

"WORKING PAPER"

WHY NOT AMNESTY?

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WHY NOT AMNESTY?

An idea that keeps cropping up purports to turn tax evaders into taxpayers giving the Treasury an infusion of revenue at a fraction of the administrative cost of the regular audit process. What's more, it may provide the base for increased future revenues as well by keeping a good portion of the "forgiven" on the tax rolls. The idea is tax amnesty. Recently it has been tried by a number of states generally with more success than anticipated. It is not, however, a popular subject with IRS Commissioner Egger, who is deadset against it.

Why not a national tax amnesty if it would improve compliance and make even a small dent in the megabuck deficit?

State Experience.

Over the last two years, a number of states have conducted short-term--usually two to three month--tax amnesty programs. While details of the programs differ, the typical pattern has been to offer tax delinquents and nonfilers a "one-time" chance to pay up without penalties or criminal prosecution. Payment of all back taxes and interest thereon usually has been required and those with civil or criminal cases for state tax violations pending were excluded from amnesty.

The response has been heavy in some major industrial states, in particular, California, Illinois, Massachusetts and Minnesota. The Massachusetts program, started in late 1983 and probably the most publicized, drew 47,000 taxpayers out of the woodwork. About two-thirds were individual income taxpayers and about one-third were nonfilers, some never having filed a state income tax return. Others paid up for underreporting income--the most

common evasion--overstating business expense, or just falling behind in making tax payments because of personal and professional economic problems.

In most of the states individual income taxpayers made up the bulk of responses but numerous corporate taxpayers came forth too, some with substantial payments. The most typical corporate transgression apparently was underpayment of sales taxes--still a difficult area of compliance for business, particularly out-of-state business.

The table below shows the overall results of amnesty in four industrial states all with significant income tax structures. Any amnesty program at the Federal level presumably would have the maximum impact on income taxes.

STATE TAX AMNESTY RECEIPTS

State	Period	Total Receipts (\$ mil.)	Income Tax Related Receipts (\$ mil.)	Income Tax Related Receipts as % of Total Fiscal 1984 Income Tax Revenues
California	Dec 1984- Feb 1985	144	103	0.8%
Illinois	Oct-Nov 1984	154	121	3.4%
Massachusetts	Aug-Oct 1984	85	52	1.5%
Minnesota	Aug-Oct 1984	12	9	0.3%

Sources: State Taxpayer Research Organizations
and Tax Foundation, Incorporated, Facts and Figures 1985.

All of the above programs were deemed successful in that they exceeded expectations of receipts. With the exception of Illinois, however, the amounts collected were all below two percent of the respective income tax base. In conjunction with the amnesty program all four states stepped up enforcement programs such as intensified auditing, stiffer reporting

requirements and larger penalties for noncompliance. These were publicized widely concurrent with the amnesty period as the "carrot and stick" approach. In Missouri, where amnesty results were disappointing, there was no special promotion of the program and some officials blamed this for the relatively poor showing.

Massachusetts conducted a high visibility campaign about both its amnesty and new enforcement measures. The state attributed a large revenue pickup in fiscal 1984, beyond the direct results of amnesty for back taxes and beyond what could be expected from economic growth, as a result of this campaign. Its administrative cost of the amnesty program itself ran somewhat over \$1 million.

Potential Federal Results.

The IRS position notwithstanding, suppose we did run a national tax amnesty along the lines proposed by Rep. Brian Donnelly (D-MA). His bill, H.R. 2530, would provide a one-time, three-month amnesty based on the Massachusetts experience coupled with more IRS enforcement powers and hiring of an additional 7,500 enforcement personnel. Disregarding the possible application of such a program to social security, estate and gift, and Federal excise taxes, what would be the potential revenue consequences for income taxes? The unweighted average of the four state programs listed above was 1.5 percent of the existing revenue base. If applied to fiscal 1985 Federal income tax receipts, personal and corporate, that would yield \$5.9 billion, and perhaps half that could be considered a permanent addition to the revenue base.

Policy Issues.

An oft-stated argument against amnesty is that it sends honest taxpayers the wrong signal--that you can get away with tax cheating. The IRS

Commissioner never fails to emphasize this. Not too long ago, of course, the IRS was extremely reluctant to admit that there was any significant tax evasion problem and to attach any numbers to it. Now, it is readily conceded that we have uncollected taxes in the legal economic sector on the order of \$100 billion--a lot of it probably beyond the reach of compliance measures no matter how sophisticated.

The states with successful amnesty programs claim that regular taxpayers don't object to letting the cheaters and delinquents off the hook on a one-time basis if they still must come up with all back taxes and interest. (Some amnesties, however, have allowed partial interest forgiveness.)

Of more concern to Congress, perhaps, would be giving the IRS significant additional enforcement power, especially large numbers of additional agents to pry into people's financial affairs. Despite the increased penalties and reporting requirements under the 1982 and 1984 tax acts, there is still much reluctance to extend the tax collector's reach over personal financial matters on a broad scale. Witness the most recent flap over car logs.

One enhanced enforcement potential should not be controversial and could be quite helpful. All the states conducting amnesty have agreed to provide IRS with information on their tax delinquents. Presumably any national amnesty would do the same for all states.

If a national amnesty were to be seriously considered, logically it should be in conjunction with major tax reform stressing simplicity and fairness, at least in the individual sector. The "carrot and stick" would seem to work best with a fresh start on the whole system. There is no guarantee, of course, that the current reform campaign will fulfill that condition.

The direct revenue implication of a national tax amnesty does appear small in relation to our current deficit. As amnesty is basically a gimmick and apparently works well only in consonance with stern enforcement measures, some will say it is just not worth the effort unless a much higher dollar return can be anticipated. But the deficit problem remains and there is no sign of its resolution on a business-as-usual basis.

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