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## Congress Will Push IRS to Get Tougher with Scofflaws

*The IRS will become more of a heat-seeking missile in the way it targets who gets audited.*

By Joan Pryde

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**The Internal Revenue Service will work harder to catch more deadbeats.** Under pressure from lawmakers who need revenue, the agency is launching a new effort to reduce noncompliance among individual taxpayers. The tax gap -- the difference between what the IRS collects and what folks should be paying -- keeps rising and is now estimated at more than \$300 billion a year. That's larger than this year's federal deficit.

**To narrow the gap, the IRS will do more audits -- and do them smarter.** To nab all scofflaws would take millions more exams, which Congress won't be willing to fund and taxpayers would never tolerate. So instead, the Service will target specific areas where noncompliance is high. That way it will get more bang for its audit buck.

Look for the IRS to follow a road map from congressional investigators who recently identified the best audit targets. The Government Accountability Office says the percentage of misreporting by taxpayers is unusually high among the following groups:

- Sole proprietors, who often underreport income and inflate write-offs.
- S corporations and partnerships, especially S company owners who take dividends instead of salaries to minimize payroll tax liability.
- Gamblers who may underreport their winnings or who subtract losses from winnings instead of reporting them as miscellaneous itemized deductions, as the law requires.
- Part-time farmers, who aren't supposed to use losses from farming to reduce their other income if they're just pursuing a hobby and not running a business.
- Taxpayers who itemize deductions on Schedule A. Errors occur most often with medical costs, charitable contributions and job-related expenses.
- Earned income tax credits taken by individuals who don't qualify.
- Investors who don't report capital gains properly. These include gains on sales of vacation homes, rental units, business property and farmland.

Another part of the IRS strategy is to do a few thousand random audits every year to find new areas to investigate. In the past, the IRS has fine-tuned the audit process by waiting several years before doing a

big batch of line-by-line audits. Obtaining fresh compliance data each year instead of twice a decade or so will help the Service spot compliance problems faster. Bringing the audit formulas up to date will also hike revenue and reduce the likelihood of exams that result in no change.

Congress will help by giving the IRS more tools to tackle noncompliance, particularly in the area of information reporting. By one estimate, about 50% of income not shown on a W-2 or a Form 1099 goes unreported. So lawmakers will require firms to file 1099s for payments of \$600 or more to corporations. And to help the IRS track capital gains, Congress will make brokers report basis when securities are sold. Also look for lawmakers to increase penalties imposed on users of abusive tax shelters and to give the IRS more funds to upgrade the computers it uses to detect fraud.

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