup>298</sup> Energy-related tax expenditures constitute a significant portion of the federal support for energy—about 44 percent in 2010.<sup>299</sup> Energy-related tax expenditures range from the venerable intangible drilling costs deduction<sup>300</sup> to the panoply of recent renewable energy tax credits, including the production tax credit (PTC)<sup>301</sup> and the investment tax credit (ITC).<sup>302</sup> The fossil fuel tax incentives, which primarily consist of expensing and accelerated depreciation type provisions, including generous percentage depletion allowances,<sup>303</sup> do not expire and have been relatively stable over time, although Congress has limited the availability of some of the benefits to independent oil producers.<sup>304</sup>

*i. Incentives for Renewable Energy*

The renewable energy tax expenditures, on the other hand, have expired multiple times and have undergone some significant changes.<sup>305</sup> The complexity and administrative burdens of the renewable energy tax credits stem from the difficulty of reaping the benefits from the credits when the renewable energy developer itself does not have taxable income. Energy projects frequently operate at a loss in the early years of development, in part because of the nature of new businesses, and, in part because of accelerated depreciation deductions, which provide larger deductions in the early years of a project. Congress does not allow the “sale” of tax credits, so energy projects must be structured to “share” the tax credits with investors that have positive tax liability (i.e., with “tax equity investors”). To reap the benefits of tax credits, project developers enter into partnership or sale-leaseback transactions with corporate investors that have income to shelter.

---

298. See generally STAFF OF THE J. COMM. ON TAX’N, PRESENT LAW AND ANALYSIS OF ENERGY-RELATED TAX EXPENDITURES, *supra* note 92.

299. U.S. ENERGY INFORMATION ADMIN., DIRECT FEDERAL FINANCIAL INTERVENTIONS AND SUBSIDIES IN ENERGY IN FISCAL YEAR 2010, at xiii (2011), <http://www.eia.gov/analysis/requests/subsidy/pdf/subsidy.pdf>.

300. I.R.C. § 263(c).

301. I.R.C. § 45.

302. I.R.C. § 48.

303. I.R.C. § 613.

304. See, e.g., STAFF OF THE J. COMM. ON TAX’N, JCX-27-11, DESCRIPTION OF PRESENT LAW AND SELECT PROPOSALS RELATING TO THE OIL AND GAS INDUSTRY (2011), <https://www.jct.gov/publications.html?func=startdown&id=3787>.

305. See, e.g., STAFF OF THE J. COMM. ON TAX’N, PRESENT LAW AND ANALYSIS OF ENERGY-RELATED TAX EXPENDITURES, *supra* note 92; STAFF OF THE J. COMM. ON TAX’N, LIST OF EXPIRING FEDERAL TAX PROVISIONS 2014–2025, *supra* note 286; Felix Mormann, *Beyond Tax Credits – Smarter Tax Policy for a Cleaner, More Democratic Energy Future*, 31 YALE J. ON REG. 303 (2014).

For example, in a so-called partnership flip transaction, one or more tax equity investors are brought in as partners to own a project with the developer. This is the only structure that is available for sharing PTCs, because the PTC rules require the owner of the facility to be the operator of the facility. A partnership flip structure may also be used to allocate ITCs. Alternatively, in a sale-leaseback transaction, the energy project would be sold to the tax investor, and leased back to the project developer, thus transferring the tax benefits to the investor/owner. Sale-leaseback transactions may only be used with ITCs, not with PTCs.

These complex transactions create uncertainty for the taxpayers and enforcement headaches for the IRS. Partnerships are notorious for non-compliance and are difficult to audit effectively;<sup>306</sup> and, in any event, the IRS only audits 0.43 percent of partnerships.<sup>307</sup> The IRS has provided safe harbor guidance on both partnership flips and sale-leasebacks, which eases taxpayer concerns about certainty to some degree.<sup>308</sup>

In the wake of the financial crisis of 2008 and 2009, Congress created new incentive grants in lieu of the renewable energy tax credits.<sup>309</sup> A report by the National Renewable Energy Laboratory found that during the financial crisis, the number of tax equity investors decreased from nearly 20 to just five.<sup>310</sup> Wanting to stimulate renewable energy projects and recognizing that investors had become scarce, Congress added the new incentive grants in lieu of ITCs in the American Recovery and Reinvestment Act of 2009 (ARRA).<sup>311</sup> While the incentive grant was not technically a tax benefit, the amount of the grant was determined by the amount the taxpayer would have received as an ITC, and the IRS was made responsible for administering the grant program. As of May 10, 2013, the Treasury, through the IRS, had awarded 9,016 grants

---

306. See, e.g., U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-53, PARTNERSHIPS AND S CORPORATIONS: IRS NEEDS TO IMPROVE INFORMATION TO ADDRESS TAX COMPLIANCE (2014), <http://www.gao.gov/assets/670/663185.pdf>.

307. See *supra* note 181 and accompanying text.

308. See, e.g., Rev. Proc. 2007-65, 2007-2 C.B. 967 (discussing partnership flips); Rev. Proc. 2001-28, 2001-1 C.B. 38 (discussing sale-leasebacks).

309. See, e.g., U.S. DEP'T OF TREASURY, *Recovery Act: 1603 Program: Payments for Specified Energy Property in Lieu of Tax Credits*, <http://www.treasury.gov/initiatives/recovery/Pages/1603.aspx> (last updated Jan. 21 2015).

310. MICHAEL MENDELSON & JOHN HARPER, NAT'L RENEWABLE ENERGY LAB. TECH. REP. NREL/TP-6A20-53720, § 1603 TREASURY GRANT EXPIRATION: INDUSTRY INSIGHT ON FINANCING AND MARKET IMPLICATIONS 3 (June 2012), <http://www.nrel.gov/docs/fy12osti/53720.pdf>.

311. American Recovery and Reinvestment Act of 2009, Pub. L. No. 111-5, § 1603, 123 Stat. 115, 344-66 (2009). The grant program was extended until the end of 2011, under the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, Pub. L. No. 111-312, § 707, 124 Stat. 3296, 3312 (2010).

totaling \$18.5 billion.<sup>312</sup> The administration's enforcement concerns regarding the administration of this grant program were: 1) whether taxpayers had claimed both ITCs or PTCs and a Section 1603 grant for the same property; and 2) whether leasing transactions were used to overstate fair market value and inflate the grant amount.<sup>313</sup>

As noted above, renewable energy tax incentives have expired repeatedly.<sup>314</sup> As a consequence, determining whether an energy project is eligible for a benefit can be challenging for both taxpayers and the IRS. For example, when Congress extended the PTC for wind energy projects in early 2013, it changed the long-standing eligibility criteria from "originally placed in service" to "the construction of which begins."<sup>315</sup> This change, although it had some precedent based on the eligibility criteria for the section 1603 grant, required more guidance from the IRS and will likely lead to more compliance burdens on both taxpayers and the IRS.<sup>316</sup>

Needless to say, it is particularly challenging for the IRS to be involved in awarding benefits to taxpayers based on technical criteria about which the IRS has little technical expertise. For example, Congress limited the amount of credits available for the qualifying advanced energy project credit to a total of \$2.3 billion.<sup>317</sup> Although the IRS was expected to act in consultation with the U.S. Department of Energy to award certifications for the credit, the IRS nonetheless ran into problems.<sup>318</sup> A Treasury Inspector General for Tax Administration study found that the IRS issued guidance using simplified criteria that were inconsistent with the statutory language, and it used program policy factors without any clear statutory authority to do so which may have affected the ranking of projects.<sup>319</sup> The tax credits for

---

312. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2014-IE-R006, REVIEW OF SECTION 1603 GRANTS IN LIEU OF ENERGY INVESTMENT TAX CREDIT 1 (Dec. 17, 2013), <http://www.treasury.gov/tigta/iereports/2014reports/2014IER006fr.pdf>.

313. *Id.* at 1–2.

314. *See supra* note 305 and accompanying text.

315. American Taxpayer Relief Act of 2012, Pub. L. No. 112–240, § 407(a)(3)(C), 126 Stat. 2313, 2340–41 (2013).

316. For example, the change has already required three notices from the IRS: Notice 2013–29, 2013–1 C.B. 1085, *clarified by* Notice 2013–60, 2013–2 C.B. 431, *clarified by* Notice 2014–46, 2014–35 I.R.B. 520.

317. I.R.C. § 48C(d)(1)(B).

318. *See generally* U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2013-40-029, ASSESSMENT OF THE INTERNAL REVENUE SERVICE'S INTERPRETATION OF SECTION 1302 OF THE RECOVERY ACT: QUALIFYING ADVANCED ENERGY PROJECT CREDIT (Mar. 21, 2013), <http://www.treasury.gov/tigta/auditreports/2013reports/201340029fr.pdf>.

319. *Id.*

advanced coal and gasification projects have led to many of the same kinds of administrative challenges.<sup>320</sup>

ii. *Energy Tax Incentives for Consumers*

Energy tax incentives for consumers have also increased the administrative burden on the IRS.<sup>321</sup> For example, the Treasury Inspector General for Tax Administration (TIGTA) identified several key elements of eligibility for the residential energy tax credit that the IRS was unable to verify under its current procedures: 1) whether the taxpayer purchased a qualified energy saving product or made energy efficient improvements or both; 2) the cost of purchasing and implementing the energy saving improvement; 3) whether the energy saving improvements were made to the taxpayer's principal residence; and 4) the time period during which the costs were incurred.<sup>322</sup> In some cases, the IRS even had the data to identify erroneous claims, but failed to do so.<sup>323</sup>

C. *The Tax Controversy Process is Unnecessarily Complicated*

As we have seen, the tax controversy process is quite complicated.<sup>324</sup> The many different types of administrative appeal mechanisms could be much better coordinated, and one really has to wonder why tax disputes can be heard by so many different courts. Moreover, the current system is highly technical, and many taxpayers can have multiple bites of the apple (e.g., in proceedings to contest the liability and in subsequent proceedings to contest collection activities). Both the IRS and taxpayers would benefit from a more streamlined system of tax dispute resolution. In general, every taxpayer should have one opportunity for an independent administrative review of IRS determinations and one opportunity for judicial review in addition to the appeals allowed by the regular judicial process.

---

320. I.R.C. §§ 48A, 48B; I.R.S., *Audit Technique Guide for Sections 48A and 48B – Advanced Coal and Gasification Project*, <http://www.irs.gov/Businesses/Audit-Technique-Guide-for-Sections-48A-and-48B---Advanced-Coal-and-Gasification-Project-Credits> (last updated Jan. 22, 2015).

321. See, e.g., I.R.S., *Energy Incentives for Individuals in the American Recovery and Reinvestment Act*, <http://www.irs.gov/uac/Energy-Incentives-for-Individuals-in-the-American-Recovery-and-Reinvestment-Act> (last updated Apr. 23, 2015) (showing lots of recent guidance).

322. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2011-41-038, PROCESSES WERE NOT ESTABLISHED TO VERIFY ELIGIBILITY FOR RESIDENTIAL ENERGY CREDITS 4 (Apr. 19, 2011), <http://www.recovery.gov/arra/Accountability/inspectors/Documents/201141038fr.pdf>.

323. *Id.*

324. See *supra* Part III.B.



Over the years, Congress has made some significant improvements in the controversy system. For example, before the Tax Equity and Fiscal Responsibility Act of 1982 (TEFRA),<sup>325</sup> IRS controversies involving partnerships that invested in tax shelters typically involved audits of individual partners rather than of the partnership itself and led to multiple controversies that burdened the IRS, clogged the courts, and resulted in inconsistent results for similarly-situated taxpayers.<sup>326</sup> The so-called TEFRA audit procedures streamlined the process.<sup>327</sup> Now, instead of auditing each and every partner, TEFRA established unified audit procedures for most partnerships with more than ten partners; basically, the IRS audits the partnership and then applies the results of that single audit to the partnership items on the tax returns of the individual partners.<sup>328</sup> Thus, the TEFRA changes significantly simplified tax administration.<sup>329</sup> All in all, changes that streamline or reduce the number of individual controversies can help both taxpayers and the IRS.

At times, Congress has also been able to reduce the number of controversies by enacting reforms that clarify specific tax provisions. For example, after years of litigation over whether or not punitive damages received in personal injury lawsuits were excluded from income, Congress amended section 104 to establish that, subject to a limited exception, punitive

---

325. Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, 96 Stat. 324 (1982).

326. *See, e.g.*, STAFF OF THE J. COMM. ON TAX'N, JCS-38-92, GENERAL EXPLANATION OF THE REVENUE PROVISIONS OF THE TAX EQUITY AND FISCAL RESPONSIBILITY ACT OF 1982 (1982).

327. I.R.C. §§ 6221-6234.

328. I.R.M. 4.31.2, [http://www.irs.gov/irm/part4/irm\\_04-031-002r.html](http://www.irs.gov/irm/part4/irm_04-031-002r.html).

329. To be sure, further improvements in the TEFRA audit procedures are probably needed. *See, e.g.*, U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-732, LARGE PARTNERSHIPS: WITH GROWING NUMBER OF PARTNERSHIPS, IRS NEEDS TO IMPROVE AUDIT EFFICIENCY (2014), <http://www.gao.gov/assets/670/665886.pdf>; Partnership Auditing Fairness Act, S. 3018, 113th Cong. (2014) (introduced by former Senator Carl Levin [D-Mich.] and referred to Finance Committee on Dec. 16, 2014); U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2015-30-004, ADDITIONAL IMPROVEMENTS ARE NEEDED TO MEASURE THE SUCCESS AND PRODUCTIVITY OF THE PARTNERSHIP AUDIT PROCESS (Mar. 18, 2015), <http://www.treasury.gov/tigta/audit-reports/2015reports/201530004fr.pdf>; Lee A. Sheppard, *Wilkins Endorses Entity-Level Tiered Partnership Audits*, 146 TAX NOTES 730 (Feb. 9, 2015); Amy S. Elliott, *Wilkins Proposes Solution to Large Partnership Audit Dilemma*, 145 TAX NOTES 748 (Nov. 17, 2014); *but see* Steve R. Johnson, *Reforming Federal Tax Litigation: An Agenda*, 41 FLA. ST. U. L. REV. 205, 258-64 (2013) (urging the abolition of the bulk of the TEFRA partnership audit regime) [hereinafter Johnson, *Reforming Federal Tax Litigation: An Agenda*].

damages are not excludable from income.<sup>330</sup> Clarifying changes such as this can reduce the need for costly and burdensome disputes.

Repealing tax expenditures or, at least, adding limits to them can also reduce the number of disputes between taxpayers and the IRS. For example, there can be no doubt that adding the ten percent floor on deductible medical expenses<sup>331</sup> and the two percent floor on the deduction for miscellaneous itemized deductions<sup>332</sup> has reduced the number of controversies between taxpayers and the IRS.

## V. RECOMMENDATIONS FOR CHANGE

The most obvious way to improve tax administration is to increase the IRS's funding, which is what virtually all observers recommend.<sup>333</sup> For that matter, a majority of taxpayers support more funding for IRS services and enforcement.<sup>334</sup> Of course, we started this Article with an understanding that the prospects for increased funding for the IRS are remote,<sup>335</sup> so we will immediately move to recommendations as to what Congress, the Treasury, and the IRS can do with the current level of resources. We divide our remaining recommendations into those that would require legislation from Congress and

---

330. The change was made by the Small Business Job Protection Act of 1996, Pub. L. No. 104-188, § 1605(a)-(c), 110 St. 1755, 1838-39 (1996). *See, e.g.*, *O'Gilvie v. United States*, 519 U.S. 79 (1996) (holding that punitive damages received by petitioners were includable in taxable income because they were not received on account of personal injuries); Ronald H. Jensen, *When Are Damages Tax Free?: The Elusive Meaning of "Physical Injury,"* 10 PITT. TAX REV. 1932 (1997).

331. I.R.C. § 213(a).

332. I.R.C. § 67(a).

333. *See supra* Part IV.A.; CHARLES O. ROSSOTTI, *MANY UNHAPPY RETURNS: ONE MAN'S QUEST TO TURN AROUND THE MOST UNPOPULAR ORGANIZATION IN AMERICA* 278, 284-85 (2005) [hereinafter ROSSOTTI, *MANY UNHAPPY RETURNS: ONE MAN'S QUEST TO TURN AROUND THE MOST UNPOPULAR ORGANIZATION IN AMERICA*] (suggesting that Congress should fund the IRS to do its job by funding technology to increase productivity and funding the IRS to rebuild staff); Susan Striz, Note, *The Key to Closing the Tax Gap: Understanding*, 112 W. VA. L. REV. 1053, 1088-89 (2009-2010) [hereinafter Striz, *The Key to Closing the Tax Gap: Understanding*]. *But see* U.S. H.R. COMM. ON WAYS & MEANS MAJORITY STAFF REP., *DOING LESS WITH LESS*, *supra* note 227 (criticizing IRS spending decisions).

334. IRS OVERSIGHT BD., *2014 TAXPAYER ATTITUDE SURVEY* 3, 10 figs. 11, 12 (2014), <http://www.treasury.gov/IRSOB/reports/Documents/IRSOB%20Taxpayer%20Attitude%20Survey%202014.pdf>.

335. Nevertheless, even we were surprised that Congress cut the IRS's Fiscal Year 2015 budget by still another three percent, and it looks like there may be even more cuts. *See supra* notes 247-250 and accompanying text.

those that generally could be done administratively by Treasury or the IRS or both.<sup>336</sup>

A. *Changes that Would Require Congressional Action*

Short of increasing the IRS budget, this Section discusses a range of tax reforms that Congress could undertake to assist the IRS in its primary task of collecting revenue. In addition to hearing from the Treasury's Office of Tax Policy on legislative matters, Congress needs to talk to and listen to taxpayers, practitioners, and the IRS. The current system is nearly broken, and it needs to be fixed.

Of course, Congressional action on tax reform is almost as unlikely as action to raise the IRS budget.<sup>337</sup> For that matter, there is no guarantee that tax reform legislation would actually improve tax administration. For example, rather than enhancing third-party information reporting to reduce opportunities for taxpayers to evade taxes, recent Congressional action has tended to curtail third-party information reporting.<sup>338</sup>

I. *Simplify the Tax System*

The complexity of the tax system increases the burdens on both taxpayers and the IRS. Complexity erodes voluntary compliance with the tax laws, creates a perception of unfairness for the system, and impedes the effective administration of the tax laws.<sup>339</sup> Consequently, simplification of the

---

336. As academics, we recognize that we are outsiders, and as such our recommendations are based on our limited perspectives based on publicly available information about the IRS. Accordingly, some of our recommendations may not actual work for the IRS. Of course, we would like to see more information about IRS operations made public as that would almost certainly lead to more and better reform recommendations.

337. For example, in a survey conducted in March of 2014 by the accounting firm Ernst & Young, business tax professionals had no expectation that tax reform would pass in 2014, and that there was only a 20 percent chance that the Ways & Means Committee would even mark-up a tax reform bill. ERNST & YOUNG, *Business tax reform and trends: survey views: Views on the prospects for federal tax reform* (2014), <http://www.ey.com/US/en/Services/Tax/Tax-Policy/Business-tax-reform-and-trends-survey-views>. As it turned out, there was no tax reform in 2014, and few believe that any major reforms will occur until at least 2017, after the next Presidential election. See, e.g., Bernie Becker, *Tax reform: Could it happen?*, THE HILL, Jan. 4, 2015, <http://thehill.com/policy/finance/228078-tax-reform-could-it-happen> [hereinafter Becker, *Tax reform: Could it happen?*].

338. TAX GAP: COMPLEXITY AND TAXPAYER COMPLIANCE, *supra* note 96, at 14–15 (recommending the enhancement third-party information reporting of higher-education expenses); See *infra* Part V.A.3.

339. See *supra* Part IV.B.

tax system should result in significant economic and equitable gains. Indeed, with limited resources, it seems unlikely that the IRS can effectively administer a tax system as complicated as the one we currently have.

There have been many calls for simplification of the tax system but few successes.<sup>340</sup> In 1984, the U.S. Department of Treasury began the most successful exploration of tax simplification to date with its white paper entitled *Tax Reform for Fairness, Simplicity, and Economic Growth*.<sup>341</sup> That report, also known as Treasury I, eventually led to the enactment of the Tax Reform Act of 1986.<sup>342</sup>

Treasury I defined simplification in two parts: 1) simplification of factors that plague taxpayers as they prepare their returns, such as forms, instructions, and record-keeping; and 2) simplification of loophole provisions that encourage tax planning and avoidance and distort decision-making.<sup>343</sup> The

---

340. A partial list of simplification proposals includes: STAFF OF THE J. COMM. ON TAX'N, JCS-3-01, STUDY OF THE OVERALL STATE OF THE FEDERAL TAX SYSTEM AND RECOMMENDATIONS FOR SIMPLIFICATION, PURSUANT TO SECTION 8022(3)(B) OF THE INTERNAL REVENUE CODE OF 1986, at vol. 1 (2001), <https://www.jct.gov/publications.html?func=startdown&id=2088>; THE PRESIDENT'S ADVISORY PANEL ON FEDERAL TAX REFORM, SIMPLE, FAIR, AND PRO-GROWTH: PROPOSALS TO FIX AMERICA'S TAX SYSTEM (2005), <http://govinfo.library.unt.edu/taxreformpanel/final-report>; THE PRESIDENT'S ECON. RECOVERY ADVISORY BD., THE REPORT ON TAX REFORM OPTIONS: SIMPLIFICATION, COMPLIANCE, AND CORPORATE TAXATION, *supra* note 283; THE NAT'L COMM'N ON FISCAL RESPONSIBILITY & REFORM, THE MOMENT OF TRUTH (2010), <http://momentoftruthproject.org/report>. Of note, both the U.S. House Ways and Means Committee and the U.S. Senate Finance Committee have recently laid the groundwork for tax reform. *See, e.g.*, U.S. House Committee on Ways & Means Chairman Dave Camp, *Tax Reform Act of 2014, Discussion Draft, Section-by-Section Summary* (2014), [http://waysandmeans.house.gov/UploadedFiles/Ways\\_and\\_Means\\_Section\\_by\\_Section\\_Summary\\_FINAL\\_022614.pdf](http://waysandmeans.house.gov/UploadedFiles/Ways_and_Means_Section_by_Section_Summary_FINAL_022614.pdf); REPUBLICAN STAFF OF THE U.S. S. COMM. ON FINANCE, COMPREHENSIVE TAX REFORM FOR 2015 AND BEYOND (2014), <http://www.finance.senate.gov/newsroom/ranking/download/?id=9dcf2310-68d2-4d80-9e92-3b1d35442b29>; U.S. S. COMM. ON FINANCE, TAX REFORM OPTION PAPERS (2013), <http://www.finance.senate.gov/issue/?id=6c61b1e9-7203-4af0-b356-357388612063>.

341. U.S. TREASURY DEP'T, TAX REFORM FOR FAIRNESS, SIMPLICITY, AND ECONOMIC GROWTH: THE TREASURY DEPARTMENT REPORT TO THE PRESIDENT (1984), <http://www.treasury.gov/resource-center/tax-policy/Pages/tax-reform-index.aspx> [hereinafter TREASURY I]. *See also* PRESIDENT OF THE U.S., THE PRESIDENT'S TAX PROPOSALS TO THE CONGRESS FOR FAIRNESS, SIMPLICITY, AND GROWTH (1985), *available at* <http://www.treasury.gov/resource-center/tax-policy/Pages/tax-reform-pres85index.aspx> [hereinafter TREASURY II].

342. Pub. L. No. 99-514, 100 Stat. 2085 (1986).

343. CHARLES E. MCLURE, JR., FED. RESERVE BANK OF BOSTON CONF. SERIES NO. 29, RATIONALE UNDERLYING THE TREASURY PROPOSALS, IN ECONOMIC CONSEQUENCES OF TAX SIMPLIFICATION 29 (1985), <https://www.bostonfed.org/economic/conf/conf29/conf29.pdf>.

latter form of simplification might not qualify as simplification if simplification is defined as reducing the number of words or pages in the tax laws. Commentators have noted that even if simplification of the Code would be possible, it may not be desirable.<sup>344</sup> For example, while the Tax Reform Act of 1986 has been held up as a model of simplification because it reduced the number of rate brackets and eliminated many tax preferences, it also added to the complexity of the Code by including anti-abuse provisions such as the passive activity loss rules.<sup>345</sup> Moreover, certainty in the tax laws comes with complexity.<sup>346</sup> At the same time, however, it is important to have clear and simple tax rules for most taxpayers.<sup>347</sup> In that regard, while it may not be possible to simplify the federal tax system for all taxpayers, it should be possible to simplify the federal tax system for most individuals and especially for low-income individuals.<sup>348</sup>

a. *Fundamentally Revamp the Tax System*

Tax academics often contemplate the optimal tax system. For some this would be a pure income tax; for others it would be a pure consumption tax.<sup>349</sup> In the real world, however, most governments impose multiple taxes and, therefore, must have multiple enforcement schemes. Arguably, it would be less costly to administer a single tax. With a single tax, however, it may be

---

344. See Samuel A. Donaldson, *The Easy Case Against Tax Simplification*, 22 VA. TAX REV. 645 (2003); Deborah L. Paul, *The Sources of Tax Complexity: How Much Simplicity Can Fundamental Tax Reform Achieve?*, 76 N.C. L. REV. 151 (1997); Calvin H. Johnson, *When 'Simplification' is a Trojan Horse for Great Harm*, 146 TAX NOTES 565 (May 4, 2015).

345. I.R.C. § 469; Donaldson, *The Easy Case Against Tax Simplification*, *supra* note 344, at 670.

346. See Giertz & Feldman, *The Costs of Tax Policy Uncertainty and the Need for Tax Reform*, *supra* note 285, at 951 ("A growing body of research suggests that policy uncertainty imposes substantial economic costs in and of itself."); Donaldson, *The Easy Case Against Tax Simplification*, *supra* note 344, at 662 (noting that section 121 did not provide enough clarity as to what constituted "unforeseen circumstances").

347. See, e.g., Kenneth W. Gideon, *Assessing the Income Tax: Transparency, Simplicity, and Fairness*, 81 TAX NOTES 999 (1998), reprinted in 25 OHIO N.U. L. REV. 101 (1999).

348. See, e.g., Jonathan Barry Forman, *Simplification for Low Income Taxpayers: Some Options*, 57 OHIO ST. L.J. 145 (1996) [hereinafter Forman, *Simplification for Low Income Taxpayers: Some Options*].

349. See generally DAVID BRADFORD AND THE U.S. TREASURY TAX POL. STAFF, BLUEPRINTS FOR TAX REFORM (Tax Analysts, 2nd ed., 1984). For the original Treasury Department version, see U.S. DEP'T OF TREASURY, *Blueprints for Basic Tax Reform* (Jan. 17, 1977), <http://www.treasury.gov/resource-center/tax-policy/Pages/blueprints-index.aspx>.

easier for taxpayers who engage in tax avoidance behaviors to avoid paying their fair share, while having multiple taxes may make it more likely that the government will collect some revenue from all citizens with the ability to pay tax. For example, because unrealized gains are not caught by the income tax, entrepreneurs, like Bill Gates and Mark Zuckerberg, can successfully avoid income taxation on much of their economic income. But if the government imposes a consumption tax or a wealth tax, in addition to an income tax, such entrepreneurs would at least be subject to some tax. In that regard, Professor David Gamage argues that rather than moving towards a comprehensive income tax (or a comprehensive consumption tax), most real-world governments should endeavor to levy labor-income taxes, value-added taxes, capital-income taxes, and wealth taxes.<sup>350</sup>

That said, we wonder whether it really makes sense for the IRS to raise revenues from as many different taxes as it does. Some might call for repeal of taxes that raise insignificant amounts of revenue. In that regard, for example, excise taxes yield less than three percent of total tax revenues.<sup>351</sup> On the other hand, excise taxes sometimes serve some important purposes. First, unlike the federal income tax, federal excise taxes are “recession-proof.” Even taxpayers who may be in a net operating loss position for federal income tax purposes will be liable for any applicable federal excise taxes. Thus, excise taxes can provide the government with a more dependable source of revenue in a down economy. Second, excise taxes can be designed to control externalities and to impose tax burdens on those who benefit from government spending.<sup>352</sup> Finally, excise taxes also can be used to discourage consumption of potentially harmful substances (such as tobacco and alcohol) that individuals might over-consume in the absence of taxation.

Estate and gift taxes are another example of low-yielding taxes and these are subject to considerable (and economically inefficient) avoidance planning.<sup>353</sup> At the same time, however, appreciated assets that avoid estate taxation may escape taxation altogether because of the income tax system’s

---

350. David Gamage, *Analyzing the Optimal Choice of Tax Instruments: The Case for Levying (all of) Labor-Income Taxes, Value-Added Taxes, Capital-Income Taxes, and Wealth Taxes*, 68 TAX L. REV. 355 (Winter 2015).

351. TAX POL. CTR., *Annual Federal Excise Tax Revenue by Type of Tax 1996 – 2012* (May 8, 2014), <http://taxpolicycenter.org/taxfacts/displayafact.cfm?Docid=74&Topic2id=80>. See also PRESENT LAW AND BACKGROUND INFORMATION ON FEDERAL EXCISE TAXES, *supra* note 64.

352. See, e.g., PRESENT LAW AND ANALYSIS OF ENERGY-RELATED TAX EXPENDITURES, *supra* note 92, at 25–26.

353. See, e.g., KEVIN BRADY, REPUBLICAN STAFF STUDY OF THE J. COMM. ON ECON., COST AND CONSEQUENCES OF THE FEDERAL ESTATE TAX: AN UPDATE (2012), [http://www.jec.senate.gov/republicans/public/?a=Files.Serve&File\\_id=bc9424c1-8897-4dbd-b14c-a17c9c5380a3](http://www.jec.senate.gov/republicans/public/?a=Files.Serve&File_id=bc9424c1-8897-4dbd-b14c-a17c9c5380a3).

step-up in basis for inherited assets.<sup>354</sup> Still, it might make sense to repeal the estate and gift tax and instead treat gifts and inheritances as income under the individual income tax.<sup>355</sup> It might also make sense to integrate the individual income tax (largely a tax on labor) with the Social Security payroll tax (another tax on labor),<sup>356</sup> and it might make sense to integrate the corporate income tax with the individual income tax.<sup>357</sup>

Professor Michael Graetz has proposed a two-tier tax system that would replace much of the current income tax system with a value-added tax.<sup>358</sup> His proposal called for a \$100,000-per-family exemption under the individual income tax together with a value-added tax of 14 or 15 percent, and he believes that his proposal would eliminate the need for as many as 100 million individual income tax returns. Under his proposal, only those relatively few families with incomes over \$100,000 would have to file individual income tax returns. However, even a simple value-added tax—one that exempted relatively few goods and services—would have its own significant administrative and compliance burdens.<sup>359</sup> To be sure, one signal benefit of a

---

354. I.R.C. § 1014.

355. *See, e.g.*, Joseph M. Dodge, *Beyond Estate and Gift Tax Reform: Including Gifts and Bequests in Income*, 91 HARVARD L. REV. 1177 (1978); Michael J. Graetz, *Taxation of Unrealized Gains at Death—An Evaluation of Current Proposals*, 59 VA. L. REV. 830 (1973).

356. *See, e.g.*, Jonathan Barry Forman, *Let's Combine the Income and Payroll Taxes into a Rational System*, 59(1) THE TAX EXECUTIVE 55 (Jan.–Feb. 2007); Forman, *Simplification for Low Income Taxpayers: Some Options*, *supra* note 348, at 192–94; Willard B. Taylor, *Should Payroll Taxes Be Repealed?*, 148 TAX NOTES 213 (July 13, 2015).

357. *See, e.g.*, U.S. DEP'T OF TREASURY, INTEGRATION OF THE INDIVIDUAL AND CORPORATE TAX SYSTEMS: TAXING BUSINESS INCOME ONCE (1992), <http://www.treasury.gov/resource-center/tax-policy/Documents/integration.pdf>; R. Glenn Hubbard, *Corporate Tax Integration: A View from the Treasury Department*, 7(1) J. OF ECON. PERSPECTIVES, 115–32 (Winter 1993), <http://pubs.aeaweb.org/doi/pdfplus/10.1257/jep.7.1.115>; KEIGHTLEY & SHERLOCK, THE CORPORATE INCOME TAX SYSTEM, *supra* note 51, at 25. *See also* Michael J. Graetz & Alvin C. Warren, *Unlocking Business Tax Reform*, 145 TAX NOTES 707 (Nov., 10, 2014) (discussing how integration could be a key to business tax reform); N. Gregory Mankiew, *One Way to Fix the Corporate Tax: Repeal It*, N.Y. TIMES, Aug. 23, 2014, [http://www.nytimes.com/2014/08/24/upshot/one-way-to-fix-the-corporate-tax-repeal-it.html?rref=upshot&abt=0002&abg=1&\\_r=0](http://www.nytimes.com/2014/08/24/upshot/one-way-to-fix-the-corporate-tax-repeal-it.html?rref=upshot&abt=0002&abg=1&_r=0).

358. *See generally* MICHAEL J. GRAETZ, 100 MILLION UNNECESSARY RETURNS: A SIMPLE, FAIR, AND COMPETITIVE TAX PLAN FOR THE UNITED STATES (2008).

359. *See, e.g.*, U.S. GOV'T ACCOUNTABILITY OFF., GAO-08-566, VALUE-ADDED TAXES: LESSONS LEARNED FROM OTHER COUNTRIES ON COMPLIANCE RISKS, ADMINISTRATIVE COSTS, COMPLIANCE BURDEN, AND TRANSITION (2008), <http://www.gao.gov/assets/280/274387.pdf>.

comprehensive shift in tax base might be to limit the use of the tax system for non-revenue purposes. As noted earlier, the growth in using the tax system to encourage behavior via tax expenditures has been metastatic, resulting in ever-increasing workloads for the IRS.<sup>360</sup>

In the end, however, we think that significant tax reform is unlikely until after the next Presidential election.<sup>361</sup> As former IRS Commissioner Charles O. Rossotti (1997–2002) noted in his 2005 memoir:

Perhaps someone, someday, will come up with an ideal, simple system that enough people can agree on for raising \$2 trillion per year so that the existing tax code can be done away with. But for now, and probably for many years to come, taxpayers and the IRS are required to comply with the tax code as it exists—and as it changes every year.<sup>362</sup>

*b. Modified Revamp: Simplify or Repeal Certain Provisions*

Because some complexity is unavoidable, we may have to settle for systematic reform of individual tax expenditures or groups of tax expenditures.<sup>363</sup> For example, it could make sense to simplify and consolidate the various family tax credits, the various tax incentives for education, and the various tax incentives for savings and retirement.<sup>364</sup> It might also make sense

---

360. See *supra* Part IV.B.2.

361. Becker, *Tax reform: Could it happen?*, *supra* note 337. See also Kaustuv Basu, *Finance Tax Reform Reports Released; Roadmap Unclear*, 148 TAX NOTES 166 (July 13, 2015). The prospects for business tax reform, or at least international tax reform are a little bit brighter as both Congress and the White House seem interested in reducing the corporate tax rate. See, e.g., Luca Gattoni-Celli & Lindsey McPherson, *Hatch Reform Report Reframes Business Tax Paradigm*, 145 TAX NOTES 1193 (Dec. 15, 2014); Kaustuv Basu, *Congress Will Likely Focus on International Tax Reform This Year*, 147 TAX NOTES 1374 (June 22, 2015).

362. ROSSOTTI, MANY UNHAPPY RETURNS: ONE MAN'S QUEST TO TURN AROUND THE MOST UNPOPULAR ORGANIZATION IN AMERICA, *supra* note 333, at 274; I.R.S., *Previous IRS Commissioners (1955-2013)*, [http://www.irs.gov/uac/Previous-IRS-Commissioners-\(1955-2013\)](http://www.irs.gov/uac/Previous-IRS-Commissioners-(1955-2013)) (last updated Oct. 2, 2015) [hereinafter I.R.S., *Previous IRS Commissioners*].

363. Jeffrey Partlow, *The Necessity of Complexity in the Tax System*, 13(1) WYO. L. REV. 303, 333 (2013). See also ROSSOTTI, MANY UNHAPPY RETURNS: ONE MAN'S QUEST TO TURN AROUND THE MOST UNPOPULAR ORGANIZATION IN AMERICA, *supra* note 333, at 274–75 (recommending that Congress at least simplify the parts of the Internal Revenue Code that affect most taxpayers); David Schizer, *Limiting Tax Expenditures*, 68 TAX L. REV. 275 (2014).

364. See, e.g., THE PRESIDENT'S ECON. RECOVERY ADVISORY BD., *The Report on Tax Reform Options*:



to repeal or limit the deductions for home mortgage interest, state and local taxes, and charitable contributions.<sup>365</sup> Simplification of capital gains taxation and business taxation would also make sense,<sup>366</sup> and many analysts have called for repeal of the alternative minimum tax.<sup>367</sup> Pertinent here, a vast number of modest tax reform proposals have been thought through and are virtually on the shelf when Congress decides to get serious about tax reform.<sup>368</sup>

---

*Simplification, Compliance, and Corporate Taxation*, *supra* note 283, at 4, 10, 23. In particular, Congress should restructure the earned income tax credit. *See, e.g.*, JONATHAN BARRY FORMAN, MAKING AMERICA WORK 129-31 (2006); ISABEL SAWHILL & QUENTIN KARPILOW, CTR. ON CHILDREN & FAMILIES AT BROOKINGS, RAISING THE MINIMUM WAGE AND REDESIGNING THE EITC (Jan. 30, 2014), [http://www.brookings.edu/~media/research/files/papers/2014/01/30-raising-minimum-wage-redesigning-eitc-sawhill.pdf](http://www.brookings.edu/~media/research/files/papers/2014/01/30-raising-minimum-wage-redesigning-eitc-sawhill/30-raising-minimum-wage-redesigning-eitc-sawhill.pdf); ELAINE MAAG, TAX POLICY CTR., INVESTING IN WORK BY REFORMING THE EARNED INCOME TAX CREDIT (May 20, 2015), <http://www.taxpolicycenter.org/UploadedPDF/2000232-investing-in-work-by-reforming-the-eitc.pdf>.

365. I.R.C. §§ 163, 164, 170. *See, e.g.*, AMANDA ENG, HARVEY GALPER, GEORGIA IVSIN & ERIC TODER, TAX POLICY CTR., OPTIONS TO REFORM THE DEDUCTION FOR HOME MORTGAGE INTEREST (Mar. 18, 2013), <http://www.taxpolicycenter.org/publications/url.cfm?ID=412768>; Lily L. Batchelder, Fred T. Goldberg, Jr. & Peter Orzag, *Efficiency and Tax Incentives: the Case for Refundable Tax Credits*, 59 STAN. L. REV. 23 (2006). For example, adding a ten percent floor to the deduction for medical expenses and a two percent floor on the deduction for miscellaneous itemized deductions has reduced the record-keeping burdens on taxpayers and the verification burdens on the IRS. I.R.C. §§ 67(a), 213(a).

366. *See, e.g.*, THE PRESIDENT'S ECON. RECOVERY ADVISORY BD., *The Report on Tax Reform Options: Simplification, Compliance, and Corporate Taxation*, *supra* note 283, at 36 (discussing the simplification of the taxation of capital gains), 46 (discussing the simplification for small businesses), 65 (discussing corporate tax reform), 81 (addressing international corporate tax issues). *See also* Comm. for a Responsible Fed. Budget, *The Tax Break-down: Preferential Rates on Capital Gains* (2013), <http://crfb.org/blogs/tax-break-down-preferential-rates-capital-gains>.

367. *See, e.g.*, THE PRESIDENT'S ECON. RECOVERY ADVISORY BD., THE REPORT ON TAX REFORM OPTIONS: SIMPLIFICATION, COMPLIANCE, AND CORPORATE TAXATION, *supra* note 283, at 49; 2012 ANNUAL REPORT TO CONGRESS, *supra* note 40, at vol. 1, at 24.

368. *See, e.g.*, THE PRESIDENT'S ECONOMIC RECOVERY ADVISORY BD., THE REPORT ON TAX REFORM OPTIONS: SIMPLIFICATION, COMPLIANCE, AND CORPORATE TAXATION, *supra* note 283; CONG. BUDGET OFF., OPTIONS FOR REDUCING THE DEFICIT: 2015-2024 ch. 4 (2014), <http://www.cbo.gov/sites/default/files/cbofiles/attachments/49638-BudgetOptions.pdf>; Calvin H. Johnson, *40 Years: The Shelf Project: Revenue-Raising Projects That Defend the Tax Base*, 136 TAX NOTES 1028 (Aug. 27, 2012).

## 2. *Improve the Legislative Process*

We are at the point where it is difficult to enact even rational improvements to the tax system.<sup>369</sup> Something needs to change.

### a. *A Permanent Loophole-closing Commission*

In the old days, technical corrections bills floated through Congress, but today we have legislative gridlock.<sup>370</sup> When faced with politically difficult decisions, Congress has sometimes resorted to limiting itself to simple up or down votes. For example, relying on the recommendation of the Base Realignment and Closure Commission, Congress managed to overcome political partisanship and significantly reduce the number of military bases.<sup>371</sup> Perhaps a similarly-styled tax reform commission would enable Congress to actually achieve tax reform or at least, to repeal a few loopholes.<sup>372</sup>

We can imagine tax legislation being hammered out by a super-group, voted up or down by Congress, and signed by the President. To be sure, our enthusiasm for this approach is tempered by the failure of Congress's Joint Select Committee on Deficit Reduction, also known as the Supercommittee.<sup>373</sup>

---

369. See, e.g., Eric Solomon, *The Process for Making Tax Policy in the United States: A System Full of Friction*, 67 TAX LAW. 547 (Spring 2014); Michael Doran, *Tax Legislation in the Contemporary U.S. Congress*, 67 TAX L. REV. 555 (2014); Brian Faler, *After IRS scandal, GOP rejects tax crackdown*, POLITICO.COM, <http://www.politico.com/story/2014/07/irs-republicans-109423.html> (last updated July 28, 2014).

370. See, e.g., SARAH A. BINDER, CTR. FOR EFFECTIVE PUB. MGMT., POLARIZED WE GOVERN? (May 2014), [http://www.brookings.edu/~media/research/files/papers/2014/05/27-polarized-we-govern-binder/brookingscepmpolarized\\_figreplacedtextrevtablerev.pdf](http://www.brookings.edu/~media/research/files/papers/2014/05/27-polarized-we-govern-binder/brookingscepmpolarized_figreplacedtextrevtablerev.pdf) (finding that levels of legislative gridlock have steadily risen over the past half-century); Jason S. Oh, *Commentary, Diagnosing Gridlock*, 67 TAX L. REV. 627 (2014).

371. See, e.g., U.S. DEP'T OF DEFENSE, 2005 DEFENSE BASE CLOSURE AND REALIGNMENT COMMISSION REPORT, [http://www.brac.gov/docs/final/BRACReport complete.pdf](http://www.brac.gov/docs/final/BRACReport%20complete.pdf) (last visited Sept. 15, 2015).

372. See James R. Hines Jr. & Kyle D. Logue, *Delegating Tax* (U. of Michigan Pub. Law Research Paper No. 391) (Oct. 2014), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2402047](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2402047).

373. See, e.g., J. Select Comm. on Deficit Reduction, *Statement from Co-Chairs of the Joint Selection Committee on Deficit Reduction* (Press Release, Nov. 21 2011), <http://cybercemetery.unt.edu/archive/deficit/20120113174127/> <http://www.deficitreduction.gov/public/index.cfm/pressreleases?ID=fa0e02f6-2cc2-4aa6-b32a-3c7f6155806d>; Lori Montgomery & Paul Kane, *Supercommittee announces failure in effort to tame debt*, WASH. POST, Nov. 21, 2011, [http://www.washingtonpost.com/business/economy/debt-committee-failure-will-become-official-with-written-joint-statement/2011/11/21/gIQAfRmCiN\\_story.html](http://www.washingtonpost.com/business/economy/debt-committee-failure-will-become-official-with-written-joint-statement/2011/11/21/gIQAfRmCiN_story.html).

Created by the Budget Control Act of 2011,<sup>374</sup> the Supercommittee was supposed to come up with a deficit reduction plan to avoid the imposition of automatic budget sequestration. If the Supercommittee had come up with a recommendation, it would have been subject to an up or down vote in Congress without amendment. Unfortunately, the Supercommittee deadlocked and failed to come up with a plan.<sup>375</sup> We worry that a tax super-group might face a similar fate.

Pertinent here, however, in 2010, the United Kingdom's Treasury Department established an independent Office of Tax Simplification that provides the government with nonbinding, independent advice on simplifying its tax system.<sup>376</sup> Perhaps, the U.S. government should create a similar permanent and independent "Office of Tax Simplification" to provide the government with nonbinding but independent advice on simplifying the tax system. Alternatively, Congress could empower the Joint Committee on Taxation to make formal, legislative tax reform proposals.<sup>377</sup>

*b. Make Congress Write the Details*

Congress regularly relies on Treasury and the IRS to fill in the details of tax legislation.<sup>378</sup> Treasury and the IRS continue to churn out regulations in an effort to make the statutes that Congress passes effective.<sup>379</sup> One might consider this a co-dependent relationship in which Treasury and the IRS have become enablers of sloppy legislation. Congress knows it can pass off responsibility for vague and badly-drafted tax laws to Treasury and the IRS. To the extent that the IRS spends its efforts and limited resources on issuing

---

374. Budget Control Act of 2011, Pub. L. 112–25, § 401, 125 Stat. 240, 259 (2011).

375. See *supra* note 373 and accompanying text.

376. See, e.g., Off. of Tax Simplification, <https://www.gov.uk/government/organisations/office-of-tax-simplification> (last visited Aug. 13, 2015); HER MAJESTY'S TREASURY, OFFICE OF TAX SIMPLIFICATION FRAMEWORK DOCUMENT (2010), [https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/193545/ots\\_framework\\_document\\_jul10.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/193545/ots_framework_document_jul10.pdf).

377. See, e.g., J. Comm. on Tax'n, *Statutory Basis for the Joint Committee on Taxation*, <https://www.jct.gov/about-us/statutory-basis.html> (last visited Aug. 13, 2015).

378. Section 7805 provides a general authorization for the Treasury and IRS to write regulations, and many provisions of the Code specifically authorize the Treasury and IRS to write regulations. See, e.g., I.R.C. §§ 132(o) (certain fringe benefits), 385(c)(3) (treatment of certain interests in corporations as stock or indebtedness).

379. See, e.g., I.R.S., *Priority Guidance Plan*, <http://www.irs.gov/uac/Priority-Guidance-Plan> (last updated July 31, 2015); Kristin E. Hickman, *Administering the Tax System We Have*, 63 DUKE L.J. 1718, 1748–49 (2014), [hereinafter Hickman, *Administering the Tax System We Have*].

guidance to “fix” those tax laws, it just encourages Congress to be even more irresponsible.

Another reason for encouraging more clearly written statutes is that regulatory pronouncements may be more likely to lead to litigation. For example, the Patient Protection and Affordable Care Act (ACA) makes tax credits available to individuals who purchase health insurance through health insurance exchanges “established by the State.”<sup>380</sup> The IRS issued a regulation interpreting that statute broadly enough to include the purchase of health insurance in federal exchanges in those States that failed to establish their own State exchanges.<sup>381</sup> A flood of litigation ensued,<sup>382</sup> and the U.S. Supreme Court has now upheld the validity of that regulation, although without giving deference to the IRS’s interpretation of the statute.<sup>383</sup>

Of course, if Congress did write all the details into its tax legislation, we would be unlikely to see a reduction in the number of pages or words in the Code or in the accompanying Treasury Regulations that followed. For example, in the 1970s, Treasury embarked on writing detailed fringe benefit regulations under section 61(a)(1).<sup>384</sup> Congress stepped in and put a budgetary freeze on the issuance of those regulations.<sup>385</sup> Finally, in 1984, Congress enacted major fringe benefit legislation that, among other things added the multi-page section 132,<sup>386</sup> which enactment, was, of course, followed by even more pages of regulations.<sup>387</sup> Moreover, both the statute and the regulations

---

380. I.R.C. § 36B(c)(2)(A)(i).

381. Reg. § 1.36B-2(a)(1).

382. *See, e.g.*, Jonathan H. Adler, *D.C. Circuit grants en banc rehearing in Halbig v. Burwell*, WASH. POST, Sept. 4, 2014, <http://www.washingtonpost.com/news/volokh-conspiracy/wp/2014/09/04/d-c-circuit-grants-en-banc-rehearing-in-halbig-v-burwell/>.

383. *See King v. Burwell*, 135 S. Ct. 2480 (2015). We are sure that a flood of articles on the Supreme Court’s take on formerly well-settled administrative law will follow.

384. *See* STAFF OF THE J. COMM. ON TAX’N, JCS-38-78 TAXATION OF FRINGE BENEFITS 5 (1978), [https://www.jct.gov/publications.html?func=download&id=4017&chk=4017&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4017&chk=4017&no_html=1).

385. *Id.*

386. I.R.C. § 132 (added by the Deficit Reduction Act of 1984, § 531(a)(1), Pub. L. No. 98-369, 98 Stat. 494, 877-81 (1984)). Cynics might note that the Deficit Reduction Act of 1984 gave politicians significant opportunities to raise campaign contributions from many industries that were affected by this and other provisions. *Cf.* JEFFREY H. BIRNBAUM & ALAN S. MURRAY, *SHOWDOWN AT GUCCI GULCH* (1988) (discussing efforts of many well-shod lobbyists working to influence the Tax Reform Act of 1986).

387. *See, e.g.*, Reg. §§ 1.132-1 *et seq.*

have been amended numerous times since 1984.<sup>388</sup>

The revenue estimating process may also encourage regulatory rather than Congressional action. Regulations that cost revenue are not accounted for by the Joint Committee on Taxation, while such “scoring” is required for all tax bills proposed by Congress.<sup>389</sup>

In the end, Treasury and the IRS really have little choice about writing regulations. The public and practitioners often need guidance, and they lobby both Treasury and Congress to get it. Not surprisingly, when Treasury is tardy in issuing regulations, Congress sometimes steps in, often making an even bigger mess.<sup>390</sup>

### 3. *Enhance Third-party Information Reporting*

As already explained, the tax gap analysis shows that third-party reporting significantly enhances compliance.<sup>391</sup> For example, Figure 2 showed that because of third-party withholding and reporting on wage income, individuals report approximately 99 percent of their wages. Moreover, third-party reporting facilitates cost-effective enforcement via automated checking of the amounts reported on the return with the amounts reported by the third party (the Automated Underreporter [AUR] program). The U.S. Government Accountability Office (GAO) estimated that the AUR program raised \$22 for every dollar spent.<sup>392</sup> The GAO examined the 2007 and 2008 tax years and found that correspondence and field examinations accounted for more than 80 percent of the total administrative costs of the four audit programs it reviewed.<sup>393</sup> These non-automated audits are much more expensive—the GAO estimated that the correspondence examinations of individual taxpayers raised just \$7 per dollar spent, and field examinations of individual taxpayers raised only \$1.80 per dollar spent.<sup>394</sup>

---

388. See, e.g., Tax Reform Act of 1986, Pub. L. No. 99-514, §§ 1114(b)(5), 1151(e)(2)(A), (g)(5), 1853(a), 1899A(5), 100 Stat. 2451, 2506–2507, 2870, 2958 (1986).

389. Mann, *Chief Counsel’s Subtle Impact on Revenue*, *supra* note 77.

390. See, e.g., *Exxon Mobil Corp. et al. v. Commissioner*, 689 F.3d 191, *aff’d* 136 T.C. 99 (2011). In 1986, Congress instructed Treasury to study and promulgate regulations on interest netting for overpayments and underpayments. In 1998, Congress became impatient with Treasury and enacted Code section 6621(d), which required a technical correction and led to the litigation cited above, in which the taxpayer prevailed.

391. See *supra* Part III.B.2.

392. TAX GAP: IRS COULD SIGNIFICANTLY INCREASE REVENUES, *supra* note 163, at 8.

393. *Id.* at 6.

394. *Id.* at 8.

Despite clear evidence that third-party reporting significantly and efficiently enhances compliance, Congress appears to be moving in the opposite direction. In 2011, for example, Congress repealed the expanded reporting requirement that had been added by the Patient Protection and Affordable Care Act (ACA) in 2010 as well as the expanded reporting requirement for landlords added by the Small Business Job Act. Before the ACA, section 6041 required businesses making payments to a single recipient of at least \$600 in a single year to file a Form 1099-MISC, Miscellaneous Income, with the IRS and send one to the recipient.<sup>395</sup> IRS regulations exempted, among other things, payments made to corporations and payments made for merchandise.<sup>396</sup> Beginning in 2012, the ACA required all businesses to report payments to, and purchases from, any taxable entity totaling \$600 or more in a calendar year, regardless of the payee's corporate status or whether the payments were made for merchandise or other property.<sup>397</sup> The Joint Committee on Taxation estimated that the provision would have raised \$17.1 billion over the following decade.<sup>398</sup>

Similarly, the Small Business Jobs Act of 2010 amended section 6041 to subject recipients of rental income from real estate to the same information reporting requirements as taxpayers engaged in a trade or business.<sup>399</sup> In particular, rental income recipients making payments of \$600 or more to a service provider (such as a plumber, painter, or accountant) in the course of earning rental income were required to provide an information return (typically, a Form 1099-MISC, Miscellaneous Income) to the IRS and to the service provider. The Joint Committee on Taxation estimated that the provision would have raised \$2.5 billion over the following decade.<sup>400</sup>

These two Form-1099 information-reporting expansions had many detractors who argued that the provisions would hurt small businesses, restrict economic growth, and increase unemployment; and the Comprehensive 1099

---

395. I.R.C. § 6041.

396. Reg. § 1.6041-1(b) (1960).

397. Pub. L. No. 111-148, § 9006, 124 Stat. 119, 855 (2010).

398. STAFF OF THE J. COMM. ON TAX'N, JCX-17-10, ESTIMATED REVENUE EFFECTS OF THE AMENDMENT IN THE NATURE OF A SUBSTITUTE TO H.R. 4872, THE "RECONCILIATION ACT OF 2010," AS AMENDED, IN COMBINATION WITH THE REVENUE EFFECTS OF H.R. 3590, THE "PATIENT PROTECTION AND AFFORDABLE CARE ACT ('PPACA')," AS PASSED BY THE SENATE, AND SCHEDULED FOR CONSIDERATION BY THE HOUSE COMMITTEE ON RULES ON MARCH 20, 2010 1 (2010), <https://www.jct.gov/publications.html?func=startdown&id=3672>.

399. Pub. L. No. 111-240, § 2101, 124 Stat. 2504, 2561 (2010).

400. STAFF OF THE J. COMM. ON TAX'N, JCX-48-10, ESTIMATED BUDGET EFFECTS OF THE REVENUE PROVISIONS CONTAINED IN SENATE AMENDMENT #4594 TO H.R. 5297, THE "SMALL BUSINESS JOBS ACT OF 2010," SCHEDULED FOR CONSIDERATION BY THE UNITED STATES SENATE ON SEPTEMBER 16, 2010 2 (2010), <https://www.jct.gov/publications.html?func=startdown&id=3708>.

Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011 soon repealed those expansions.<sup>401</sup> One congressional supporter praised the repeal: “[N]ow because of the President’s signature, our job creators can go about their business without fear of being hammered by mountains of additional, unnecessary tax paperwork.”<sup>402</sup> The fate of these expanded-reporting provisions casts doubt as to whether Congress would be willing to make the IRS more efficient by requiring more third-party reporting.<sup>403</sup>

#### 4. *Simplify the Tax Penalty System*

The tax penalty system is another world altogether. The purpose of tax penalties is to encourage compliance, but the tax penalty system has become so complex that it is both difficult for the IRS to determine the appropriate penalty as well as nearly impossible for taxpayers to connect their behavior with a particular penalty.<sup>404</sup> Moreover, tax penalties are among the most litigated issues identified in the annual reports of the National Taxpayer

---

401. Pub. L. No. 112–9, 125 Stat. 36 (2011).

402. Statement of Republican Senator Mike Johanns of Nebraska, cited in Felicia Sonmez, *Obama Signs Repeal of Health Care Laws 1099 Tax Reporting Rule*, WASH. POST, Apr. 14, 2011, [http://www.washingtonpost.com/blogs/2chambers/post/obama-signs-1099-repeal-into-law-marking-first-repeal-of-national-health-care-law-provision/2011/04/14/AFRhYjeD\\_blog.html](http://www.washingtonpost.com/blogs/2chambers/post/obama-signs-1099-repeal-into-law-marking-first-repeal-of-national-health-care-law-provision/2011/04/14/AFRhYjeD_blog.html).

403. We also have some concerns about the appropriate use of third-party reports in assessing taxes. In particular, the limited information that is reported by third parties can sometimes lead the IRS to over-assess taxes. For example, amounts that banks and other financial institutions report on IRS Forms 1099-A & 1099-C as cancellation of indebtedness are not always accurate. *See, e.g.*, 2010 ANNUAL REPORT TO CONGRESS, *supra* note 86, at vol. 1, at 12. Similarly, amounts that brokers and other financial institutions report (on IRS Form 1099-B, Proceeds from Broker and Barter Exchange Transactions) as basis with respect to sales are not always accurate and can lead the IRS to over-assess gains. *See, e.g.*, Jonathan Horn, *The brave new world of cost basis reporting*, J. OF ACCOUNTANCY, Sept. 1, 2013, <http://www.journalofaccountancy.com/issues/2013/sep/20137345.html>; AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, *Recommendations for 2015-2016 Guidance Priority List (Notice 2015-27)*, (2015), <http://www.aicpa.org/advocacy/tax/downloadable/documents/aicpas-2015-2016-priority-guidance-plan-list-final.pdf>.

404. *See, e.g.*, AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, REPORT ON CIVIL TAX PENALTIES: THE NEED FOR REFORM (Apr. 11, 2013), <http://www.aicpa.org/Advocacy/Tax/TaxLegislationPolicy/DownloadableDocument/s/AICPA-legislative-proposals-penalties-2013.pdf> [AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, REPORT ON CIVIL PENALTIES: THE NEED FOR REFORM 2013].

Advocate.<sup>405</sup> Numerous commentators have called for simplification of the tax penalty regime.<sup>406</sup>

Imposing penalties for failure to accurately report tax liability is supposed to improve compliance.<sup>407</sup> It is not only the penalty itself, but the perception of the penalty that encourages compliance. In particular, if taxpayers believe that tax penalties are imposed arbitrarily or unjustly, penalties could have the opposite effect and lead to lack of respect for the tax system and reduced compliance. While the penalty system is statutory, the IRS has some discretion in whether to impose or abate a penalty.<sup>408</sup>

In 1998, as part of the IRS Reform and Restructuring Act (RRA), Congress required Treasury to study the tax penalty system.<sup>409</sup> Treasury recommended restructuring the failure to file and failure to pay penalties,<sup>410</sup> establishing a threshold below which the failure to pay estimated tax penalty would not be imposed,<sup>411</sup> and increasing the penalty for filing a frivolous tax return from \$500 to \$1,500.<sup>412</sup> RRA also required the Joint Committee on Taxation to conduct a study of the tax penalty system.<sup>413</sup> The Joint Committee

---

405. See, e.g., 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 423 (noting that tax penalties are among the most litigated issues); 2013 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 322 (noting that tax penalties are among the most litigated issues).

406. See, e.g., Charles P. Rettig, *Practice: Enhancing Voluntary Compliance Through the Administration of Civil Tax Penalties*, 13 J. OF TAX PRACTICE & PROCEDURE 17 (CCH) (Apr.–May 2011) (calling for a comprehensive review of the civil tax penalty structure); Kyle D. Logue, *Optimal Tax Compliance and Penalties When the Law Is Uncertain*, 27 VA. TAX REV. 241 (2007); Alex Raskolnikov, *Crime and Punishment in Taxation: Deceit, Deterrence, and the Self-Adjusting Penalty*, 106 COLUM. L. REV. 569 (2006).

407. See, e.g., Michael Doran, *Tax Penalties and Tax Compliance*, 46 HARV. J. ON LEGIS. 111, 123 (2009).

408. I.R.M. 20.1.1, [http://www.irs.gov/irm/part20/irm\\_20-001-001r.html](http://www.irs.gov/irm/part20/irm_20-001-001r.html).

409. Pub. L. No. 105–206, § 3801, 112 Stat. 685, 782 (1998).

410. U.S. DEP'T OF TREASURY, OFF. OF TAX POL., REPORT TO CONGRESS ON PENALTY AND INTEREST PROVISIONS OF THE INTERNAL REVENUE CODE 3–4 (1999), <http://www.treasury.gov/resource-center/tax-policy/Documents/intpenal.pdf> (recommending that the Code section 6651 failure to file and failure to pay penalties be restructured to eliminate the frontloading of the failure to file penalty and to impose a higher failure to pay penalty) [hereinafter REPORT TO CONGRESS ON PENALTY AND INTEREST].

411. *Id.* at 4–5 (recommending simplifying changes to the Code section 6654 failure to pay estimated tax penalty).

412. *Id.* at 7 (recommending simplifying changes to the section 6702 penalty for filing a frivolous return).

413. IRS Reform and Restructuring Act (RRA), Pub. L. No. 105–206, § 3801, 112 Stat. 685, 782 (1998); J. COMM. ON TAX'N, JCS-3-99, STUDY OF PRESENT-LAW PENALTY AND INTEREST PROVISIONS AS REQUIRED BY SECTION 3801 OF THE



recommended repealing the penalty for failure to pay tax, modifying the accuracy related penalty standards, and changing the preparer penalty.<sup>414</sup> Some of these legislative recommendations were eventually enacted. For example, in 2006, Congress increased the penalty for filing a frivolous tax return from \$500 to \$5,000.<sup>415</sup> However, Congress has not yet enacted any systematic reform of tax penalties.<sup>416</sup>

In the late 2000s, the National Taxpayer Advocate and the American Institute of Certified Public Accountants (AICPA) both issued calls for penalty reform.<sup>417</sup> The AICPA expressed concern that “the overall framework of civil penalties . . . is not sufficiently geared towards encouraging voluntary compliance.”<sup>418</sup> National Taxpayer Advocate Nina E. Olson has noted that inappropriately designed penalties could reduce compliance if “they provide a disincentive for noncompliant taxpayers to step forward, are so disproportionate or arbitrarily imposed that taxpayers feel they are unjust, or result in protracted disputes that leave the IRS with few resources to impose them.”<sup>419</sup> Also, a recent National Taxpayer Advocate study found that taxpayers who were subject to default penalty assessments were significantly less compliant five years after the assessment than taxpayers who were not

---

INTERNAL REVENUE SERVICE RESTRUCTURING AND REFORM ACT OF 1998 (INCLUDING PROVISIONS RELATING TO CORPORATE TAX SHELTERS) (1999), vol. 1, [https://www.jct.gov/publications.html?func=download&id=2896&chk=2896&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=2896&chk=2896&no_html=1) [hereinafter PRESENT LAW PENALTY & INTEREST STUDY]; *id.* at vol. 2, [https://www.jct.gov/publications.html?func=download&id=2893&chk=2893&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=2893&chk=2893&no_html=1).

414. *See, e.g.*, PRESENT LAW PENALTY & INTEREST STUDY, *supra* note 413, at vol. 1, at 3–6.

415. Tax Relief and Health Care Act of 2004 Pub. L. No. 109–432, § 407(a), 120 Stat. 2922, 2960–62 (2004).

416. NATIONAL TAXPAYER ADVOCATE, 2008 ANNUAL REPORT TO CONGRESS (2008), at vol. 2, at 11 (A Framework for Reforming the Penalty Regime), [http://www.irs.gov/file\\_source/pub/tas/08\\_tas\\_arc\\_vol2.pdf](http://www.irs.gov/file_source/pub/tas/08_tas_arc_vol2.pdf) [hereinafter 2008 ANNUAL REPORT TO CONGRESS].

417. *Id.*; AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, REPORT ON CIVIL PENALTIES: THE NEED FOR REFORM (Aug. 28, 2009), <http://www.aicpa.org/press/pressreleases/2009/downloadabledocuments/aicpa-report-civil-tax-penalty-reform.pdf> [hereinafter AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, REPORT ON CIVIL PENALTIES: THE NEED FOR REFORM 2009].

418. AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, REPORT ON CIVIL PENALTIES: THE NEED FOR REFORM 2009, *supra* note 417, at 2. *See also* AM. INST. OF CERTIFIED PUB. ACCOUNTANTS, REPORT ON CIVIL TAX PENALTIES: THE NEED FOR REFORM 2013, *supra* note 404.

419. 2008 ANNUAL REPORT TO CONGRESS, *supra* note 416, at 4–5.

penalized.<sup>420</sup> This evidence suggests that thoughtful reform of the tax penalty regime could improve compliance, while also lessening the IRS's workload.

##### 5. *Increase Transparency to Increase Compliance*

Making the tax system more open could also help the IRS administer the tax system. For example, Professor George Yin recently recommended that the IRS could regain the public's trust by increasing the transparency of the agency's tax administrative decisions.<sup>421</sup> Specifically, he recommends that the IRS should increase disclosure of its decisions in the tax-exempt organization area. Professor Yin believes that there should be meaningful transparency of the IRS's decision as to whether or not to grant tax-exempt status *and* the underlying tax return information provided by the applicants. Some have also advocated for public disclosure of the tax returns of corporations.<sup>422</sup> Others have suggested that the judicial standing rules should be changed to allow litigants to challenge the tax benefits received by other taxpayers.<sup>423</sup> As section

---

420. 2013 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 2, at 1, 11. *See also* 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, vol. 1, at 94.

421. Yin, *The Most Critical Issue Facing Tax Administration Today -- And What to Do About It*, *supra* note 274; George K. Yin, *Reforming (and Saving) the IRS by Respecting the Public's Right to Know*, 100 VA. L. REV. 1115 (2014).

422. *See, e.g.*, Joshua D. Blank, *Reconsidering Corporate Tax Privacy*, 11 N.Y.U. J.L. & BUS. 31 (2014); *Panel 2: Should Corporate Tax Returns Be Public?* David Kamin, moderator; Joshua D. Blank, presenter; Allison Christians, Reuven S. Avi-Yonah, Peter A. Barnes, discussants, 11 N.Y.U. J.L. & BUS. 159 (2014); Reuven S. Avi-Yonah & Ariel Siman, *The 1 Percent Solution: Corporate Tax Returns Should Be Public (And How to Get There)*, 2014 WORLDWIDE TAX DAILY 32–11 (Feb. 17, 2014). *See also* Paul Caron, *Dwenger Presents Improving Tax Collection by Public Shaming Today at UC-Berkeley*, TAXPROF BLOG (Nov. 10, 2014), [http://taxprof.typepad.com/taxprof\\_blog/2014/11/dwenger-presents-improving-tax-collection.html](http://taxprof.typepad.com/taxprof_blog/2014/11/dwenger-presents-improving-tax-collection.html); Ricardo Perez-Truglia & Ugo Troiano, *Shaming Those Who Skip Out on Taxes*, N.Y. TIMES, Apr. 15, 2015, at A25, [http://www.nytimes.com/2015/04/15/opinion/shaming-those-who-skip-out-on-taxes.html?\\_r=1#story-continues-1](http://www.nytimes.com/2015/04/15/opinion/shaming-those-who-skip-out-on-taxes.html?_r=1#story-continues-1); Jon Forman, *Shaming tax cheats*, JOURNAL RECORD [of Oklahoma City], June 8, 2009, at 6A; Mike Donoghue, *Vermont Tax Department issues new delinquent lists*, BURLINGTON FREE PRESS, Feb. 2, 2015, <http://www.burlingtonfreepress.com/story/news/politics/2015/02/02/vermont-tax-department-issues-delinquent-lists/22770087/>.

423. *See, e.g.*, Eileen J. O'Connor, remarks at a panel of the A.B.A. Tax Sec., Midyear Meeting, Committee on Tax Policy and Simplification (Jan. 24, 2014). In general, taxpayers do not have standing to sue the federal government over the tax benefits of other taxpayers. *Frothingham v. Mellon*, 262 U.S. 447 (1923). Taxpayers do, however, have standing to sue the government to prevent an unconstitutional use of taxpayer funds. *Flast v. Cohen*, 392 U.S. 83 (1968) (finding that a taxpayer had standing to sue the federal government to prevent it from spending funds on religious schools in violation of the First Amendment's ban on the establishment of religion); *but see Arizona Christian Sch. Tuition Org. v. Winn*, 555 U.S. 488 (2011) (finding

6103 currently limits the disclosure of taxpayer information in most situations, legislation would be needed for such increases in transparency.

We firmly believe that the IRS should release detailed information about its operations so that it can be held accountable. At present, however, the IRS is subject to oversight by numerous Congressional committees, the IRS Oversight Board, the IRS National Taxpayer Advocate, the Treasury Inspector General for Tax Administration (TIGTA), the Secretary of the Treasury, the U.S. Government Accountability Office, the Office of Management and Budget (OMB), Congress, the Congressional Research Service (CRS), numerous advisory committees, the press, public and private think tanks, and the public generally.<sup>424</sup> We believe in oversight, but we are concerned about the extensive oversight that the IRS is subject to, and, in particular, we are concerned with the resources that the IRS must expend in providing information in various formats to all its overseers.<sup>425</sup> Pertinent here, some believe that the IRS Oversight Board has not done enough to supervise the agency and that it should be reinvigorated and its role should be expanded.<sup>426</sup>

#### 6. *Streamline Dispute Procedures*

It is clear that the IRS and U.S. Department of Justice spend a great

---

that the First Amendment does not give taxpayers standing to challenge the constitutionality of tax credits or other tax expenditures). *See also* Linda Sugin, *Colloquium on Tax Policy & Public Finance, Invisible Taxpayers* (2015), [http://www.law.nyu.edu/sites/default/files/upload\\_documents/Linda%20Sugin.pdf](http://www.law.nyu.edu/sites/default/files/upload_documents/Linda%20Sugin.pdf).

424. *See, e.g.,* I.R.S., *IRS Oversight Organizations*, <http://www.irs.gov/uac/IRS-Oversight-Organizations> (last updated Feb. 23, 2015); Danshera Cords, Law & Society Assoc. Annual Meeting, in Seattle, Washington, *Peeling Back the Layers: Oversight of Tax Administration in the United States* (unpublished manuscript prepared for May 28, 2015).

425. In particular, we are concerned that Congressional oversight hearings focus too much on grandstanding about past mistakes rather than future improvements in tax collection. *See, e.g.,* Tom Cohen, *Koskinen: IRS troubles 'suspicious,' but no crime uncovered*, CNN POLITICS, June 27, 2014, <http://www.cnn.com/2014/06/26/politics/john-koskinen-irs-commissioner-cnn-interview/>; Lindsey Boerma, *Benghazi, IRS hearings: Political grandstanding, or has "do-nothing Congress" found its legs?*, CBSNEWS, May 14, 2013, <http://www.cbsnews.com/news/benghazi-irs-hearings-political-grandstanding-or-has-do-nothing-congress-found-its-legs/>; *Senate Panel Hears Stories Of Alleged IRS Abuses*, ALLPOLITICS CNN, Apr. 28, 1998, <http://www.cnn.com/ALLPOLITICS/1998/04/28/irs.hearings/>.

426. David van den Berg, *IRS Oversight Board's Effectiveness Questioned*, 146 TAX NOTES 746 (Feb. 9, 2015). Recall that, because the IRS Oversight Board does not currently have enough members for a quorum, its operations have been suspended. *See supra* note 80 and accompanying text.

deal of their resources on dispute resolution and litigation.<sup>427</sup> Accordingly, Congress and the agencies should streamline the applicable procedures. Taxpayers should always get an opportunity to dispute their tax liabilities. In that regard, Congress should expand the jurisdiction of the Appeals Office so that it could consider an appeal from virtually every IRS determination or action, and Congress should also expand the jurisdiction of the U.S. Tax Court so that it could hear virtually all tax disputes.<sup>428</sup> Indeed, some argue that the U.S. Tax Court should be virtually the only court for federal tax disputes.<sup>429</sup> In any event, Congress should take tax refund jurisdiction away from the U.S. Court of Federal Claims.<sup>430</sup> Of course, in order to resolve disputes more efficiently, the U.S. Tax Court will need more resources.

Congress should also rethink its commitment to collection due process (CDP) hearings and appeals.<sup>431</sup> CDP is one of the most litigated issues identified in the annual reports of the National Taxpayer Advocate,<sup>432</sup> and according to Professor Steve Johnson, these “CDP cases claim substantial resources from the IRS and the Tax Court.”<sup>433</sup> Like Professor Johnson, we

---

427. For example, see *supra* note 225 and Table 5 to see how the IRS allocated its budget in a recent year.

428. See, e.g., Comment, Adrienne Hodgkins, *Getting a Second Chance: The Need for Tax Court Jurisdiction Over IRS Denials of Relief Under Section 66*, 65 LA. L. REV. 1167 (2005). See also STAFF OF THE J. COMM. ON TAX’N, JCX-19-15, DESCRIPTION OF THE CHAIRMAN’S MARK OF VARIOUS PROPOSALS RELATING TO ACCESS AND ADMINISTRATION OF THE U.S. TAX COURT (2015), [https://www.jct.gov/publications.html?func=download&id=4699&chk=4699&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4699&chk=4699&no_html=1) (discussing various proposals concerning access to the U.S. Tax Court and U.S. Tax Court Administration); Leandra Lederman, *When the Bough Breaks: The U.S. Tax Court's Branch Difficulties*, 34 A.B.A. TAX SEC. NEWS QUARTERLY 10 (Winter 2015), <http://www.americanbar.org/content/dam/aba/publishing/newsquarterly/15win/aba-newsq-winter2015.pdf>.

429. See, e.g., Larry Kramer, *The Division of Jurisdiction Between State and Federal Courts: Diversity Jurisdiction*, 1990 BYU L. REV. 97 (1990).

430. Johnson, *Reforming Federal Tax Litigation: An Agenda*, *supra* note 329, at 256–57. We come to this conclusion even though author Jonathan Barry Forman once clerked for a judge on the U.S. Court of Federal Claims, and he fondly recalls that the tax cases that he worked on then were the most interesting cases on the court’s docket. See *supra* note 132.

431. See *supra* note 198 and accompanying text.

432. See, e.g., 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 477.

433. Johnson, *Reforming Federal Tax Litigation: An Agenda*, *supra* note 329, at 265–66. See also Bryan T. Camp, *The Failure of Adversarial Process in the Administrative State*, 84 IND. L.J. 57 (2009); but see Leslie Book, *A Response to Professor Camp: the Importance of Oversight*, 84 IND. L.J. SUPP. 63 (2009).

believe that judicial review of IRS collection activities should be more limited.<sup>434</sup>

Finally, some have recommended creating a national appellate tax court to hear virtually all appeals from tax cases.<sup>435</sup> This approach would lead to faster resolution of tax issues and greater national uniformity.

### 7. *Give the IRS More Authority to Regulate Tax Practitioners and Preparers*

Tax preparers and tax practitioners are often the gateway between the IRS and taxpayers. For example, 55.5 percent of the almost 147.4 million individual tax returns filed for tax year 2013 were completed by a paid preparer.<sup>436</sup> Unfortunately, the IRS's authority to regulate practitioners and preparers is limited,<sup>437</sup> and recent cases have questioned even that limited authority.<sup>438</sup> In order to ensure the competency of tax preparers and

---

434. Johnson, *Reforming Federal Tax Litigation: An Agenda*, *supra* note 329, at 266.

435. *See, e.g.*, Erwin N. Griswald, *The Need for a Court of Tax Appeals*, 57 HARV. L. REV. 1153 (1944); Jasper L. Cummings, Jr., *Creation of National Appellate Tax Court Will Improve Tax Law*, TOWARD TAX REFORM: RECOMMENDATIONS FOR PRESIDENT OBAMA'S TASK FORCE 30, 30–32 (Tax Analysts ed., 2009), [http://www.taxanalysts.com/www/freefiles.nsf/Files/CUMMINGS-9.pdf/\\$file/CUMMINGS-9.pdf](http://www.taxanalysts.com/www/freefiles.nsf/Files/CUMMINGS-9.pdf/$file/CUMMINGS-9.pdf); Striz, *The Key to Closing the Tax Gap: Understanding*, *supra* note 333, at 1087–88; FED. JUDICIAL CTR., REPORT OF THE FEDERAL COURTS STUDY COMMITTEE 69 (Apr. 2, 1990), [http://www.fjc.gov/public/pdf.nsf/lookup/repfsc.pdf/\\$file/repfsc.pdf](http://www.fjc.gov/public/pdf.nsf/lookup/repfsc.pdf/$file/repfsc.pdf); Martin D. Ginsberg, *The Federal Courts Study Commission Committee on Claims Court Tax Jurisdiction*, 40 CATH. U. L. REV. 631 (1991); *but see* James P. Holden, *The Federal Courts Study Committee Has Not Made the Cases for Its Proposed Overhaul of the Tax Litigation Process*, 40 CATH. UNIV. L. REV. 639 (1991); Johnson, *Reforming Federal Tax Litigation: An Agenda*, *supra* note 329, at 252–54.

436. *SOI Tax Stats*, *supra* note 9.

437. U.S. GOV'T ACCOUNTABILITY OFF., PAID TAX RETURN PREPARERS, *supra* note 41, at i, 3–6 (Statement of James R. McTigue, Jr.).

438. *See, e.g.*, *Loving v. Internal Revenue Service*, 742 F.3d 1013 (D.C. Cir. 2014) (finding that the IRS lacked statutory authority to require all federal tax return preparers to submit to registration, competency testing, and continuing education requirements); Internal Revenue Service, *IRS Statement on Court Ruling Related to Return Preparers*, <http://www.irs.gov/uac/Newsroom/IRS-Statement-on-Court-Ruling-Related-to-Return-Preparers> (last updated Feb. 3, 2015); Alex Levy, *Believing in Life After Loving: IRS Regulation of Tax Preparers*, 17 FLA. TAX REV. 437 (2015); Steve R. Johnson, *How Far Does Circular 230 Exceed Treasury's Statutory Authority?*, 146 TAX NOTES 221 (2015); Jamie Patrick Hopkins, *Loving v. IRS: The IRS's Achilles' Heel for Regulated Tax Advice?*, 34 VA. TAX REV. 191 (2014) [hereinafter Hopkins, *Loving v. IRS: The IRS's Achilles' Heel for Regulated Tax*

practitioners, Congress should give the IRS explicit authority to regulate them.<sup>439</sup>

8. *Do Not Expand Private Debt Collection*

While increasing third-party reporting would likely increase IRS efficiency, another one of Congress's ideas would likely increase costs for the IRS. The American Jobs Creation Act of 2004 authorized the IRS to enter into contracts for private debt collection of tax debts.<sup>440</sup> Some commentators think that the private sector can do almost anything better than the government.<sup>441</sup> The IRS began using private debt collectors in 2006 but discontinued the program in 2009.<sup>442</sup> According to the *2013 Annual Report* of the National Taxpayer Advocate Nina E. Olson, the IRS was significantly more effective than the private debt collectors in collecting tax liabilities in all but the first six months after case receipt, collecting about twice as much as a percent of the dollars available for collection.<sup>443</sup> The National Taxpayer Advocate report further concluded that

these results likely understate the difference in IRS and [private debt collector] effectiveness, since our analysis placed the IRS at a significant disadvantage: All of the cases were older when the IRS got them, and some were more than two years older; and the [private debt collectors] worked the

---

*Advice?*]; STAFF OF THE J. COMM. ON TAX'N, JCX-34-14, PRESENT LAW AND BACKGROUND RELATED TO THE REGULATION OF CONDUCT OF PAID TAX RETURN PREPARERS (2014), [https://www.jct.gov/publications.html?func=download&id=4580&chk=4580&no\\_html=1](https://www.jct.gov/publications.html?func=download&id=4580&chk=4580&no_html=1); Kip Dellinger, *Ridgely Allows Contingent Fees? Not So Fast, CPAs!*, 145 TAX NOTES 575 (2014).

439. See, e.g., I.R.S. ADVISORY COUNCIL, 2014 PUBLIC REPORT, *supra* note 264, at 20; 2013 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 61; Hopkins, *Loving v. IRS: The IRS's Achilles' Heel for Regulated Tax Advice?*, *supra* note 438; William R. Davis & Jaime Arora, *Legislation Needed to Strengthen Circular 230, Hawkins Says*, 145 TAX NOTES 492 (Nov. 3, 2014); W. Edward Afield, *A Market for Tax Compliance*, 62 CLEV. ST. L. REV. 315 (2014); Johnson, *How Far Does Circular 230 Exceed Treasury's Statutory Authority?*, *supra* note 438, at 237-38; Michelle Drumbl, *When Helpers Hurt: Protecting Taxpayers From Preparers*, 145 TAX NOTES 1365 (Dec. 22, 2014).

440. Pub. L. No. 108-357, § 881(e), 118 Stat. 1418, 1625 (2004).

441. See, e.g., John Stossel, *Private Enterprise Does It Better*, TOWNHALL.COM, Aug. 8, 2004, [http://townhall.com/columnists/johnstossel/2010/08/04/private\\_enterprise\\_does\\_it\\_better](http://townhall.com/columnists/johnstossel/2010/08/04/private_enterprise_does_it_better); but see Erik Eckholm, *Democrats Step Up Criticism of Halliburton Billing in Iraq*, N.Y. TIMES, June 28, 2005, <http://www.nytimes.com/2005/06/28/politics/28haliburton.html?pagewanted=all>.

442. 2013 ANNUAL REPORT TO CONGRESS, *supra* note 2, vol. 2, at 97, 99.

443. *Id.* at 107.

cases first and collected the easy dollars, while the IRS only got cases the [private debt collectors] had already worked.<sup>444</sup>

Despite this evidence, private tax collection is again being proposed on Capitol Hill.<sup>445</sup> In a recent letter describing the prior program, National Taxpayer Advocate Nina E. Olson said that it “undermined effective tax administration, jeopardized taxpayer rights protections, and did not accomplish its intended objective of raising revenue.”<sup>446</sup> Although the Joint Committee on Taxation predicted that the program authorized by the American Jobs Creation Act of 2004 would raise more than \$1 billion in revenue,<sup>447</sup> the program actually lost money.<sup>448</sup>

According to Olson, recent private-debt-collection proposals are even worse than the prior program.<sup>449</sup> The private debt collection proposal contained in a bill reported out of the Senate Finance Committee in April of 2014 would have required (prior legislation “allowed”) the IRS to operate a new private debt collection program and would have required that all “inactive tax receivables” be assigned to private debt collectors, subject to limited exceptions (prior legislation allowed IRS discretion to select).<sup>450</sup> Critically, the new proposal and Olson’s response highlight an important consideration for attempts to streamline IRS operations: the government must consider long-term compliance. Olson notes that aggressive collection actions by private debt collectors might force some marginal taxpayers into public assistance programs, which could cost the government more than the amount of the tax collected.<sup>451</sup> The private debt collectors would not care about long-term compliance or taxpayer hardship, as their compensation would be based on a

---

444. *Id.*

445. *See, e.g.*, Expiring Provisions Improvement Reform and Efficiency (EXPIRE) Act of 2014, S. Rep. No. 113-154, at 121–24 (2014) [hereinafter EXPIRE Act of 2014] (explaining sections 304 and 305 of the version of S. 2260, the EXPIRE Act of 2014, 113th Cong.).

446. IRS Taxpayer Advocate Nina E. Olson, *Letter to various members of the U.S. Senate Finance and House Ways and Means committees 2* (May 13, 2014), [http://www.taxpayeradvocate.irs.gov/userfiles/file/NTA\\_PDC\\_letter.pdf](http://www.taxpayeradvocate.irs.gov/userfiles/file/NTA_PDC_letter.pdf) [hereinafter Olson, *Letter to U.S. Senate Finance and House Ways and Means committees*].

447. STAFF OF THE J. COMM. ON TAX’N, JCX-69-04, ESTIMATED BUDGET EFFECTS OF THE CONFERENCE AGREEMENT FOR H.R. 4520, THE “AMERICAN JOBS CREATION ACT OF 2004” 9 (2004), <http://www.jct.gov/x-69-04.pdf>.

448. Olson, *Letter to U.S. Senate Finance and House Ways and Means committees*, *supra* note 446, at 2.

449. *Id.*

450. The prior legislation was contained in the Code section 6306 (2004). The new proposal is contained in sections 304 and 305 of the EXPIRE Act of 2014. EXPIRE Act of 2014, *supra* note 445.

451. Olson, *Letter to U.S. Senate Finance and House Ways and Means committees*, *supra* note 446, at 7.

percentage of tax collected.<sup>452</sup> Moreover, the Joint Committee on Taxation estimated that the Senate Finance Committee private debt collection proposal would only raise \$2.4 billion over ten years—not very much compared to the size of the tax gap or compared to the amount of revenue brought in by the IRS collection function in 2013 (\$31.4 billion).<sup>453</sup> All in all, it seems likely that the government would get more bang-for-the-buck by giving more money to the IRS rather than by giving it to private debt collectors.

*B. Administrative Actions that Could be Taken by Treasury or IRS or Both*

In this Section we offer a number of recommendations that generally could be done administratively by Treasury or the IRS or both, although here, too, some recommendations might require legislation or, at least, tacit approval from Congress.

*1. Issue Simplifying Regulations*

The IRS and Treasury have the primary responsibility for drafting regulations that interpret the Code.<sup>454</sup> Regulations do not always complicate tax law. Simplifying regulations can be both popular and non-controversial.

The so-called “check-the-box” regulations are a case in point. Before 1996, the IRS decided how to tax business entities by applying the so-called *Kintner* regulations.<sup>455</sup> The regulations identified four corporate characteristics: 1) continuity of life; 2) centralized management; 3) limited liability; and 4) freely transferable interests.<sup>456</sup> If an entity had three corporate characteristics, it was taxed as a corporation.<sup>457</sup> If it had two or fewer corporate characteristics, the IRS would disregard it for tax purposes if it had a single owner, or tax it as a partnership if it had more than one owner.<sup>458</sup> The *Kintner* regulations intentionally made it more difficult to obtain corporate tax

---

452. *Id.* at 8.

453. *Id.* at 14; STAFF OF THE J. COMM. ON TAX’N, JCX-51-14, ESTIMATED BUDGET EFFECTS OF AN AMENDMENT IN THE NATURE OF A SUBSTITUTE TO H.R. 3474, THE “EXPIRING PROVISIONS IMPROVEMENT, REFORM, AND EFFICIENCY (‘EXPIRE’) ACT OF 2014,” SCHEDULED FOR CONSIDERATION BY THE SENATE 4 (May 15, 2014), <https://www.jct.gov/publications.html?func=startdown&id=4601>.

454. *See, e.g.*, I.R.C. § 7805.

455. *Kintner v. United States*, 107 F. Supp. 976, 979 (D. Mont. 1952), *aff’d.*, 216 F.2d 418 (9th Cir. 1954); Reg. § 301.7701-2(a)(1) (1960); *see* Heather M. Field, *Checking in on “Check-the-Box,”* 42 LOY. L.A. L. REV. 451, 460 (2009) [hereinafter Field, *Checking in on “Check-the-Box”*].

456. Reg. § 301.7701-2(a)(1) (1961).

457. Reg. § 301.7701-2(a)(2), (3) (1961).

458. *Id.*



treatment. In 1996, Treasury promulgated the so-called “check-the-box” regulations.<sup>459</sup> Whereas under prior *Kintner* regulations, the IRS determined the tax classification of a business entity by examining its corporate characteristics, the check-the-box regulations allowed non-corporate entities to elect their tax classification. The regulations solved problems for both the IRS and taxpayers. The IRS no longer needed to use resources to litigate or issue guidance on entity classification issues.<sup>460</sup> Of course, the check-the-box regulations may be a special case. The rise of the limited liability company under State law together with the 1986 Tax Reform Act’s lowering of individual income tax rates had fundamentally changed the business-entity landscape.

For that matter, despite their length, the fringe benefit regulations discussed above did provide much simplifying guidance for taxpayers.<sup>461</sup> The Treasury regulations dealing with alimony and property settlement also provided significant simplifying guidance, and, notably, they were written in a clear question-and-answer style that was designed to be understandable by both divorce attorneys and tax attorneys.<sup>462</sup>

While simplifying regulations are helpful if the opportunity arises, in many circumstances simplifying regulations would merely lead to revenue loss. For example, the IRS spends a lot of time and resources litigating the employee/independent contractor distinction,<sup>463</sup> but a check-the-box regime for that classification would likely eviscerate the entire employment tax system.<sup>464</sup>

## 2. *Move to a Return-free System*

One way to simplify the tax system, at least for low-income taxpayers,

---

459. Reg. § 301.7701-3, T.D. 8697 (1996).

460. Field, *Checking in on “Check-the-Box,”* *supra* note 455, at 464.

461. *See supra* note 387 and accompanying text.

462. Reg. §§ 1.71-1 *et seq.*, 1.215-1 *et seq.*, 1.1041-1 *et seq.*

463. *See, e.g.,* I.R.S., *Independent Contractor (Self-Employed) or Employee?*, <http://www.irs.gov/Businesses/Small-Businesses-&Self-Employed/Independent-Contractor-Self-Employed-or-Employee> (last updated Aug. 5, 2015); I.R.M. 4.23.5, [http://www.irs.gov/irm/part4/irm\\_04-023-005.html](http://www.irs.gov/irm/part4/irm_04-023-005.html); 2012 ANNUAL REPORT TO CONGRESS, *supra* note 40, vol. 1, at 197.

464. To be sure, with the enactment of section 530 of the Revenue Act of 1978, Congress made it difficult for the IRS to regulate the line between employees and independent contractors. *See, e.g.,* I.R.M. 4.23.5; STAFF OF THE J. COMM. ON TAX’N, JCX-26-07, PRESENT LAW AND BACKGROUND RELATING TO WORKER CLASSIFICATION FOR FEDERAL TAX PURPOSES (2007), <http://www.irs.gov/pub/irs-utl/x-26-07.pdf>. *See also* Martin A. Sullivan, *Economic Analysis: 10 Tax Challenges for The Sharing Economy*, 148 TAX NOTES 136, 137 (July 13, 2015) (wondering if Uber drivers should be classified as employees or independent contractors).

would be to move to either a return-free or final withholding tax system.<sup>465</sup> Under a return-free system, the IRS would prepare tax returns for individual taxpayers based on information reports received from employers and other third-party information sources. Under a final withholding system, the amounts withheld from employers and other income sources would be the tax, thus eliminating the need for many taxpayers to file tax returns. For example, under its Pay-As-You-Earn system (PAYE), the United Kingdom uses information reporting and withholding to ensure that most wage earners do not need to file an annual tax return.<sup>466</sup>

Along similar lines, the IRS recently considered moving towards a so-called “real-time tax system” that could receive all third-party information returns and make them available online for use by taxpayers and preparers.<sup>467</sup> Although Congressional action to expand third-party reporting would enhance such return-free tax systems, the IRS should be able to eliminate return preparation for many taxpayers under current law.<sup>468</sup> Pertinent here,

---

465. See, e.g., Forman, *Simplification for Low Income Taxpayers: Some Options*, *supra* note 348, at 197–200; Roberta Mann, *Beyond Enforcement: Top 10 Strategies for Encouraging Tax Compliance*, 111 TAX NOTES 919, 927–28 (May 22, 2006); Joseph Bankman, *Using Technology to Simplify Individual Tax Filing*, 61 NAT’L TAX J. 773 (2008); THE PRESIDENT’S ECONOMIC RECOVERY ADVISORY BOARD, THE REPORT ON TAX REFORM OPTIONS: SIMPLIFICATION, COMPLIANCE, AND CORPORATE TAXATION, *supra* note 283, at 41–42 (discussing California’s “ReadyReturn” program); *Ways to Improve the Tax System: Return-Free Filing*, URBAN-BROOKINGS TAX POLICY CENTER, <http://www.taxpolicycenter.org/briefing-book/improve/return-free/index.cfm> (last visited Aug. 14, 2015); U.S. DEP’T OF TREASURY, REPORT TO CONGRESS ON RETURN-FREE TAX SYSTEMS: TAX SIMPLIFICATION IS A PREREQUISITE (2003), <http://www.treasury.gov/resource-center/tax-policy/Documents/noreturn.pdf>; Austan Goolsbee, *The Simple Return: Reducing America’s Tax Burden Through Return-Free Filing* (Brookings Institution, Hamilton Project Discussion Paper No. 2006-04, (2006), <http://www.brookings.edu/research/papers/2006/07/useconomics-goolsbee>).

466. See, e.g., U.S. GOV’T ACCOUNTABILITY OFF., GAO-11-540T, TAX ADMINISTRATION: PRELIMINARY INFORMATION ON SELECTED FOREIGN PRACTICES THAT MAY PROVIDE USEFUL INSIGHTS (STATEMENT OF MICHAEL BROSTEK) 9 (2011), <http://www.gao.gov/assets/130/125975.pdf>.

467. I.R.S., *Real Time Tax Initiative*, <http://www.irs.gov/Tax-Professionals/Real-Time-Tax-Initiative> (last updated Jan. 13, 2015); I.R.S., *December 8, 2011 Meeting (on Real-Time Tax System)*, <http://www.irs.gov/Tax-Professionals/December-8,-2011-Meeting> (last updated Jan. 12, 2015).

468. To be sure, there are real challenges with trying to prepare returns based largely on third-party reporting of wages, interest, dividends, etc. First, those third-party information returns are not always perfected and filed with the IRS in time to prepare returns by April 15th of each year. Second, even if the IRS receives those third-party information returns, it will not know about any taxpayer information that is not covered by those third-party information returns. Telling taxpayers “this is all the income we know about” might undermine their incentive to report other amounts

recognizing how burdensome return preparation can be, the National Taxpayer Advocate recently recommended that the IRS should help prepare returns, at least for vulnerable populations (including low income, disabled, and elderly taxpayers).<sup>469</sup> Alternatively, the IRS could create TurboTax-like software so that taxpayers could more easily prepare and file their own tax returns.<sup>470</sup>

### 3. *Improve the IRS's Allocation of Resources*

The IRS could also do a better job with the resources that it has. The U.S. Government Accountability Office (GAO) believes that “[a] long-term strategy that includes a fundamental reexamination of IRS’s operations, program, and organizational structure could help it operate more effectively and efficiently in an environment of budget uncertainty.”<sup>471</sup> For example, some believe that the IRS should restore at least some of the geographic organizational structure that it had before its 1998 functional reorganization.<sup>472</sup>

---

that are not subject to third-party reporting. In any event, the IRS will still need more information from taxpayers to determine their eligibility for various tax benefits (including filing status). Finally, from a policy perspective, many believe that it is important for citizens to prepare and file tax returns so that they know the price they pay for citizenship. *See, e.g.*, LAWRENCE ZELENAK, *LEARNING TO LOVE FORM 1040: TWO CHEERS FOR THE RETURN-BASED MASS INCOME TAX* (2013).

469. 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 315; *but see* JOSEPH CORDES & ARLENE HOLEN, *TECH. POL. INST., SHOULD THE GOVERNMENT PREPARE INDIVIDUAL INCOME TAX RETURNS?* i (2010), <https://www.techpolicyinstitute.org/files/should%20the%20government%20prepare%20individual%20income%20tax%20returns.pdf> (arguing that “[a]dopting a return-free tax system is not an advisable policy for the federal government”).

470. *See, e.g.*, Stuart Goldenberg, *Would You Let the I.R.S. Prepare Your Taxes?*, N.Y. TIMES, Apr. 15, 2015, [http://www.nytimes.com/2015/04/16/technology/personaltech/turbotax-or-irs-as-tax-preparer-intuit-has-a-favorite.html?\\_r=0](http://www.nytimes.com/2015/04/16/technology/personaltech/turbotax-or-irs-as-tax-preparer-intuit-has-a-favorite.html?_r=0).

471. U.S. GOV’T ACCOUNTABILITY OFF., *IRS 2015 BUDGET*, *supra* note 250, at 18.

472. *See, e.g.*, Frank Wolpe, *Restoring Trust in the Internal Revenue Service*, 33(2) ABA TAX. SEC. NEWS QUARTERLY 1 (Opinion Point, Winter 2014), <http://www.americanbar.org/content/dam/aba/publishing/newsquarterly/14win/opinionpoint-restoring-trust.pdf>; Frank Wolpe, *The Rebuild IRS Initiative* (Apr. 19, 2015), <http://ssrn.com/abstract=2596390>; Frank Wolpe, *A Renewed Call for True Structural Reform to Restore Trust in the Internal Revenue Service by Rebuilding Field Operations with Democratic and Republican Participation* (Nov. 25, 2014), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2530786](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2530786). *See also* 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 31 (discussing the IRS local presence), 46 (discussing how the IRS lacks a permanent appeals presence in 12 States and Puerto Rico), 311 (discussing taxpayer access to appeals).

a. *Shift Resources from Guidance to Enforcement*

Although the IRS needs to strike the proper balance between taxpayer service and enforcement activities, it probably should shift more of its limited resources towards enforcement.<sup>473</sup> Pertinent here, a recent report by the Treasury Inspector General for Tax Administration (TIGTA) found that IRS employees could take more action to collect outstanding taxpayer liabilities before closing cases as “currently not collectible” (e.g., filing more notices of federal tax lien).<sup>474</sup> Also, to reduce the amount of identity theft and refund fraud, the IRS could take a little longer evaluating returns and complete more compliance checks before it issues refunds.<sup>475</sup>

We note that, in the past, encouraging enhanced enforcement has sometimes backfired. For example, the 1998 IRS Reform and Restructuring Act implemented collection due process procedures because Congress got the impression that IRS agents and revenue officers had become overzealous in pursuing taxpayers, in part, because performance reviews were based on revenue collected.<sup>476</sup> The pendulum of tax enforcement has swung several

---

473. See *supra* note 225 and Table 5 to see how the IRS allocated its budget in a recent year. To be sure, as Congress appropriates separate amounts for distinct categories of IRS activity, the IRS’s ability to shift resources around without Congressional approval is somewhat limited. See *supra* notes 226–227 and accompanying text.

474. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2014-30-052, DELINQUENT TAXES MAY NOT BE COLLECTED BECAUSE REQUIRED RESEARCH WAS NOT ALWAYS COMPLETED PRIOR TO CLOSING SOME CASES AS CURRENTLY NOT COLLECTIBLE (Aug. 25, 2014), <http://www.treasury.gov/tigta/auditreports/2014reports/201430052fr.pdf>; see also Erik Miller, Stacy Orlett & Alex Turk, RESEARCH, ANALYSIS, AND STAT. I.R.S., I.R.S. RESEARCH BULLETIN 2014, *Uncollectible Versus Unproductive: Compliance Impact of Working Collection Cases That Are Ultimately Not Fully Collectible*, in AN IRS-TPC RESEARCH CONFERENCE: ADVANCING TAX ADMINISTRATION 79 (Alan Plumley, ed., 2015), <http://www.irs.gov/pub/irs-soi/14rescon.pdf> [hereinafter Miller, Orlett & Turk, *Uncollected Versus Unproductive*, in AN IRS-TPC RESEARCH CONFERENCE]; U.S. GOV’T ACCOUNTABILITY OFF., GAO-15-647, IRS CASE SELECTION: COLLECTION PROCESS IS LARGELY AUTOMATED, BUT LACKS ADEQUATE INTERNAL CONTROLS (2015), <http://www.gao.gov/assets/680/671733.pdf> (recommending that the IRS take actions to improve its collection controls).

475. See, e.g., U.S. GOV’T ACCOUNTABILITY OFF., IRS 2015 BUDGET, *supra* note 250, at 20–21. See also I.R.S., *Security Summit: Protecting Taxpayers from Identity Theft Tax Refund Fraud* (2015), <http://www.irs.gov/uac/Newsroom/Security-Summit-2015> (announcing new steps to fight identity theft).

476. See *supra* notes 198, 431–434, and accompanying text.

times during the time we have been watching, and we hesitate to advocate pushing the pendulum too far towards enforcement.<sup>477</sup>

With limited resources, the IRS will simply not be able to issue as much guidance. In that regard, for example, the so-called 2015–2016 priority guidance plan lists just 277 projects, which is significantly less than it has proposed in recent years.<sup>478</sup> The IRS will also have to better prioritize the kinds of guidance that it issues.<sup>479</sup> In the long run, it seems inevitable that the IRS will spend less time on private letters rulings and determination letters for individual taxpayers and will instead favor regulations, revenue rulings, and other forms of guidance that can reach many taxpayers simultaneously, rather than one-by-one.<sup>480</sup> Indeed, the IRS has already announced that it is going to significantly reduce the scope of its determination letter program for individually designed pension plans.<sup>481</sup> With limited resources, the IRS will almost have to shift more of the burdens of reporting and compliance onto taxpayers,<sup>482</sup> and it has already begun shifting resources towards “digital

---

477. See, e.g., Kathryn Keneally & Charles P. Rettig, *IRS Enforcement: The Pendulum has Swung Too Far*, 9 J. OF TAX PRACTICE & PROCEDURE 13 (2007–2008); ROSSOTTI, MANY UNHAPPY RETURNS: ONE MAN’S QUEST TO TURN AROUND THE MOST UNPOPULAR ORGANIZATION IN AMERICA, *supra* note 333, at 103–07.

478. Nathan J. Richman & Andrew Velarde, *Shrinking Priority Guidance Plan Addresses Spinoffs, Marriage*, 148 TAX NOTES 608 (Aug. 10 2015); U.S. DEP’T OF TREASURY, 2015–2016 PRIORITY GUIDANCE PLAN (July 31, 2015), [http://www.irs.gov/pub/irs-utl/2015-2016\\_pgp\\_initial.pdf](http://www.irs.gov/pub/irs-utl/2015-2016_pgp_initial.pdf). (joint statement by Assistant Secretary (Tax Policy) Mark J. Mazur, Commissioner John A. Koskinen, and Chief Counsel William J. Wilkins).

479. See *supra* Part III.B.5 for a discussion of the kinds of guidance that the IRS issues.

480. Alison Bennett, *Annual Guidance Plan May Be Affected By Shrinking Budget, Top IRS Official Says*, 03 DAILY TAX REP (BNA), Jan. 7, 2015, at G–3.

481. Announcement 2015-19, 2015-32 I.R.B. 157 (“effective January 1, 2017, these changes will eliminate the staggered [five]-year determination letter remedial amendment cycles for individually designed plans and will limit the scope of the determination letter program for individually designed plans to initial plan qualification and qualification upon plan termination.”). See, e.g., FERENCZY BENEFITS LAW CENTER LLP, *Is This the End of Rico . . . er, FDLs?*, [http://www.ferenczylaw.com/Documents/FlashPoint/4\\_1\\_15\\_FlashPoint\\_Is\\_This\\_the\\_End\\_of\\_Rico\\_er\\_FDLs.pdf](http://www.ferenczylaw.com/Documents/FlashPoint/4_1_15_FlashPoint_Is_This_the_End_of_Rico_er_FDLs.pdf) (last viewed Aug. 14, 2015); Matthew R. Madara, *IRS Not Expecting to Eliminate Plan Determination Letter Program*, 145 TAX NOTES 778 (Nov. 17, 2014) (“The IRS has no intention of eliminating its determination letter program for retirement plans, but the agency would like to expand its use of preapproved plans to cover more types of arrangements, an IRS official said November 13.”).

482. See, e.g., William R. Davis, *IRS Budget Woes Could Pave Way for More Taxpayer Reporting*, 147 TAX NOTES TODAY 508 (May 4, 2015); Laura Davison, *IRS:*

communication products” to communicate with taxpayers—instead of face-to-face, telephonic, and mail communications.<sup>483</sup>

*b. Shift Audit Resources*

While enhanced third-party reporting seems unlikely to happen<sup>484</sup> and private debt collection appears counterproductive,<sup>485</sup> the IRS could shift its audit resources to enhance its efficiency.<sup>486</sup> Refundable tax credits pose a particular problem for the IRS, both in terms of time and adverse press.<sup>487</sup> In 2011, for example, 24.6 million returns claimed the refundable earned income tax credit (EITC), 20.5 million returns claimed the refundable child credit, and 7.6 million returns claimed the refundable portion of the American Opportunity Tax Credit.<sup>488</sup>

Recently, the U.S. Government Accountability Office (GAO) analyzed a hypothetical reallocation of IRS examination resources over two years (2007 and 2008) and found that a shift of about \$124 million in enforcement resources could have increased direct revenue by \$1 billion over

---

*Koskinen: IRS Budget Cuts Mean More: Burdensome Audits for Corporations*, 68 DAILY TAX REP. (BNA), Apr. 10, 2015, at G–8.

483. See, e.g., COURTNEY RASEY & MACKENZIE WILEY, I.R.S. WAGE & INVESTMENT, 2014 TAXPAYER CHOICE MODEL: DESIGNING DIGITAL COMMUNICATION PRODUCTS TO REDUCE PHONE AND MAIL INVENTORY (2015), [http://www.irs.gov/file\\_source/pub/irs-soi/15rescontaxpayerchoice.pptx](http://www.irs.gov/file_source/pub/irs-soi/15rescontaxpayerchoice.pptx).

484. See *supra* Part V.A.3.

485. See *supra* Part V.A.8.

486. See, e.g., 2014 ANNUAL REPORT TO CONGRESS, *supra* note 2, at vol. 1, at 112.

487. See, e.g., U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2015-40-009, THE INTERNAL REVENUE SERVICE IS WORKING TOWARD COMPLIANCE WITH EXECUTIVE ORDER 13520 REPORTING REQUIREMENTS (Dec. 29, 2014), <http://www.treasury.gov/tigta/auditreports/2015reports/201540009fr.pdf> (estimating that in Fiscal Year 2013, earned income tax credit claims totaled approximately \$60 billion and that 24 percent of the earned income tax credit payments were paid in error); U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-737T, IMPROPER PAYMENTS: GOVERNMENT-WIDE ESTIMATES AND REDUCTION STRATEGIES 4 (July 9, 2014), <http://www.gao.gov/assets/670/664692.pdf> (showing the earned income tax credit to be in the top five programs with improper payment estimates); U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2014-40-093, EXISTING COMPLIANCE PROCESSES WILL NOT REDUCE THE BILLIONS OF DOLLARS IN IMPROPER EARNED INCOME TAX CREDIT AND ADDITIONAL CHILD TAX CREDIT PAYMENTS (Sept. 29, 2014), <http://www.treasury.gov/tigta/auditreports/2014reports/201440093fr.pdf>.

488. Justin Bryan, *Individual Income Tax Returns, 2011*, 33(2) STATISTICS OF INCOME BULLETIN 5, 13, 14 (Fall 2013). See also *Individual Income Tax Returns 2012*, *supra* note 25.

the \$5.5 billion per year the IRS actually collected.<sup>489</sup> The GAO analysis hypothetically shifted the \$124 million from examinations of lower-income returns with the earned income tax credit (EITC) and from lower-income business returns without the EITC to examinations of higher-income returns and lower-income nonbusiness returns without the EITC.<sup>490</sup> The GAO concluded that the IRS should collect and analyze more return and audit data to assist them in “more finely adjusting its resource allocation decisions.”<sup>491</sup>

The GAO suggested that the IRS should study the feasibility of estimating the marginal revenue and marginal costs within each program, and within each taxpayer group, and determine how “the broad characteristics of the returns that would likely be selected (or not selected) in a modest program expansion (or contraction) would differ from the average return actually audited now.”<sup>492</sup> That “information would help the IRS assess the extent to which revenue productivity would likely decline, if at all, if more exam resources are devoted to a particular group of taxpayers.”<sup>493</sup> In short, the IRS should select returns for enforcement that are the most cost-effective to pursue.

In addition, the GAO suggested that the IRS should examine whether there is a link between the time that specific examiners spend on each case and the revenue collection amounts for each case.<sup>494</sup> That analysis would allow the IRS to estimate ratios of direct revenue to cost that better incorporate differences in the hourly costs across examiners with different skill levels.<sup>495</sup> The GAO noted that there are challenges in estimating the influence of enforcement activity on voluntary compliance, but the GAO encouraged the IRS to leverage its existing efforts to study voluntary compliance to improve information on the influence of enforcement activity on voluntary compliance.<sup>496</sup>

Basically, the IRS should use return-on-investment information to help manage its enforcement resources.<sup>497</sup> Of course, collecting and studying

---

489. TAX GAP: IRS COULD SIGNIFICANTLY INCREASE REVENUES, *supra* note 163, at 10.

490. *Id.* at 10.

491. *Id.* at 15.

492. *Id.*

493. *Id.*

494. *Id.*

495. *Id.*

496. *Id.*

497. *See, e.g.*, U.S. GOV'T ACCOUNTABILITY OFF., IRS 2015 BUDGET, *supra* note 250, at 18–24; U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2013-10-104, THE USE OF RETURN ON INVESTMENT INFORMATION IN MANAGING TAX ENFORCEMENT RESOURCES COULD BE IMPROVED (Sept. 23, 2013), <http://www.treasury.gov/tigta/auditreports/2013reports/201310104fr.pdf>. Technically speaking, the IRS should estimate the marginal return-on-investment of its various

data requires resources. When budgets are slim, what should the IRS cut? Should it cut research or revenue-collecting staff? It is a conundrum similar to the age-old question of what came first, the chicken or the egg.

Enhanced examination of partnership tax returns could also improve collections. Limited Liability Companies (LLCs) taxed as partnerships are frequently used by both small businesses and large corporations to facilitate tax sheltering, yet the audit rate of partnership returns is only around 0.43 percent.<sup>498</sup> The GAO has found that the IRS does not effectively audit large partnerships because of tax law complexity and the administrative constraints due to tight budgets.<sup>499</sup> The GAO also found that IRS examinations and automated document matching have not been effective in finding partnership and S corporation misreported income and that matching Form K-1s to partnership and S corporation tax returns could enhance detection of non-compliance.<sup>500</sup> The IRS is already moving in this direction. A senior official at the IRS Office of Chief Counsel announced plans to assess only the top tier of partners in tiered partnerships.<sup>501</sup> A new legislative proposal may help the IRS in this regard. U.S. Representative James Renacci recently introduced the “Partnership Audit Simplification Act of 2015,” which is designed to simplify the audit of large tiered partnerships, in part, by shifting the burden from the IRS to the partners.<sup>502</sup>

---

enforcement possibilities and allocate its resources to the strategies that will maximize revenue (i.e., get the best bang-for-the-buck).

498. See *supra* note 181. See also the discussion of partnership audit procedures *supra* Part IV.C.

499. U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-746T, LARGE PARTNERSHIPS: GROWING POPULATION AND COMPLEXITY HINDER EFFECTIVE IRS AUDITS (STATEMENT OF JAMES R. WHITE) 17 (2014), <http://gao.gov/assets/670/664917.pdf>.

500. U.S. GOV'T ACCOUNTABILITY OFF., GAO-14-453, PARTNERSHIPS AND S CORPORATIONS: IRS NEEDS TO IMPROVE INFORMATION TO ADDRESS TAX NONCOMPLIANCE 15, 19 (2014), <http://www.gao.gov/assets/670/663185.pdf>.

501. Laura Davison, *IRS Aims to Audit C Corporations, Large Partnerships at Similar Rates*, 39 DAILY TAX REP. (BNA), Feb. 26, 2015, at G-6 (quoting comments by William Heard, III, senior counsel in the Office of Chief Counsel (Procedure and Administration): “We assess the first passthrough to the partner and they have to figure out how to handle it with indirect partners. They figure out how to share the liability or become a C corp.”). See also *supra* notes 325–329 and accompanying text (discussing the TEFRA audit procedures).

502. H.R. 2821, 114th Cong, 1st Sess. (2015). See also Aaron E. Lorenzo, *New Audit Legislation Aims to Cut Complexity, Adds Burdens to Partners*, 128 DAILY TAX REPORT (BNA), July 3, 2015, at G-1.



c. *Expand the Compliance Assurance Process (CAP) program*

The IRS initiated the Compliance Assurance Process (CAP) program for large business taxpayers in 2005 and expanded it, and made it permanent, in 2011.<sup>503</sup> Under CAP, participating taxpayers work collaboratively with the IRS to identify and resolve potential tax disputes before the taxpayer files its federal income tax return. Both taxpayers and the IRS are able to achieve tax certainty sooner and with less administrative burden than in the traditional post-filing examination program.<sup>504</sup> CAP has proven to be effective and efficient, and the IRS should explore further expansions of the program.

4. *Expand Alternative Dispute Resolution and the Use of IRS Appeals*

Alternative dispute resolution (ADR) is often considered a cost effective way to avoid litigation.<sup>505</sup> The Appeals Office at the IRS, founded in 1927, could be regarded as one of the earliest dispute-resolution organizations in the United States.<sup>506</sup> While negotiation was the original ADR function of

---

503. I.R.S., *IRS Expands and Makes Permanent Its Compliance Assurance Process (CAP) for Large Corporate Taxpayers*, IR-2011-32, [http://www.irs.gov/uac/IRS-Expands-and-Makes-Permanent-Its-Compliance-Assurance-Process-\(CAP\)-for-Large-Corporate-Taxpayers](http://www.irs.gov/uac/IRS-Expands-and-Makes-Permanent-Its-Compliance-Assurance-Process-(CAP)-for-Large-Corporate-Taxpayers). See also I.R.M. 4.51.8 (Compliance Assurance Process (CAP) Examinations), [http://www.irs.gov/irm/part4/irm\\_04-051-008.html](http://www.irs.gov/irm/part4/irm_04-051-008.html); Loren M. Opper, *Compliance Assurance Process*, 63(6) THE TAX EXECUTIVE 413 (Nov.–Dec. 2011), <http://www.tei.org/news/articles/Documents/Compliance%20Assurance%20Process.pdf>.

504. U.S. TREASURY INSPECTOR GEN. FOR TAX ADMIN., REF. NO. 2013-30-021, THE COMPLIANCE ASSURANCE PROCESS HAS RECEIVED FAVORABLE FEEDBACK, BUT ADDITIONAL ANALYSIS OF ITS COSTS AND BENEFITS IS NEEDED (Feb. 22, 2013), <http://www.treasury.gov/tigta/auditreports/2013reports/201330021fr.pdf>; U.S. GOV'T ACCOUNTABILITY OFF., GAO-13-662, CORPORATE TAX COMPLIANCE: IRS SHOULD DETERMINE WHETHER ITS STREAMLINED CORPORATE AUDIT PROCESS IS MEETING ITS GOALS 2 (2013), <http://www.gao.gov/assets/660/657092.pdf>; Amy Dunbar & Andrew Duxbury, *The Effect of CAP on Tax Aggressiveness*, in AN IRS-TPC RESEARCH CONFERENCE: ADVANCING TAX ADMINISTRATION, *supra* note 474, at 149; *but see* Leigh Osofsky, *Getting Realistic About Responsive Tax Administration*, 66 TAX L. REV. 121 (2012) (cautioning that CAP has weaknesses).

505. See, e.g., NAT'L ARBITRATION FORUM, BUSINESS-TO-BUSINESS MEDIATION/ARBITRATION VS. LITIGATION 1 (2005), <http://cdm16064.contentdm.oclc.org/cdm/ref/collection/p266901coll4/id/2834>.

506. David Parsly, *The Internal Revenue Service and Alternative Dispute Resolution: Moving from Infancy to Legitimacy*, 8 CARDOZO J. CONFLICT RESOL. 677, 678 (2007); U.S. GOV'T ACCOUNTABILITY OFF., GGD-97-71, IRS INITIATIVES TO RESOLVE DISPUTES OVER TAX LIABILITIES 2 (1997), <http://www.gao.gov/assets/230/224004.pdf>. See also *supra* notes 183–188 and accompanying text.

Appeals, it now offers mediation, arbitration, and rapid settlement procedures.<sup>507</sup> Taxpayers may use ADR before or after entering the formal Appeals process.<sup>508</sup> Appeals ADR programs appear to be underutilized, although statistics about particular programs are not available.<sup>509</sup> Transparency and information about the use or non-use of ADR at Appeals would be useful in evaluating possible ways to improve the program.<sup>510</sup>

### 5. *Change the IRS Mission*

In 1998, the IRS adopted a new mission statement:

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities by applying the tax law with integrity and fairness to all.<sup>511</sup>

In recent years, however, many have noted that the IRS has clearly suffered from mission creep, much of it mandated by Congress.<sup>512</sup> In addition to collecting taxes, the IRS now administers dozens of government programs that distribute government benefits; regulate non-profits, pensions, and health care; and subsidize activities such as renewable energy electricity generation.<sup>513</sup> Professor Kristin Hickman found that about a third of the IRS's recent regulatory efforts were concerned with programs and projects that are not associated with traditional revenue-raising; i.e., projects concerned with non-revenue-raising tax expenditures, the Patient Protection and Affordable Care Act (ACA), exempt organizations, employee benefits, and campaign

---

507. Ken Jones, *Appeals Arbitration: Not a Compelling Litigation Alternative*, 143 TAX NOTES 1059 (June 2, 2014) [hereinafter Jones, *Appeals Arbitration*]. See also Rev. Proc. 2003-41, 2003-1 CB. 1047 (announcing the availability of "fast-track" mediation for small business/self-employed taxpayers); Rev. Proc. 2003-40, 2003-1 C.B. 1044 (announcing the availability of "fast-track" settlement for large and mid-size business taxpayers); I.R.S., *Appeals Mediation Programs*, <http://www.irs.gov/Individuals/Appeals-Mediation-Programs> (last updated May 15, 2015).

508. Stephen Folan, *Even ADR Must Pay Its Dues: An Analysis of the Evolution of the Internal Revenue Service's ADR Programs and Where They Still Need to Grow*, 13 PEPP. DISPUTE RESOL. L.J. 281, 284-87 (2013).

509. Jones, *Appeals Arbitration*, *supra* note 507, at 1062.

510. Moreover, as already mentioned, Congress should expand the jurisdiction of the Appeals Office so that it could consider an appeal from virtually every IRS determination or action. See *supra* note 428 and accompanying text.

511. I.R.S., *The Agency, its Mission and Statutory Authority*, <http://www.irs.gov/uac/The-Agency,-its-Mission-and-Statutory-Authority> (last updated Jan. 23, 2015).

512. See, e.g., Coder, *The New IRS*, *supra* note 86, at 579.

513. See *supra* Part IV.B.2.

finances.<sup>514</sup> Professor Hickman found that “whether the focus is on documents, projects, or page counts, it is apparent that Treasury and the IRS commit substantial resources to adopting regulations that interpret, elaborate, and implement tax provisions aimed primarily at regulatory and social welfare programs, purposes, and functions rather than raising revenue.”<sup>515</sup>

Similarly, National Taxpayer Advocate Nina E. Olson has noted that “the trend toward requiring the IRS to administer social benefits in addition to its core tax administration duties increasingly diverts current IRS resources and diminishes taxpayer service.”<sup>516</sup> Olson has argued for a new mission statement that recognizes the IRS’s “dual role as part tax collector, part benefits administrator.”<sup>517</sup> Olson said that the mission statement is important for two reasons: “first, it serves as the organizing principle around which the IRS’s strategic plan is built, and second, a revised mission statement would make clear that the IRS will require sufficient funding to perform both roles well.”<sup>518</sup>

On the other hand, former IRS Commissioner Mortimer Caplin (1961–1964) would move the mission statement in the opposite direction, noting that “the IRS’s core purpose is to collect the proper amount of tax revenue in a fair, efficient, and impartial manner.”<sup>519</sup> Caplin laments that the current mission “does not even mention the collection of taxes.”<sup>520</sup>

Changing the IRS mission statement, whether to go back to a focus on revenue collection or to reflect the IRS’s actual dual role, is primarily a matter of symbolic value. If the IRS were to go back to its original mission, it could use that to object to the additional burdens placed upon it. If it were to adopt a dual mission, as Olson suggests, it could use that mission to request additional funding. Unfortunately, having slashed the IRS budget in recent years, Congress is unlikely to be swayed by either argument.<sup>521</sup>

---

514. Hickman, *Administering the Tax System We Have*, *supra* note 379, at 1748–49.

515. *Id.* at 1752–53.

516. NAT’L TAXPAYER ADVOCATE, FISCAL YEAR 2011 OBJECTIVES REPORT TO CONGRESS, at v (June 30, 2010), <http://www.irs.gov/pub/tas/nta2011objectivesfinal.pdf>.

517. Coder, *The New IRS*, *supra* note 86, at 577. If the IRS were to change its mission statement to reflect its dual role, would it also make sense to rename it the “Internal Revenue and Benefits Service?”

518. *Id.*; 2010 ANNUAL REPORT TO CONGRESS, *supra* note 86, at vol. 1, at 17.

519. Coder, *The New IRS*, *supra* note 86, at 579; I.R.S., *Previous IRS Commissioners*, *supra* note 362.

520. Coder, *The New IRS*, *supra* note 86, at 576.

521. *See supra* Part IV.A.

## VI. CONCLUSION

In this Article, we have explored many ways to help the IRS live within its shrinking budget. We continue to believe that taxpayers and the federal fisc would be best served by increasing the IRS budget in line with its vastly increased responsibilities. Our research has revealed that advice is one valuable commodity that the IRS has received in abundance. Taking all or a portion of the advice offered in this Article could help the IRS cope with its budget woes. However, if Congress continues to treat the IRS as a scapegoat for Congress's own failures and as the servant for its unfunded mandates, respect for the agency and compliance are both likely to continue to decline.