Harnessing Technology to Improve Tax Administration

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Three observations about tax administration:

- Too costly to audit more than a small fraction of taxpayers.
- Collect substantial amounts of data electronically, in the normal course of business.
- Many taxpayers want to comply, and would welcome help in doing so.
> How to manage in this environment?

> Create a National Fiscal Database.
  • Persons
  • Property
  • Expenditure and income
    – “One person’s expenditure leads to another person’s income thereby creating an ex-income audit trail.”

> Use it to verify taxpayer reports (modeling).

> Or, use it to pre-populate taxpayer accounts.
> Questions:

> How comprehensive and accurate would the database – especially the ex-income data – be?

> How would taxpayers respond to pre-populated reports?

> How costly would it be to assemble and process the data?
The Taxpayer Relief Act of 1997 made it more cost-effective for IRS to levy certain Federal payments.

- Provided for a “continuous levy” that may remain in effect until the debt is paid.
- Maximum amount is 15% of payment.
- Most taxpayers affected are Social Security recipients.
Building a Better Filter

> Social Security recipients may be vulnerable.
  > About a third of Social Security recipients depend on Social Security for virtually all of their income.

> IRS initially excluded Social Security recipients with low Total Positive Income (TPI).
  > About 55 percent of delinquent Social Security recipients.

> GAO (2003) argued that many of these taxpayers could pay their tax debts.

> IRS dropped the TPI filter in 2005; FPLP cases referred to the Taxpayer Advocate grew from 500 in FY 2004 to over 4,000 in FY 2006.
Building a Better Filter

> Options:

  > No filter

  > TPI filter using last tax return

  > Tax return + third party data income filter

  > Collection standards applied to “best income” filter

  > Other filters

> Which filter does the best job of separating those who can pay from those who cannot? How do we know?
Building a Better Filter

> Establish a benchmark for a “good” filter.
> Paper uses actual dispositions.

<table>
<thead>
<tr>
<th>Case Status/Filter Result</th>
<th>Cannot Pay</th>
<th>Can Pay</th>
</tr>
</thead>
<tbody>
<tr>
<td>Levy</td>
<td>28,420 (15%)</td>
<td>128,635 (67%)</td>
</tr>
<tr>
<td>Paid</td>
<td>785 (&lt;1%)</td>
<td>14,435 (8%)</td>
</tr>
<tr>
<td>Installment Agreement</td>
<td>935 (&lt;1%)</td>
<td>12,303 (6%)</td>
</tr>
<tr>
<td>Hardship waiver</td>
<td>952 (&lt;1%)</td>
<td>4,851 (3%)</td>
</tr>
</tbody>
</table>
Building a Better Filter

> Actual dispositions might not be the correct outcomes.

> Investigate the levy cases further.
  > “Accepting” a levy does not mean that hardship has not occurred.
  > Is IRS levying inappropriately, or is the filter exempting too many cases?

> Other data (e.g., experience with levying wages)?
Building a Better Filter

> Compare taxpayers excluded by each filter.

> What is the rationale and methodology behind alternative filters?

> Are there substantial differences in the numbers and types of taxpayers screened out by each filter?

> Can a fast, cheap, easily implemented filter perform nearly as well as a more complicated filter?
  • Looking for assets probably not productive.

> How do taxpayer circumstances change over time? Should cases be reevaluated? Annually?
A Lifetime of Electronic Filing

> First research goal: determine whether the Free File program acts as a gateway to electronic filing.

> Answer seems to be YES.


> 87% using Free File for 2005 and eligible to use Free File for 2006, filed electronically.

- 40 percent via Free File
- 11 percent via a paid preparer
- 36 percent on their own

> 73% of 2005 Free Filers filed electronically (including telefile) for 2004
Second research goal: identify market segments with the greatest potential for increasing participation in Free File.

> Young filers
> Self-prepared, V-coded return filers
> “Students”
A Lifetime of Electronic Filing

> Young filers

  > Shackleford (2007) finds younger filers prefer to get forms and information on-line.

  > Chu and Kovalick (2007) find that Free Filers are likely to be young.

  > Most taxpayers eligible to free file are young.

  > Thus, young filers account for the largest number of eligible non-participants as well as the largest group of participants.

  - 41% of Free Filers & 24% of non-participants are < age 25.
  - 24% of Free Filers & 21% of non-participants are age 25-34.

> Compare the characteristics of young participants and non-participants
A Lifetime of Electronic Filing

> Self-prepared, V-coded filers

> Hypothesize that V-coded filers would be receptive to Free File and electronic filing, because they are already using a computer to prepare their return

> 8.5 million such filers eligible for Free File

  • 2.8 million under age 25
  • 1.5 million age 25 – 34
  • 1.2 million aged 65 and older

> What else do we know about these filers? Why don’t they Free File and what would make them do so?
A Lifetime of Electronic Filing

> “Students”
  > Aged 18 – 24
  > AGI under $17,000
  > No EITC claimed
  > 48% filing on paper (compared to 40% of all taxpayers)
> A diverse group of taxpayers, including many who are low-wage workers, not students
> How do you reach them?
  > Use Form 1098-T or other data to identify students
  > Determine market share of students vs. non-students