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TAX REPORT
By TOM HERMAN



IRS Estimates of Unpaid Taxes Appear to Be Low, Report Says *April 26, 2006; Page D2*

The IRS may face an even bigger job in collecting unpaid taxes than earlier estimates indicated -- and is likely to feel additional pressure to intensify its crackdown on tax dodgers.

A new Treasury Department report, released yesterday, suggests that Internal Revenue Service estimates early this year probably were too low. In February, IRS researchers said the nation's "tax gap," or the difference between what the government collects and what it should be collecting, is around \$290 billion a year.

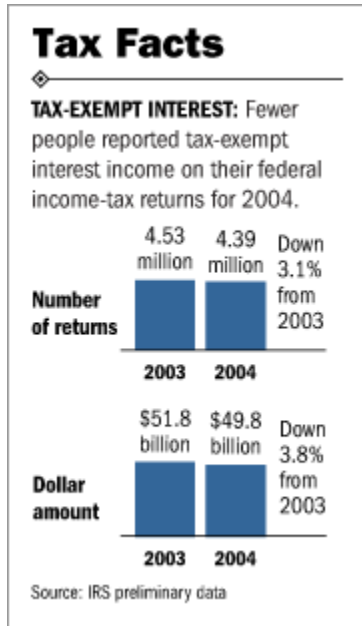
The Treasury report doesn't offer different numbers. But the report does point to areas that analysts say the IRS didn't cover in its report, or where information appears stale, and urges the IRS to do more research, including more rounds in the future of special types of taxpayer audits. The IRS says it generally agrees with that recommendation but won't say when it will do those audits or how many people will be involved.

The IRS "still does not have sufficient information to completely and accurately assess" the dimensions of the problem, concludes the report by the Treasury Inspector General for Tax Administration, or TIGTA.

The Treasury report, coupled with congressional concern about big budget deficits for years to come, is likely to add to pressure on the IRS to improve its research and fight tax fraud. IRS officials already have stepped up enforcement efforts, such as increasing audits.

"The IRS will have a hard time closing the tax gap as long as they don't know what the tax gap really is," says Sen. Max Baucus of Montana, the Finance Committee's ranking Democrat. Since the TIGTA report indicates the tax gap "may be even more" than the IRS's estimate, "there's really no more time for the IRS to waste."

The IRS's estimates earlier this year were based on a special study, the most



detailed in nearly 15 years. The IRS analyzed about 46,000 individual income-tax returns, chosen randomly from various income groups, for the 2001 tax year. The TIGTA report urged the IRS to conduct similar studies in the future on "a regular cycle" -- but didn't say when. In response to the TIGTA report, the IRS said "we generally agree" with that recommendation. Subject to "resource constraints," the IRS "will conduct reporting compliance studies on a regular basis for the foreseeable future."

Asked when and how many audits will be involved, an IRS spokesman said the agency "is still in the planning process on follow-up compliance studies" and that "no final decisions have been made."

Nobody knows precisely how much revenue the government loses each year because of tax cheating and other forms of noncompliance. For example, it's especially tough to figure out how much taxable income goes unreported and how many people who should be filing tax returns aren't doing so. It's also very difficult to sort out how much of the tax gap stems from outright cheating and how much is caused by taxpayer confusion over tax laws.

IRS officials have acknowledged that their tax-gap numbers, released initially last year and updated in February, aren't precise, and that some areas are still being studied.

The IRS came up with two general tax-gap measurements. First, there is the "gross" gap, or the difference between what the IRS thinks it should be collecting and what it actually does collect on a timely basis. The IRS estimated that gap to be about \$345 billion, with a "voluntary compliance rate" of about 83.7%. The IRS says its enforcement activities, coupled with other late payments, recover about \$55 billion of the tax gap, leaving a net tax gap of \$290 billion.

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SALES TAX RATES generally held steady last year.

The average state-tax rate fell slightly to 5.282% from 5.318% in 2004, says Vertex Inc. of Berwyn, Pa. (www.vertexinc.com¹). That's the second year in a row in which the average sales-tax rate has edged lower. The average county rate rose slightly last year to 1.678% from 1.653% in 2004, Vertex said. The average city rate rose to 1.589% from 1.585%.

Vertex says these averages are based on jurisdictions that impose a sales tax.

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BRIEFS: Jeff Yablon, a Washington lawyer at Pillsbury Winthrop Shaw Pittman, has updated his annual list of tax-related quotations for Tax Notes, a weekly publication. The list includes this observation by Will Rogers: "It is a good thing that we do not get as much government as we pay for."