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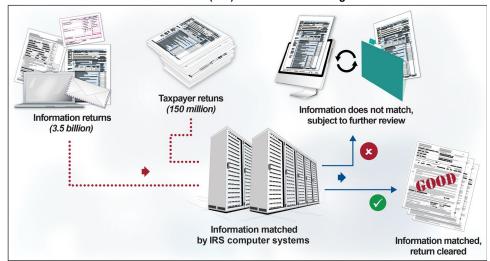
TAX ADMINISTRATION

Better Coordination Could Improve IRS's Use of Third-Party Information Reporting to Help Reduce the Tax Gap

Why GAO Did This Study

For tax year 2018, IRS received and processed more than 3.5 billion information returns that it used to facilitate compliance checks on more than 150 million individual income tax returns. By matching information reported by taxpayers against information reported by third parties, IRS identifies potential fraud and noncompliance.

GAO was asked to review IRS's use of information returns. This report provides an overview of information returns and assesses the extent to which IRS has a coordinated approach to identifying and responding to risks related to the use of information returns in the tax system, among other objectives.

GAO reviewed IRS documents and data on information returns filing, processing, and use, and interviewed cognizant officials. GAO compared IRS's efforts in this area to federal internal control standards, and IRS's strategic plan.

What GAO Recommends

GAO is making nine recommendations to IRS, including that IRS revise its modernization plans for its information returns processing systems and incorporate it into broader IT modernization efforts and develop a collaborative mechanism to improve coordination among IRS groups that use information returns. IRS neither agreed, nor disagreed with the recommendations; however, IRS outlined actions it plans to take to address the recommendations. Social Security Administration had no comments.

View GAO-21-102. For more information, contact James R. McTigue at (202) 512-9110 or McTigueJj@gao.gov.

What GAO Found

Information returns are forms filed by third parties, such as employers and financial institutions that provide information about taxable transactions. These forms are submitted to the Internal Revenue Service (IRS), the Social Security Administration, and taxpayers. Fifty unique types of information returns provide information on individual taxpayers and have a variety of purposes, such as reporting on wages earned or amounts paid that qualify for a tax credit or deduction. IRS identifies mismatches between information returns and tax returns for potential additional review, including enforcement actions. According to IRS research, taxpayers are more likely to misreport income when little or no third-party information reporting exists than when substantial reporting exists.

Overview of Internal Revenue Service's (IRS) Process for Matching Information Returns

Source: GAO analysis of tax year 2018 IRS information. | GAO-21-102

IRS's ability to process and use information returns is limited by its outdated legacy information technology (IT) systems. In 2017, IRS developed a plan to modernize its information return processing systems; however, IRS paused its efforts due to, according to IRS, resource constraints. IRS has an opportunity to capitalize on prior planning efforts by re-evaluating and updating these efforts and integrating them into its broader IT modernization efforts.

IRS does not have a coordinated approach with cross-agency leadership that strategically considers how information reporting could be improved to promote compliance with the tax code. While information returns affect many groups across IRS and support multiple compliance programs, no one office has broad responsibility for coordinating these efforts. A formalized collaborative mechanism, such as a steering committee, could help provide leadership and ensure that IRS acts to address issues among the intake, processing, and compliance groups. For example, IRS has not undertaken a broad review of individual information returns to determine if thresholds, deadlines, or other characteristics of the returns continue to meet the needs of the agency.

_____ **United States Government Accountability Office**