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INTRODUCTION

Most small business and self-employed taxpayers cheat on their taxes. In fact, in the aggregate, they fail to pay about half the tax they owe to the federal government, and this unpaid tax amounts to roughly $150 billion annually. This figure is about half of the "tax gap," or the amount of tax due that the federal government does not collect.

This Article argues that more salient government communications and greater attention to principles of influence would improve existing and proposed policies to encourage self-employed and small business taxpayers to pay their taxes. Reversing widespread tax evasion among self-employed and small business taxpayers requires changing the existing social norm of noncompliance, which in turn demands a better connection between the government's message and the experience of the taxpayers. Policymakers should recraft their anti-tax-gap messages so that they grab the attention of the target audience. Policymakers should also take advantage of established influence tools to leverage predictable taxpayer heuristics such as conformity to the compliance behavior of similar peers and availability bias.

This Article contains five parts. Part I describes the details and limitations of several existing tax-gap-closing approaches relevant to self-employed and small business taxpayers: third-party reporting, audit, whistleblower rewards, and gatekeeper strategies. Part II outlines the concepts of salience and influence and places them in the context of proposals to address or close the tax gap. Part III considers how salience and the influence principle of social proof could improve government messages to taxpayers about taxpaying obligations and

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audit risks, and to tax preparers about diligence requirements. Part IV outlines strategies based on the influence principles of reciprocity and commitment consistency, which could help the government initiate and maintain productive relationships with taxpayers. Part V points out several complications that could emerge from government use of such salience and influence strategies: measurement and cost-benefit analysis, the uncertain place of such strategies in the budget process, and the awkwardness of implementing strategies that might involve the use of stereotypes.

I. EXISTING PROPOSALS TO NARROW THE TAX GAP

A. Who Cheats and Why?

The tax gap data gathered by U.S. Treasury and the Internal Revenue Service (IRS) show that many self-employed and small business taxpayers cheat on their taxes. For example, the government estimates that income, employment, and estate tax underpayments by sole proprietors, who are largely self-employed and small business taxpayers, made up about fifty percent of the $345 billion gross tax gap in 2001.[1] In addition, such taxpayers pay only about half their taxes. Non-farm proprietor income has a misreporting rate of fifty-seven percent which compares to a rate of only one percent for wage income subject to withholding and information reporting and similarly low rates for other items subject to at least some reporting.[2] The headline is clear: individuals with business income evade taxes and make a large contribution to the tax gap.

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1. INTERNAL REVENUE SERV. & DEP'T OF THE TREASURY, A REPORT ON IMPROVING VOLUNTARY COMPLIANCE 12 (Aug. 2, 2007) [hereinafter IRS 2007 TAX GAP REPORT] (reporting estimates based on National Research Program (NRP) data). The net tax gap, after audit and collections activity, amounts to about $290 billion annually. *Id.* at 1. Tax gap estimates from raw data are adjusted upward to account for factors including the difficulty of detecting misreporting of cash income. *See* Eric Toder, *What is the Tax Gap?*, 117 TAX NOTES 367, 371 (Oct. 22, 2007) (explaining that low-visibility income such as sole proprietor income is adjusted upward by a multiplier of between 3.3 and 4.2). A number of factors feed into the fifty percent calculation, including individuals' business income tax underreporting ($109 billion), and payroll, employment, and self-employment tax underreporting ($80 billion). *See* IRS 2007 TAX GAP REPORT, *supra*, at 12–13.

2. *See* IRS 2007 TAX GAP REPORT, *supra* note 1, at 14 (reporting figures). This report categorizes items by visibility and concludes that income subject to both reporting and withholding, such as wages, has a misreporting percentage of only one percent; income subject to substantial information reporting, such as interest and dividends, has a misreporting percentage of five percent; items subject to some information reporting, such as partnership income and deductions, have a misreporting percentage of nine percent; and items subject to little or no reporting, such as sole proprietor business income, have a much larger rate of misreporting, fifty-four percent. *See id.*

Opportunity provides one important reason for noncompliance among self-employed and small business taxpayers. Self-employed and small business taxpayers often receive substantial cash revenue,[3] and earnings often either lack a third-party reporting requirement or have a frequently-ignored reporting requirement.[4] Not surprisingly, social science and empirical studies confirm that income visibility is an important determinant of tax compliance[5] and that reporting requirements significantly reduce tax cheating.[6]

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3. *See* Joseph Bankman, *Eight Truths About Collecting Taxes from the Cash Economy*, 117 TAX NOTES 506, 506 (Oct. 29, 2007) (distinguishing between cash and non-cash components of the economy and applicable effective tax rates).

4. Payments made to self-employed and small business taxpayers in the course of the payer's business are reportable on Form 1099-MISC. *See* I.R.C. § 6041(a) (2006). But there are significant gaps in reporting. For example, amounts paid by consumers as opposed to businesses are not reportable under Section 6041, which requires reporting of payments of $600 or more to "[a]ll persons engaged in a trade or business and making payment in the course of such trade or business to another person." I.R.C. § 6041(a). In addition, determining whether the law requires the filing of a 1099-MISC and managing the logistics of filing the form can present difficulties. *See* U.S. GOV'T ACCOUNTABILITY OFFICE, TAX GAP: A STRATEGY FOR REDUCING THE GAP SHOULD INCLUDE OPTIONS FOR ADDRESSING SOLE PROPRIETOR NONCOMPLIANCE 6–7, 17–18 (July 2007) [hereinafter GAO SOLE PROPRIETOR REPORT] (explaining the inconvenience and spotty coverage of 1099-MISC reporting). The low $50 penalty for violating Section 6041 may also contribute to payers' willingness to ignore it. *See* I.R.C. § 6721 (imposing a $50 penalty for failure to file an information return and also imposing a penalty of $100 or, if greater, ten percent of the aggregate amount of the items required to be reported for a failure to file an information return due to intentional disregard); *see also* I.R.C. § 6724(d)(1)(A)(i) (defining information return to include returns required under I.R.C. § 6041(a)).

5. *See, e.g.*, *Understanding Taxpayer Compliance: Self-Interest, Social Commitment, and Other Influences*, *in* TAXPAYER COMPLIANCE: AN AGENDA FOR RESEARCH 71, 112–13 (Jeffrey A. Roth et al. eds., 1989) [hereinafter TAXPAYER COMPLIANCE] (reporting that taxpayers are more likely to report visible income); James Andreoni et al., *Tax Compliance*, 36 J. ECON. LITERATURE, 818, 841–43 (1998) (summarizing studies indicating that "noncompliance is discouraged by a high risk of detection"); Gregory A. Carnes & Ted D. Englebrecht, *An Investigation of the Effect of Detection Risk Perceptions, Penalty Sanctions, and Income Visibility on Tax Compliance*, 17 J. AM. TAX'N ASS'N 26, 39 (1995) (noting that income source strongly influences the perceived likelihood of detection).

6. For example, a study of 1992 income tax payments concluded that employees reported 99.1% of their wage income subject to withholding, that recipients of interest income subject to reporting reported 97.7% of such income, that sole proprietors reported 67.7% of their income, and that informal suppliers such as housepainters and babysitters reported just 18.6% of their income. *See* JOEL SLEMROD & JON BAKIJA, TAXING OURSELVES: A CITIZEN'S GUIDE TO THE GREAT DEBATE OVER TAX REFORM 178 (2d ed. 2001). *See generally* Maryann Richardson & Adrian J. Sawyer, *A Taxonomy of the Tax Compliance Literature: Further Findings, Problems and Prospects*, 16 AUSTL'N TAX F. 137, 168 (2001) (describing literature showing that income source is an important tax compliance factor). The likelihood of detection fits comfortably into the classic economic analysis of taxpayer behavior. This frames a tax compliance decision as a comparison between (1) the cost of paying tax, and (2) the difference between the benefit of avoiding the tax and the cost of the imposition of tax, interest, and penalties, risk-adjusted for the possibility that the government will successfully challenge the tax avoidance strategy and perhaps adjusted for other factors such as risk aversion. *See generally* Michael G. Allingham & Agnar

Social norms can also influence noncompliance.[7] Work by social scientists specific to the problem of tax compliance has consistently demonstrated that taxpayers who believe their peers are noncompliant are less likely to comply themselves.[8] The relationship between group norms, individual ethics, and taxpayer behavior is complicated. For example, although it is possible that group norms influence individual taxpayer compliance decisions, causality could also run the other way, so that a noncompliant taxpayer might use peer behavior to defend a prior decision not to comply, or might seek out noncompliant peers.[9]

The social norm of noncompliance has such strength for small business and self-employed taxpayers that the use of the phrase "tax evasion" to describe their failure to pay tax on unambiguous income sometimes meets resistance. Some research suggests that these taxpayers' mental processes do not reflect intentional stealing from the government, but instead involve mental habits that categorize cash receipts as belonging fully to the taxpayer, for example, and not partly to the government.[10] Still, the core noncompliance paradigm explored in this Article—the nonpayment of tax on cash business income—plainly meets the statutory definition of tax evasion, and sometimes the Article refers to it as such.

The image of a misreporting taxpayer as the owner of a corner store or local construction business may also prompt hesitation about whether the government should crack down on such taxpayers.[11] Self-employed

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Sandmo, *Income Tax Evasion: A Theoretical Analysis*, 1 J. PUB. ECON. 323–38 (1972).

7. *See, e.g.*, Benno Torgler, *Speaking to Theorists and Searching for Facts: Tax Morale and Tax Compliance in Experiments*, 16 J. ECON. SURV. 657, 663–66 (2002) (describing studies connecting group decisionmaking or cultural differences to individual tax compliance decisions).

8. *See* TAXPAYER COMPLIANCE, *supra* note 5, at 112–13; Richardson & Sawyer, *supra* note 6, at 173–77.

9. *See* TAXPAYER COMPLIANCE, *supra* note 5, at 112–13; Richardson & Sawyer, *supra* note 6, at 174. However, one study based on longitudinal survey data suggests that a causal link, in addition to a correlation, exists, and that taxpayers internalize the taxpaying norms of a group with which the taxpayer strongly identifies. *See* Michael Wenzel, *Motivation or Rationalisation? Causal Relations Between Ethics, Norms and Tax Compliance*, 46 J. ECON. PSYCHOL. 491, 504–05 (2005). Another recent study comparing taxpayers in different European countries reports a high correlation between taxpayers' compliance and their perception of others' compliance and concludes after some statistical analysis that the data suggests that the perception of others' behavior drives compliance decisions, not the other way around. *See* Bruno S. Frey & Benno Torgler, *Tax Morale and Conditional Cooperation*, 35 J. COMP. ECON. 136, 146, 152 (2007).

10. *See, e.g.*, Paul Webley et al., *Value Added Tax Compliance*, *in* BEHAVIORAL PUBLIC FINANCE 175, 182, 187 (Edward J. McCaffery & Joel Slemrod eds., 2006) (noting interview and survey results suggesting that under some small business owners' mental accounting processes, VAT revenues come out of the business owner's own funds).

11. *See* Joseph Bankman, *Tax Enforcement: Tax Shelters, The Cash Economy, and Compliance Costs*, 31 OHIO N.U. L. REV. 1, 7 (2005) ("Many undoubtedly feel that the cash economy is a less appealing target for increased enforcement than tax shelters."). 2006 survey

individuals and small business owners operate under a systematic disadvantage in that they lack economies of scale when paying for inventory or supplies, health insurance, fixed regulatory costs, and numerous other items. Moreover, some may provide a local, 'Main Street' consumption experience that deserves categorization as a subsidy-deserving public good.[12]

However, the roughly fifty percent income tax break that evasion provides to cash businesses is huge, and underreporting also reduces employment and sales taxes in many cases.[13] Even if the operation of a small business is a public good that deserves a subsidy, the existing government subsidies (including both significant tax incentives[14] and nontax programs)[15] do not achieve the desired level of public good, and the tax system would best implement an additional subsidy,[16] a well-designed subsidy would be smaller, transparent, and available regardless of a taxpayer's taste for tax evasion. The current ability of cash businesses to evade tax presents a large incentive to engage in

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results showed that eighty percent of respondents thought it "very important" that corporations were reporting and paying their taxes honestly; a lower percentage, sixty-eight percent, gave the same response with respect to small businesses. *See* IRS OVERSIGHT BOARD, 2006 TAXPAYER ATTITUDE SURVEY 3 (2007), *available at* http://www.treas.gov/I.R.S.ob/reports/2006_taxpayer_attitude_survey.pdf.

12. *See* Lily L. Batchelder et al., *Efficiency and Tax Incentives: The Case for Refundable Tax Credits*, 59 STAN. L. REV. 23, 42–43 (2006) (noting that numerous tax provisions aim "to correct for positive externalities").

13. *See* IRS 2007 TAX GAP REPORT, *supra* note 1, at 11 (noting the link between income and employment tax evasion among sole proprietors). *See also* Susan Cleary Morse et al., *Cash Businesses and Tax Evasion*, 20 STAN. L. & POL'Y REV., at Part III.B (forthcoming 2009) (reporting interview results indicating that income, sales, and employment tax evasion moved in tandem).

14. Incentives on the books include the ability to expense certain depreciable property, *see* I.R.C. § 179; a fifty-percent exclusion for certain small business stock gain, *see* I.R.C. § 1202, although part of this exclusion is an alternative minimum tax preference, *see* I.R.C. § 57(a)(7); ordinary treatment for certain small business stock losses, *see* I.R.C. § 1244; and the availability of a pass-through organization as a sole proprietor, partnership, or S corporation to a non-publicly traded entity. *See, e.g.*, Treas. Reg. § 301.7701-3(a) (permitting business entities that do not meet the definition of corporation to elect to be taxed as partnerships or disregarded entities). *See also* I.R.C. § 1361 (defining an S corporation); § 1362 (permitting S corporation election).

15. For example, the Small Business Administration provides disaster assistance, loan guarantees, and some government contract bidding advantages. *See* N. ERIC WEISS, CONGRESSIONAL RESEARCH SERV., SMALL BUSINESS ADMINISTRATION: A PRIMER ON PROGRAMS 3, 5 (2006), *available at* http://www.opencrs.com/rpts/RL33243_20060120.pdf.

16. *Compare* Stanley S. Surrey, *Tax Incentives as a Device for Implementing Government Policy: A Comparison with Direct Government Expenditures*, 83 HARV. L. REV. 705, 734–35 (1970) (criticizing enactment of tax expenditures for lack of transparency and lack of expertise), *with* Edward A. Zelinsky, *James Madison and Public Choice at Gucci Gulch: A Procedural Defense of Tax Expenditures and Tax Institutions*, 102 YALE L.J. 1165, 1194–95 (1993) (arguing that the generalist committees that oversee tax expenditures can better avoid special interest group capture).

business in cash, which results in a misallocation of resources to cash businesses and perhaps little ultimate benefit to the owners or employees of evading businesses.[17]

But what government action would work to deter self-employed and small business taxpayers from underreporting their cash revenues? The government's September 2006 and August 2007 white papers recommend a seven-point strategy: reduce evasion opportunity, increase research, improve information technology, improve audit and related activities, improve taxpayer service, reform and simplify the law, and coordinate with state and foreign governments and other stakeholders.[18] Yet only some of these proposals are relevant, and they cannot fully address the problem.

Although influence tools do not figure prominently on this seven-point list, the government implicitly embraces influence strategies at several points. For example, proposals to improve taxpayer service and education[19] are important not only as a tool to correct taxpayer misunderstandings about legal requirements,[20] but also as a reciprocal influence strategy.[21] In addition, Treasury has acknowledged the potential of audit activity to achieve broad deterrence,[22] which implicates tools of publicity and influence.[23]

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17. *See* Bankman, *supra* note 11, at 7–8 (explaining that the lower effective tax rate for cash businesses produces lower before-tax wages and lower before-tax investment returns for cash businesses by encouraging over-investment and over-employment in that sector). *But see* Joel Slemrod, *Small Business and the Tax System*, *in* THE CRISIS IN TAX ADMINISTRATION 69, 70 (Henry J. Aaron & Joel Slemrod eds., 2004) (outlining the argument that lower de facto small business tax rates offset regressive tax and other compliance costs).

18. *See* DEP'T OF THE TREASURY, OFFICE OF TAX POLICY, A COMPREHENSIVE STRATEGY FOR REDUCING THE TAX GAP 2–4 (2006) [hereinafter TREASURY 2006 TAX GAP REPORT] (recommending (1) reducing evasion opportunity through mechanisms including third-party reporting and more stringent ethical requirements for practitioners; (2) making a multi-year commitment to research; (3) improving information technology; (4) improving matching, audit and collection activities; (5) improving taxpayer service; (6) reforming and simplifying the tax law; and (7) coordinating with state and foreign governments, practitioner groups, and other stakeholders).

19. *See, e.g.*, *id.* at 14–15 (including taxpayer service enhancement among its tax gap closing strategies); *see also* CAL. FRANCHISE TAX BD., TAX GAP PLAN: A STRATEGIC APPROACH TO REDUCING CALIFORNIA'S TAX GAP 21 (2006) (setting the goal of "becom[ing] more innovative in attacking the tax gap").

20. *See* IRS 2007 TAX GAP REPORT, *supra* note 1, at 4 ("Service is especially important to help taxpayers avoid unintentional errors.").

21. *See infra* Part IV.B (discussing reciprocity).

22. *See infra* text accompanying notes 122–24 (describing government press releases).

23. *See infra* Part III.B (discussing publicity of enforcement activities as a social proof tool). In a somewhat similar vein, the GAO has suggested sending targeted "soft notices" to self-employed and small business taxpayers who may have potential compliance issues, but whom the government does not plan to audit. *See* GAO SOLE PROPRIETOR REPORT, *supra* note 4, at 59

Finally, the National Taxpayer Advocate, Nina Olson, has included serious consideration of behavioral factors relevant to tax compliance in her office's research program. For example, Professor Marjorie Kornhauser wrote a chapter in the office's 2007 annual report in which she recommended that the IRS create a group to research tax morale and implement tactics including taxpayer education and multifaceted publicity campaigns.[24] But neither the Treasury nor the IRS has publicly adopted such policies.

Despite these nods to influence strategies, most policymakers do not appear to think systematically about compliance norm development.[25] In particular, salience and influence strategies are not usually featured as a centerpiece of the tax-gap-closing proposals made by other commentators. This Article aims to help fill that gap by considering specific salience and influence ideas to enhance and supplement existing tax-gap-closing proposals. But first, the remainder of this Part outlines several other proposals relevant to the issue of cash business tax evasion: expanded third-party reporting; better audit selection strategies facilitated by information technology and partnerships with other governments; whistleblower or *qui tam* provisions; and gatekeeper strategies aimed at tax preparers.[26]

B. Third-Party Reporting

Currently, the statutory requirement to report certain payments to independent contractors on Form 1099 constitutes the main third-party reporting mechanism for income earned by small business or self-employed taxpayers.[27] Some tax-gap-closing proposals recommend

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(listing pros and cons of sending such soft notices). The GAO's suggestion to communicate that taxpayers should "recheck . . . filed tax returns or change . . . reporting on future returns" also appears to aim to increase taxpayers' perception of the likelihood of audit. *Id.*

24. *See* Marjorie Kornhauser, *Normative and Cognitive Aspects of Tax Compliance: Literature Review and Recommendations for the IRS Regarding Individual Taxpayers*, *in* 2 NAT'L TAXPAYER ADVOCATE, 2007 ANNUAL REPORT TO CONGRESS (2008) 138, 157–58 (summarizing recommendations on tax morale).

25. Some contributions from IRS researchers do seriously consider behavioral issues. *See, e.g.*, Sagit Leviner, *An Overview: A New Era of Tax Enforcement—From "Big Stick" to Responsive Regulation*, 2 REG. & GOVERNANCE 360, 365 (2008).

26. The proposal to reform and simplify the tax code is not relevant to the unambiguous problem of failing to report cash income. *See* Bankman, *supra* note 11, at 8 ("[T]he evasion [by cash businesses] is not—how shall I put this—subtle. It involves false books, false reporting, safety deposits full of cash, and so on."). The proposal for additional research, although it has not yet generated a concrete set of proposals, is relevant here insofar as this Article attempts to build on existing tax compliance research.

27. *See* I.R.C. § 6041 (requiring reporting by "persons engaged in a trade or business" to certain recipients, including individuals, of $600 or more annually). *See also* Treas. Reg. § 1.6041-3(p) (2006) (providing that payments to corporations and various other entities do not

extending third-party reporting to new categories of self-employment and small business income, such as payments to corporations,[28] payments by consumers[29] or governments,[30] or payments totaling less than $600 annually.[31] Another idea is to require line-item listing of items subject to third-party reporting requirements on tax returns to facilitate automated matching by the government.[32] A third category of reporting proposals would require firms that process payments, such as credit card companies, eBay and other online brokers, and banks, to report them.[33]

Third-party reporting proposals aim to eliminate taxpayers' opportunities to omit revenue from taxable income, consistent with data demonstrating that taxpayers pay tax on reported items of income at rates in excess of ninety percent.[34] But there are at least three problems with additional third-party reporting. First, its costs are perceived to exceed its benefits. Second, and partly as a result of the first issue, there appears to be little political will to enact sweeping third-party reporting requirements. Third, there is likely no popular or political appetite for restricting the use of traceless cash in transactions.

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require reporting under Section 6041).

28. *See, e.g.*, DEP'T OF THE TREASURY, GENERAL EXPLANATIONS OF THE ADMINISTRATION'S FISCAL YEAR 2008 REVENUE PROPOSALS 63 (2007) [hereinafter 2008 BLUEBOOK] (proposing such reporting to corporations and estimating a resulting revenue gain of $7.7 billion over ten years).

29. *See* GAO SOLE PROPRIETOR REPORT, *supra* note 4, at 51–52 (discussing a proposal to require reporting by consumers); Bankman, *supra* note 3, at 509, 512–13 (noting that an Australian consumer reporting initiative failed in the face of popular objections); Joshua Rosenberg, *Narrowing the Tax Gap: Behavioral Options*, 117 TAX NOTES 517, 523–24 (Oct. 29, 2007) (discussing consumer reporting).

30. *See* 2008 BLUEBOOK, *supra* note 28, at 69 (proposing requiring governments to report all non-wage payments made in exchange for property and services, with a revenue estimate of $390 million over ten years).

31. *See* GAO SOLE PROPRIETOR REPORT, *supra* note 4, at 48–49 (discussing a proposal to require reporting of amounts under $600).

32. *See id.* at 48 (discussing proposal to break out gross receipts sums on sole proprietor tax returns). *See also* Martin A. Sullivan, *Economic Analysis: Treasury Expects Billions From Credit Card Reporting Proposal*, 115 TAX NOTES 890, 891 (June 4, 2007) (noting that automatic matching of income items reported by third parties requires separate listing on tax returns).

33. *See* I.R.C. § 6050W (requiring reporting of payments processed by a "third party network" or by a bank through a credit or debit card arrangement); Notice 2009-19, 2009 I.R.B. LEXIS 106 (noting the law's effective date of January 1, 2011).

34. *See supra* note 2 (citing compliance figures). As Professor Leandra Lederman has noted, third-party reporting is the most visible of a number of ways, including certain subtle structural ways, in which third parties support tax compliance. *See* Leandra Lederman, *Statutory Speed Bumps: The Roles Third Parties Play in Tax Compliance*, 60 STAN. L. REV. 695, 698–99 (2007) (discussing the enforcement benefits that merit better treatment for third-party verified items such as reimbursed expenses).

With respect to the cost-benefit point, potential third-party payers have strenuously argued that reporting proposals could generate significant costs for initial system overhauls as well as significant ongoing expenses. The large institutional third-party payers targeted by the legislative proposals in the administration's 2008 budget objected that the expected benefits did not merit compliance costs,[35] causing Treasury officials to retreat from the proposals.[36] In addition, for large and small potential reporters, information reporting is a complicated and confusing exercise requiring difficult determinations, like whether a service provider is an employee or an independent contractor,[37] possibly implicating privacy concerns.[38]

The revenue estimates that have accompanied recent third-party reporting proposals also suggest that these costs may not result in significant additional tax revenues. For example, the seven information reporting proposals in the Bush administration's 2008 budget taken together would generate only $30 billion over ten years, or less than one

35. *See, e.g.*, Statement of Timothy J. McCormally, Executive Director of Tax Executives Institute, Inc., before the IRS Oversight Board, Mar. 7, 2007, at 5 (arguing that expanding third-party reporting would impose significant time, financial, and "intrusion" burdens, including changes to information systems, on large corporate payers that are themselves compliant and that costs and benefits should be weighed, compensation considered, and the IRS ability to use the information demonstrated); Martin Vaughan, *Ebay Battling Treasury Demands For Internet Sales Info*, CONGRESS DAILY, Feb. 9, 2007 (reporting that eBay believed the online auction reporting provision would impose extremely burdensome compliance costs).

36. *See* Dustin Stamper, *Simplification Trumps Bush Administration's Solutions at I.R.S. Tax Gap Forum*, TAX NOTES TODAY, Mar. 9, 2007, *available at* http://www.lexisnexis.com (search "2007 TNT 48-5") ("'Maybe we have gotten some of these [information reporting and related proposals] wrong' he said. 'Maybe we've misguided the impact of some of them.'") (quoting IRS Commissioner Mark Everson); Dustin Stamper, *Implementing Bush Budget Could Cost New I.R.S. $20 Billion Per Year by 2010, Says Everson*, TAX NOTES TODAY, Feb. 14, 2007, *available at* http://www.lexisnexis.com (search "2007 TNT 32-2") ("'Let's do [the measures proposed in the 2008 budget] and then see where our stomach is,' Everson said. 'Already we're into arguments where people are screaming about how much burden and how unfair some of these steps will be.'").

37. *See* GAO SOLE PROPRIETOR REPORT, *supra* note 4, at 7 ("To determine independent contractor status, payers are to use 20 common law rules."); Bankman, *supra* note 3, at 512–13 (discussing compliance burden for consumers if required to report payments to gardeners and other service providers and recommending a tax credit as partial reimbursement).

38. For example, expanding the merchant card reporting proposal to require banks and Paypal to report the payments they process, as the GAO has suggested, *see* GAO SOLE PROPRIETOR REPORT, *supra* note 4, at 50, presents a personal privacy concern, since individuals receive personal, nontaxable payments such as gifts and reimbursements for personal expenses, through their personal bank and Paypal accounts. *See* J.C. Santos, Analyzing the Treasury Proposal for Reporting by Merchant Banks 14 (Apr. 27, 2007) (unpublished manuscript, on file with author). A properly structured reporting system would reliably exclude such untaxable receipts, perhaps by requiring separate business and personal accounts and taxpayer identification numbers. *See* GAO SOLE PROPRIETOR REPORT, *supra* note 4, at 50 (noting that separate accounts and TINs would facilitate reporting by financial institutions).

percent on average of the $345 billion gross annual tax gap.[39] The low revenue estimates may result at least in part from taxpayers' existing tendency to report more visible income, including income that a large third party knows about.[40]

One expanded reporting proposal, the requirement to report securities basis, became law in October 2008 as part of the Emergency Economic Stabilization Act of 2008.[41] The Bush administration, apparently sensing a lack of political will to enact sweeping third-party reporting requirements, did not provide Congress a continued stream of new third-party reporting proposals. The set of reporting proposals in the Bush Administration's 2009 budget included fewer items than in 2008; it included the securities basis and merchant card proposals, for example, but not the expansion of broker reporting to online merchants.[42]

Finally, even if sweeping third-party reporting were implemented in the United States, there is even less political and popular appetite for provisions that would marginalize the use of cash. Despite the experience of some other governments,[43] measures such as limiting deductions for cash transactions, providing tax incentives for credit card

39. *See* Lori Montgomery, *Narrowing Tax Gap Called 'Unrealistic'*, WASH. POST, Apr. 19, 2007, at D3. The $30 billion figure included some measures relevant to small businesses, such as requiring credit card companies to report aggregate annual payments processed to merchants over $600 (scored at about $10.7 billion over ten years), requiring online brokers such as eBay to report transactions for customers where the total transactions exceed 100 and the total proceeds amount to at least $5000 (scored at about $2 billion over ten years), and requiring information reporting on payments to corporations, including S corporations (scored at about $7.7 billion over ten years). It also included some proposals not relevant to the problem of tax evasion by small business, such as the proposal to require basis reporting on security sales (scored at about $6.7 billion over ten years).

40. *See supra* note 5 (citing sources in support of the link between ease of detection and income reporting); Morse et al., *supra* note 13, at text accompanying notes 53–54 (reporting that interviewed cash business owners tended to report credit and debit card receipts but noting that the government might use credit card receipt information to target audits at taxpayers with lopsided ratios of reported credit card receipts to reported cash receipts).

41. Emergency Economic Stabilization Act of 2008, Pub. L. No. 110-343, 122 Stat. 3798 (codified at I.R.C. § 6045(g) (2008)).

42. *See* DEP'T OF THE TREASURY, GENERAL EXPLANATIONS OF THE ADMINISTRATION'S FISCAL YEAR 2009 REVENUE PROPOSALS 63–69 (2008) [hereinafter 2009 BLUEBOOK] (listing reporting proposals).

43. *See* Bankman, *supra* note 3, at 510 (noting that countries including South Korea, Argentina, Costa Rica, Columbia, Mexico, and Uruguay have subsidized merchant card use); Richard M. Bird & Eric M. Zolt, *Technology and Taxation in Developing Countries: From Hand to Mouse* 9 (July 4, 2008) (unpublished manuscript), *available at* http://ssrn.com/abstract=1086853 (reporting that in an attempt to reduce the use of untraceable cash, India allows a tax deduction of only eighty percent of most current cash expenses and that Korea encourages the use of credit cards by, for example, permitting a tax deduction equal to twenty percent of credit card expenses).

use, requiring non-cash electronic transactions or permitting close government monitoring of personal bank accounts would likely be inconsistent with popular sensibilities and perhaps would raise constitutional issues.[44] Although credit and debit card transactions are on the rise, cash still plays an important role in consumer commerce.[45] And if we are unwilling to give up untraceable cash transactions, many third-party reporting proposals present the problem that cash may be substituted and reporting requirements easily avoided.[46]

C. Audit

Other tax gap closing techniques seek to improve the audit and collections process. Using enforcement to improve taxpayer compliance is an important strategy.[47] It is particularly important for blatantly noncompliant taxpayers such as tax-evading cash businesses, as a strong noncompliance norm may require a particularly strong countering audit signal.[48] Even those who believe that both cooperation

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44. The First Amendment's right to free expression is one relevant constitutional protection. *See, e.g.*, *In re* Grand Jury Subpoena to Amazon.com Dated August 7, 2006, No. 07-GJ-04, 2007 U.S. Dist. LEXIS 86563 (W.D. Wis. June 26, 2007) (refusing to enforce government subpoena requesting Amazon.com to reveal the identities of 120 buyers who purchased books from an individual who allegedly evaded taxes on the proceeds of the sales, based on the First Amendment rights of the buyers and the possibility that subpoena enforcement would chill book-buying activity on the Internet).

45. Cash use in the U.S. is concentrated in retail sale transactions. Although credit and debit cards have eroded the use of cash, it remains an important form of payment. One study puts the use of cash in 2000 at twenty percent of consumer payments, down from thirty-one percent in 1974, and reports that the use of credit and debit cards rose from thirteen percent to twenty-seven percent over the same period, while check use fell from fifty-six percent to forty-six percent. *See* David B. Humphrey, *Replacement of Cash by Cards in U.S. Consumer Payments*, 56 J. ECON. & BUS. 211, 223 (2004) (reporting results).

46. Professor Leandra Lederman has developed a framework intended to guide the analysis of third-party reporting proposals. Her approach considers several factors, including whether the reporting party acts at arm's length, is centralized, and has a sufficient bookkeeping infrastructure; whether the government will have the information required for matching to tax returns; whether taxpayers can easily substitute another arrangement not subject to reporting; and whether the transaction targeted for reporting contributes significantly to the tax gap. *See* Leandra Lederman, Reducing Information Gaps to Reduce the Tax Gap: When Is Information Reporting Warranted 6–8 (Indiana Univ. Maurer Sch. of Law-Bloomington, Legal Stud. Res. Paper No. 126, 2009), *available at* http://ssrn.com/abstract=1347668. The framework might not support wholesale debit and credit card reporting due to the problem of cash substitution. *See id.* at 24–26.

47. *See, e.g.*, Leandra Lederman, *The Interplay Between Norms and Enforcement in Tax Compliance*, 64 OHIO ST. L.J. 1453, 1509–10 (2003) (noting that increased audits could prompt the development of an improved compliance norm).

48. *See id.*; *see, e.g.*, Edward McCaffery, *Cognitive Theory and Tax*, 41 UCLA L. REV. 1861, 1916 (1994) (noting that the ingrained use of individual tax shelters in the 1970s and 1980s may have required the overbroad hammer of the passive activity loss rules).

and punishment are important tools think that punishment is an appropriate response to habitual tax evaders.[49]

Several elements feed into improved audit processes, including electronic systems to improve document matching, cooperation with state authorities that may have relevant information from sales tax audits or other sources, better funding for audit and collections, and better audit selection based on expanded research. Improved technology and resource allocation might improve IRS collection productivity,[50] and figures indicate in any case that additional resources could produce some easy collections[51] and, through the "indirect audit effect," fuel a significant positive increase in voluntary compliance.[52]

Unfortunately, the necessary additional audit resources may not be available any time soon,[53] in part because of public and political discomfort with increased audit rates and in part because the IRS has begun, even while raising the audit rate, to shift some resources to computerized processing of tax data.[54] Moreover, despite serious recent efforts to increase the individual audit rate, it remains vanishingly small—1.03% for the fiscal year ending in September 2007, including

49. *See infra* note 91 and accompanying text (discussing limits of responsive or cooperative tax regulation).

50. *Cf.* William J. Hunter & Michael A. Nelson, *An I.R.S. Production Function*, 49 NAT'L TAX J. 105, 113–14 (1996) (concluding based on an econometric model and empirical data that technology investment and reassigning employees from the National Office to the field would improve IRS productivity); Dave Rifkin, *An Overview of the "Tax Gap,"* TAXES, Nov. 2008, at 27, 29–30 (explaining that the IRS mistakenly pursues high-dollar cases and lets small-dollar cases languish until so much interest has accrued that they are no longer easily collectible).

51. *See, e.g.*, David Cay Johnston, *I.R.S. Enlists Help in Collecting Delinquent Taxes Despite the Higher Costs*, N.Y. TIMES, Aug. 20, 2006, at 12 (citing Charles Rossotti's statement, confirmed by IRS personnel, that more than $9 billion could be collected at a cost of three cents on the dollar). This figure does not complete the cost-benefit analysis, as the payment of taxes to the government represents not an increase in economic activity, but rather a transfer that hopefully promotes a more efficient and equitable tax system. *See* JOEL SLEMROD & JON BAKIJA, TAXING OURSELVES: A CITIZEN'S GUIDE TO THE DEBATE OVER TAXES 183 (3d ed. 2004) (noting that increased tax revenue does not represent increased economic activity). However, three cents on the dollar is a good starting place.

52. Estimates of the indirect positive impact of audits on voluntary compliance include 11.6 times the amount of the actual audit adjustments, *see* ALAN H. PLUMLEY, I.R.S. PUBLICATION 1916: THE DETERMINANTS OF INDIVIDUAL INCOME TAX COMPLIANCE: ESTIMATING THE IMPACTS OF TAX POLICY, ENFORCEMENT, AND IRS RESPONSIVENESS 35 (1996), and 15 times that amount, *see* Jeffrey A. Dubin, *Criminal Investigation Enforcement Activities and Taxpayer Noncompliance*, 35 PUB. FIN. REV. 500, 521 (2007) (providing figures for simulation involving a hypothetical doubling of the audit rate).

53. *See* Johnston, *supra* note 51 (noting that Congressional reluctance to authorize additional IRS funding necessitated the hiring of private collection agencies).

54. *See* Bankman, *supra* note 3, at 514–15 (describing IRS resource shift and public opinion against audits).

correspondence and face-to-face audits.[55] Even a large budget increase and better audit selection would not raise the audit rate to a significant percentage.

D. Whistleblower and Qui Tam *Provisions*

As others have argued, the expansion of whistleblower and *qui tam* provisions has potential as a tool for building tax compliance norms.[56] Under the whistleblower statute, as amended in 2006, citizens who inform the government about tax violations can collect between fifteen and thirty percent of the resulting tax collections.[57] The whistleblower program has had some success[58] and attracted some publicity.[59] The salience and influence communication strategies outlined below could further expand public knowledge of the program. This would contribute to its success, which depends on the initiative of whistleblowers.

E. Gatekeeper Regulation

A large body of academic literature explores the concept of using gatekeepers such as lawyers, accountants, or tax preparers to regulate the conduct of their clients.[60] According to one survey, eighty-eight

55. *See* INTERNAL REVENUE SERV., FISCAL YEAR 2007 IRS ENFORCEMENT AND SERVICE STATISTICS 3 (2008) [hereinafter IRS, FISCAL YEAR 2007] *available at* http://www.irs.gov/pub/newsroom/irs _enforcement_and_service_tables_fy_2007.pdf. The 2007 coverage rate is 1.77% for individuals with income $100,000 and higher, 2.87% for individuals with income $200,000 and higher, and 9.25% for individuals with income $1 million and higher. *See id.* at 3–4.

56. *See* Joshua D. Rosenberg, *The Psychology of Taxes: Why They Drive Us Crazy and How We Can Make Them Sane*, 15 VA. TAX REV. 155, 204–18 (1996) (discussing solutions for increasing compliance and communication); *see also* Dennis J. Ventry Jr., *Whistleblowers and* Qui Tam *for Tax*, 61 TAX LAW. 357 (2008) (examining the IRS whistleblower program).

57. *See* I.R.C. § 7623(b)(1) (2006).

58. *See, e.g.*, Ventry, *supra* note 56, at 361–62 (reporting on the success of the 2006 whistleblower amendments).

59. *See, e.g.*, Press Release, IRS Oversight Board, IRS and Oversight Board Discuss Long-Term Measures and IRS Workforce Initiative at September Meeting (Sept. 16, 2008), *available at* http://www.treas.gov/irsob/press-posting_09162008.shtml (reporting that the 2006 statute has "yielded higher-dollar cases" including cases in the first eight months of 2008 from more than 800 whistleblowers who allege $2 million or more in unpaid taxes); Tom Herman, *Whistleblower Law Scores Early Success, Higher Rewards Attract Informants Submitting Tips*, WALL ST. J., May 16, 2007, at D3 (reporting that the IRS received important tips from informants hoping to cash in on the law offering sharply higher rewards in cases involving large amounts of tax cheating).

60. *See, e.g.*, John C. Coffee, Jr., *Gatekeeper Failure and Reform: The Challenge of Fashioning Relevant Reforms*, 84 B.U. L. REV. 301, 349–53 (2004) (proposing better alignment of gatekeeper and shareholder corporate governance incentives through regulatory strict liability); *see also* Reinier H. Kraakman, *Gatekeepers: The Anatomy of a Third-Party Enforcement Strategy*, 2 J. L. ECON. & ORG. 53 (1986) (introducing the gatekeeper regulation concept).

percent of small businesses use a paid tax preparer or accountant to prepare their federal income tax returns.[61] This large percentage might indicate that gatekeeper regulation could significantly improve this group's tax compliance. However, as discussed below, most gatekeeper provisions seem unlikely to have a significant impact on the problem of cash revenue-related tax evasion by self-employed and small business taxpayers.

Gatekeeper measures intended to improve deterrence of aggressive tax planning or outright tax cheating include raising return filing standards and disclosure requirements,[62] reducing privilege,[63]

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61. *See* NAT'L FED'N OF INDEP. BUS., NATIONAL SMALL BUSINESS POLL: COMPLEXITY AND THE I.R.S. 6 (2006) [hereinafter NFIB 2006 SURVEY] (reporting average results for firms with 1–250 employees).

62. *See, e.g.*, Linda M. Beale, *Tax Advice Before the Return: The Case for Raising Standards and Denying Evidentiary Privilege*, 25 VA. TAX REV. 583, 638 (2006) (summarizing a proposal to raise return filing standard to "more-likely-than-not"); Jay A. Soled, *Tax Shelter Malpractice Cases and Their Implications for Tax Compliance*, 58 AM. U. L. REV. 267, 301–03, 307 (2008) (arguing that successful tax shelter malpractice litigation illustrates the value of disclosure requirements and government access to taxpayer information). The Small Business and Work Opportunity Act of 2007 adopted an increased return filing standard for purposes of tax preparer penalties, *see* I.R.C. § 6694(a) (2006) (providing more-likely-than-not return preparer standard), although some criticize the new standard, *see, e.g.*, Jonathan S. Brenner, *New Standard for Tax Return Positions Is Inappropriate*, 116 TAX NOTES 559 (Aug. 13, 2007) (criticizing the amended Section 6694). Proposed regulations under Circular 230 would make the regulatory standard of practice the same as the statutory standard. *See* Regulations Governing Practice Before the Internal Revenue Service, 72 Fed. Reg. 54540 (proposed Sept. 24, 2007) (to be codified at 31 C.F.R. § 10.34(a), (e)) (requiring that return positions are supported either by a reasonable belief that the position is more likely than not to be sustained if challenged or by a reasonable basis disclosed to the IRS).

63. *See* Beale, *supra* note 62, at 638 (proposing to remove attorney-client privilege protection for pre-filing advice). Privilege in the tax context stems from the common law attorney-client privilege, *see* 3 JACK B. WEINSTEIN & MARGARET A. BERGER, WEINSTEIN'S FEDERAL EVIDENCE § 503.10 (Joseph M. McLaughlin, ed., 2d ed. 1997 & Supp. 2008), and from the statutory tax practitioner privilege, *see* I.R.C. § 7525 (2006). Recently courts have narrowed the scope of privilege, for example, holding that there is no privilege when the tax advisor prepares a tax return or when tax advice is offered as part of a marketing package. *See* United States v. Frederick, 182 F.3d 496, 502 (7th Cir. 1999) (Posner, C.J.) (stating that nothing in Section 7525 "suggests that these nonlawyer practitioners are entitled to privilege when they are doing other than lawyers' work"); Doe #1 v. Wachovia Corp., 268 F. Supp. 2d 627, 637 (W.D.N.C. 2003) (finding no privilege for Jenkens & Gilchrist or KPMG where advice was embedded in identical tax shelter packages *when they are doing other than lawyers' work*"). The availability of work product protection continues to depend on a more general balancing test that considers the strength of the claim that the material was developed in anticipation of litigation and the importance of the material to the requesting litigant's case. *See* BERNARD WOLFMAN ET AL., STANDARDS OF TAX PRACTICE § 306.4.4.2, at 304 (6th ed. 2004) (describing the balancing test). As privilege claims become less promising, practitioners may increasingly rely on work product. *See, e.g.*, United States v. Textron, Inc., 507 F. Supp. 2d 138, 153–55 (D.R.I. 2007), *aff'd in part, vacated in part*, No. 07-2631, 2009 WL 136752 (1st Cir. Jan. 21, 2009) (denying IRS petition to enforce summons for taxpayer workpapers based on work product doctrine). However, some argue that work product protection is inappropriate for documents such as workpapers prepared in

increasing penalties,[64] tightening ethical standards and disciplinary procedure,[65] imposing additional licensing requirements,[66] and

a tax regulatory context rather than in connection with a tax controversy. *See* Dennis J. Ventry Jr., *Protecting Abusive Tax Avoidance*, 120 TAX NOTES 857, 871–83 (Sept. 1, 2008).

64. *See, e.g.*, James S. Eustice, *Abusive Corporate Tax Shelters: Old 'Brine' in New Bottles*, 55 TAX L. REV. 135, 163 (2002) (recommending tougher Circular 230 sanctions). Recent statutory developments have, in fact, increased some penalties. For example, strict liability penalties for violation of the new Section 6694 "more-likely-than-not" standard are set at the greater of $5,000 or fifty percent of the tax preparer's compensation with respect to the return. I.R.C. § 6694(b)(1). Prior law set this "first-tier" penalty at $250. *See* JOINT COMM. ON TAXATION, TECHNICAL EXPLANATION OF THE "SMALL BUSINESS AND WORK OPPORTUNITY TAX ACT OF 2007" AND PENSION RELATED PROVISIONS CONTAINED IN H.R. 2206 (2007). A final Circular 230 provision also gives the IRS the authority, consistent with a statutory provision enacted in 2004, *see* American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 822(a), 118 Stat. 1418 (2004) § 822(a), to impose a monetary penalty up to the amount of gross income to be derived from the relevant conduct, *see* Circular 230, 31 C.F.R. § 10.50(c) (2008).

Other provisions enacted by the American Jobs Creation Act of 2004 target gatekeepers in an effort to combat tax shelters. *See, e.g.*, I.R.C. § 6111(b) (2000) (requiring "material advisors" to file statements describing "reportable transactions"); *id.* § 6112(a) (requiring such advisors to keep investor lists); *id.* § 6707(b)(1) (imposing penalties of $50,000 for failure to disclose reportable transactions and higher penalties for failure to disclose listed transactions); *id.* § 6708(a)(1) (imposing $10,000 per day penalty for failure to provide investor list on request). Finally, the Bush Administration's 2008 budget proposal included a provision that would increase the monetary penalty for failures such as failure to sign a return, failure to furnish a preparer TIN, failure to retain a copy of a return, or failure to file a correct information return. The existing penalty is $50 for a strict liability failure, $250 if the preparer knew or reasonably should have known of the failure, and $1000 if the failure is due to willful, reckless or intentional disregard of the rules. The proposal would increase the penalties from $50 to $150, from $250 to the greater of $1000 or fifty percent of the preparer's fee, and from $1000 to the greater of $5000 or fifty percent of the preparer's fee. *See* 2008 BLUEBOOK, *supra* note 28, at 80 (outlining existing law and proposal).

65. *See, e.g.*, Soled, *supra* note 62, at 290-96 (recommending stronger and better-enforced ethical standards). In 2003, the IRS created the Office of Professional Responsibility (OPR) as an expanded effort to oversee tax professionals. IRS News Release IR-2003-3 (Dec. 16, 2004), *available at* http://www.irs.gov/newsroom/article/0,,id=105533,00.html. The IRS has tried to strengthen the OPR. For example, it proposed opening Circular 230 disciplinary proceedings to the public. Regulations Governing Practice Before the Internal Revenue Service, 71 Fed. Reg. 6421 (proposed Feb. 8, 2006) (to be codified at 31 CFR § 10.72(d)). Final regulations, however, required only publication of final reports and decisions. *See* Circular 230, 31 C.F.R. § 10.72(d) (2008); *see also* T.D. 9359, 2007-45 C.B. 10 (2007) (explaining concern that practitioners' reputations would unfairly suffer from premature disclosure of hearings).

66. *See, e.g.*, S. 832, 109th Cong. § 4 (2005) (listing return preparer provision including an exam requirement and recertification of eligibility every three years); *see also* NAT'L TAXPAYER ADVOCATE, 2006 ANNUAL REPORT TO CONGRESS 197 (2007) (recommending certification program and explaining that "untrained and unscrupulous preparers present a serious problem"); U.S. GOV'T ACCOUNTABILITY OFFICE, TAX PREPARERS: OREGON'S REGULATORY REGIME MAY LEAD TO IMPROVED FEDERAL TAX RETURN ACCURACY AND PROVIDES A POSSIBLE MODEL FOR NATIONAL REGULATION 25 (2008) (suggesting that Oregon's regulation of tax preparers, including challenging examinations, might provide a national model). However, the government recently chose not to finalize a more limited provision targeted at unlicensed return preparers. *See* T.D. 9359, *supra* note 65 (explaining that proposed regulation that would have barred unenrolled preparers from representing clients before the IRS even in cases where they had

modifying tax preparers' investigation obligations.[67] Recent statutory amendments,[68] judicial developments,[69] and changes to Circular 230[70] implement some of these gatekeeper-targeted proposals. However, few such ideas have relevance for tax preparers assisting self-employed and small business taxpayers with significant cash revenue.

For example, provisions targeted at adjusting return filing standards and disclosure requirements have little relevance to the unambiguous problem of underreporting cash income. Likewise, reductions in attorney-client or work product privilege do not affect most self-employed and small business taxpayers. These doctrines have never protected the advice of most tax preparers who advise cash businesses because such preparers are generally not lawyers, and tax preparation does not constitute protected advice.[71]

Unlike filing standards and privilege, increased practitioner penalties and tougher disciplinary proceedings could be important tools for increasing compliance among self-employed and small business taxpayers. Thus, the increase in penalties under the 2007 amendments to section 6694[72] might well reduce tax preparers' willingness to cheat—except that they appear to be protected under current law if they can reasonably claim to be unaware of their clients' unreported income. If a tax preparer prepares a return for a cash business client that omits significant income, the tax preparer faces penalties only if the diligence rules attribute knowledge of that income to the preparer.

The 2006 amendments to section 6694 did not change the knowledge standard for purposes of the statutory return preparer penalty. The inquiry remains whether "the tax return preparer knew (or reasonably should have known) of the position,"[73] and the standard for avoiding penalties remains "reasonable cause for the understatement and [that the tax preparer] acted in good faith."[74] The analogous Circular 230

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prepared the contested tax return was not finalized).

67. *See* I.R.C. § 6694(a)(3) (2000) (providing that no tax preparer penalty is due if "there is reasonable cause for the understatement and [the preparer] acted in good faith"); Treas. Reg. § 1.6694-2(e)(4) (2008) (describing the "good faith" standard to include consideration of the actual knowledge of the preparer and whether the preparer's normal procedures promote accuracy and include "methods for obtaining necessary information from the taxpayer").

68. *See supra* notes 62 and 64 (describing statutory changes relating to return filing standards and increasing penalties).

69. *See supra* note 63 (describing judicial decisions restricting privilege).

70. *See supra* notes 62 and 64–65 (describing changes to Circular 230).

71. *See supra* note 63 (commenting on privilege law).

72. *See supra* note 64 (describing new penalties).

73. I.R.C. § 6694(a)(2) (2000).

74. *Id.*

provision, which states that a practitioner's responsibility to ensure that a client's return is accurate consists of using reasonable care in a due diligence process, also remains unchanged.[75] Existing guidance interpreting these provisions indicates that preparers may generally rely on taxpayer-provided information.[76]

The relevant guidance includes language that could be considered to require a tax preparer to ask questions about cash revenue in order to avoid penalties: "[T]he tax return preparer, however, may not ignore the implications of information furnished to the tax return preparer or actually known by the tax return preparer."[77] But the few examples do not portray a tax preparer who inquires about the big picture, for instance by asking how the client's business success, cash revenue experience, and lifestyle fit together. Instead, the examples present situations involving the question of whether the preparer had a specific reason to know about a particular income item.

The guidance permits a preparer to avoid violation by asking questions in a way that telegraphs that so long as she does not know about a taxpayer's other income, it will not be necessary to include it on the tax return she prepares. A preparer might ask, for example, "So I assume these records you've given me list all the revenue, right?" At least some research suggests that many preparers take the second "don't ask, don't tell" approach.[78]

Possible additional measures targeted at preparers and better-tailored to the problem that preparers now have the safe option of "indifference" to their clients' taste for tax evasion exist, as Professor Leslie Book pointed out in the 2008 Taxpayer Advocate report.[79] Such measures include more stringent and specific due diligence requirements[80] and improved data collection about preparers through such steps as uniform use of preparer identification numbers, bar coding of preparer returns and computer sifting of data to identify trends such as high refunds

75. *See* Circular 230, 31 C.F.R. § 10.22(a) (2008) (stating a due diligence requirement).

76. *See* Treas. Reg. § 1.6694-1(e)(1) (2008) (requiring reasonable inquiries if furnished information "appears to be incorrect or incomplete").

77. *Id.*

78. *See* Morse et al., *supra* note 13, at Part III.E.3 (reporting that according to series of information interviews, many practitioners appear to have a "don't ask, don't tell" norm that supports their clients' underreporting).

79. *See* Leslie Book, *The Need to Increase Preparer Responsibility, Visibility and Competence*, *in* 2 NAT'L TAXPAYER ADVOCATE, 2008 ANNUAL REPORT TO CONGRESS 74, 81 (2009) (describing types of tax preparers).

80. *See id.* at 86–88 (recommending changes to due diligence requirements).

traced to preparers.[81] These approaches would be most effective if accompanied by effective publicity.

II. SALIENCE AND INFLUENCE

Existing tax gap proposals, such as expanded third-party reporting, increased audit activity, and increased gatekeeper penalties and responsibilities make some sense, but as currently conceived they are incomplete. Salient and influential communication strategies can provide help. This Part describes what is meant by salience and influence in the context of promoting tax compliance.

The concepts of salience and influence as they relate to the formulation of tax and other public policies emerge from behavioral economics,[82] critical realism,[83] and behavioral public finance.[84] Salience here means relevance, prominence and accessibility. A salient communication grabs the attention of the audience. One way in which salience influences tax politics, for example, is that politicians may find that voters appreciate efforts to reduce prominent or salient taxes, like the individual income tax, more than hidden taxes like the corporate income tax.[85] Salience is also relevant to the relationship between the IRS and the taxpaying public because taxpayers give more attention and focus to more salient IRS communications.

Influence as used here means persuasion, typically through methods that do not rely on logic or argument. A communication may prompt a certain reaction because it activates a certain behavior pattern or heuristic.[86] But this does not necessarily make it influential as the term

81. *See id.* at 88–91 (describing measures to increase preparer visibility).

82. *See, e.g.*, Christine Jolls et al., *A Behavioral Approach to Law and Economics*, 50 STAN. L. REV. 1471, 1537 (1998) (recommending that prescriptive legal solutions "exploit salience").

83. *See, e.g.*, Jon Hanson & David Yosifon, *The Situational Character: A Critical Realist Perspective on the Human Animal*, 93 GEO. L. J. 1, 32–33, 43 (2004) (explaining that even though we often experience our interior cognitive processes as rational, "interior situation" and external manipulations can strongly influence that cognition). Hanson and Yosifon comment that due to the "interior fundamental attribution error," factors that we do *not* experience as salient can have significant influence; we are not aware, in many cases, what it is that drives us to a particular action. *Id.* at 31–32. I do not mean to challenge their observation about the importance of non-salient internal factors here, though I focus on external factors with salience and influence.

84. *See, e.g.*, Edward J. McCaffery & Joel Slemrod, *Toward an Agenda for Behavioral Public Finance*, *in* BEHAVIORAL PUBLIC FINANCE, *supra* note 10 (outlining the project of connecting analyses of individual "heuristics and biases" to "normative public finance" and noting that social norms and other factors outside the economic actor model contribute to tax compliance decisions).

85. *See* Edward J. McCaffery & Jonathan Baron, *Thinking About Tax*, 12 PSYCHOL., PUB. POL'Y & L. 106, 119–20 (2006) (noting taxpayer aversion to increases in the salient individual income tax).

86. *See* Ronald Chen & Jon Hanson, *Categorically Biased: The Influence of Knowledge*

is intended here. Influence implies intent. A person making an influential communication crafts it to take advantage of a particular behavior pattern or heuristic to produce a desired result.[87]

Other commentators have considered the use of tools of influence to improve tax compliance in various circumstances. Some recommend, for example, appeals to taxpayers' sense of morals or social obligation.[88] Others focus on the desirability of "responsive" or "cooperative" tax compliance efforts, in which the government and taxpayers establish a tit-for-tat partnership marked by the government's provision of useful and accessible services to the taxpayer and the taxpayer's honesty with the government.[89]

One challenge in the case of self-employed and small business taxpayers and the tax gap is that the audience includes many habitual evaders.[90] Even cooperation advocates agree that punishment remains an appropriate response to "dedicated cheaters,"[91] and thus a communication plan should direct a punishment message to this group. But other taxpayers may be willing to engage in a cooperative relationship with the government, and effective communication to this group should deliver a message that the government stands ready to

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Structures on Law and Legal Theory, 77 S. CAL. L. REV. 1106, 1179 (2004) ("[C]ues that are prominent or catch our attention are more likely to activate associated categories and schemas.").

87. *See* ROBERT B. CIALDINI, INFLUENCE: SCIENCE AND PRACTICE ix, 8–9 (4th ed. 2001) (noting the automatic reactions that advertisers and other "compliance professionals" can prompt).

88. *See, e.g.*, Eugene Bardach, *Moral Suasion and Taxpayer Compliance*, 11 L. & POL'Y 49, 49, 61 (1989) (listing several authors who recommend "'moral appeals,'" including fairness to one's fellow taxpayer and to improve tax compliance); Trivedi et al., *Impact of Personal and Situational Factors on Taxpayer Compliance: An Experimental Analysis*, 47 J. BUS. ETHICS 175, 179 (2003) (recommending that standard punishment-based enforcement be supplemented with information about other taxpayers' compliance, tax fairness, and appeals to taxpayers moral and social conscience).

89. *See, e.g.*, Leviner, *supra* note 25, at 11–15 (praising the Australian tax authorities' tit-for-tat responsive regulation strategy); Dennis J. Ventry, Jr., *Cooperative Tax Regulation*, 41 CONN. L. REV. 431, 436 (2009). Both Leviner and Ventry rely in part on the extensive work done in Australia on responsive tax regulation. *See, e.g.*, Valerie Braithwaite, *A New Approach to Tax Compliance*, *in* TAXING DEMOCRACY, UNDERSTANDING TAX AVOIDANCE AND EVASION 1–11 (2003); *see also* Dan M. Kahan, *The Logic of Reciprocity: Trust, Collective Action, and Law*, 102 MICH. L. REV. 71, 83–84 (2003) (suggesting that governments should encourage reciprocal compliance behavior by emphasizing other taxpayers' compliance rather than the possibility of audit).

90. The evasion of tax on cash income, as Professor Bankman has observed, "is not . . . subtle." Bankman, *supra* note 11, at 8.

91. Kahan, *supra* note 89, at 83–84; *see also* Leviner, *supra* note 25, at 15–16 (describing a tit-for-tat strategy); Ventry, *supra* note 89, at 446–47 ("[T]he feedback provided by a reciprocal approach can help tax authorities identify noncompliant taxpayers and respond with harsher penalties, aggressive enforcement, regular audits, and ongoing monitoring.").

reciprocate. For example, if, as Professor Alex Raskolnikov suggests, the government were to require taxpayers to choose between a "deterrence regime" targeted at gamers and a "compliance regime" targeted at good-faith taxpayers, salient and influential communications should not only inform taxpayers of the choice, but also build the credibility of the compliance option by persuading them of the government's ability and willingness to participate in a good-faith cooperative regulatory relationship.[92]

Professor Marjorie Kornhauser recognized the diversity among taxpayers' motivations and learning styles when she recommended incorporating behavioral compliance research into IRS policy in the 2007 Taxpayer Advocate report. She also acknowledged the difficulty of translating behavioral research into tax policy. Her proposal includes establishing a multidisciplinary behavioral science research division within the IRS, building a multifaceted understanding of tax morale that acknowledges the many differences among taxpayers, and launching diverse education and media campaigns aimed in part at improving tax morale.[93] Other work, including work by business professor Robert Cialdini and law professor Joshua Rosenberg, also presents a number of ideas to promote tax compliance that are grounded in behavioral insights.[94]

This Article has a more focused goal. It aims to provide a detailed and specific analysis of salient and influential tactics that might apply to the self-employed and small business taxpayer segment, and to consider

92. *See* Alex Raskolnikov, *Revealing Choices: Using Taxpayer Choice to Target Tax Enforcement*, 108 COLUM. L. REV. (forthcoming 2009) (manuscript at 15, 52, on file with author) (describing goal of targeting tax enforcement and role of accompanying educational campaign). Some existing pre- and post-filing issue resolution programs at the Large and Midsize Business (LMSB) division of the IRS, which invite taxpayers to disclose and agree with the IRS on issues in exchange for resolution of those issues, already invite taxpayers to elect a more cooperative regime. *See, e.g.*, CLIFF JERNIGAN, CORPORATE TAX AUDIT SURVIVAL 69–78 (2004) (describing initiatives including pre-filing agreements, industry issue resolution agreements, limited issue focused examinations, fast track appeals, and the compliance assurance process program). Participating in these initiatives in at least some cases builds on pre-existing relationships between taxpayers and IRS auditors or other personnel.

93. *See* Kornhauser, *supra* note 24, at 159–65 (detailing recommendations). *See also* Marjorie E. Kornhauser, *Tax Compliance and the Education of John (and Jane) Q. Taxpayer*, 121 TAX NOTES 737, 740–44 (Nov. 10, 2008) (outlining several education and media tactics).

94. *See* Robert B. Cialdini, *Social Motivations to Comply: Norms, Values and Principles*, *in* TAXPAYER COMPLIANCE: SOCIAL SCIENCE PERSPECTIVES 200 (Jeffrey A. Roth & John T. Scholz, eds., 1989) (recommending tax compliance tools under the six categories: social proof, commitment and consistency, reciprocation, liking, authority and scarcity); Rosenberg, *supra* note 29, at 530–31 (suggesting the use of media, schools and other access points to establish a positive models for taxpayers and to publicize tax compliance efforts such as whistleblower programs).

communication to both determined evaders and good-faith actors. Part III outlines how more salient and social proof-based communications about tax evasion could claim the attention of taxpayers and tax preparers and increase the perception that the government understands their game and can catch them at it. Part IV sets out several ideas based on the influence principles of reciprocity, commitment and consistency which could help initiate and sustain a cooperative taxpayer-agency relationship.

III. CASH, AUDITS, SHAMING, AND TAX PREPARER DILIGENCE: USE SOCIAL PROOF AND DON'T BURY THE LEAD

A. Cash

1. Existing guidance lacks salience

Tax evasion by self-employed and small business taxpayers who do not pay tax on all of their business income contributes half of the tax gap, and the failure to report cash income contributes significantly to the shortfall.[95] This group presents a big target audience for persuasive communications aimed at increasing voluntary compliance. However, the current communications aimed at them miss the mark.

For example, the first entry in the IRS tax gap fact sheet series, titled "Business Income and the Tax Gap," begins with six paragraphs of dense background information about the National Research Program and the measurement of the tax gap.[96] Not until the second paragraph of the second section is there this key piece of information: "Small business owners and self-employed taxpayers must report on their tax returns all income received from their businesses unless specifically excluded by law. In most cases, business income will be in the form of cash, checks and credit card charges." This text is not set off by emphasized text style, white space or otherwise. But after this important message, a bullet list does highlight other, less important news—that barter, cancellation of debt, damages, kickbacks, and other more unusual forms of income are also taxable. The fact sheet goes on to devote a significant portion of its two pages to the calculation of cost of goods sold and the calculation of income.[97]

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95. *See supra* Part I.A (outlining tax gap data).

96. *Cf.* Toder, *supra* note 1, at 4 (describing the National Research Program).

97. Internal Revenue Serv., Business Income and the Tax Gap, F.S. 2006-20 (June 2006), *available at* http://www.irs.gov/newsroom/article/0,,id=158618,00.html. An April 2008 Fact Sheet is similarly dense. *See* Internal Revenue Serv., Tax Challenges of Business Income, F.S. 2008-20 (Apr. 2008), *available at* http://www.irs.gov/newsroom/article/0,,id=182821,00 .html.

IRS products directed at the self-employed and small business community similarly focus on the details, offering helpful but dense information about choosing a tax preparer, social security benefits, choices among retirement plans, depreciation and so forth. The products tend to bury information about paying tax on cash income. Consider this information about the cash method of accounting from a free calendar the IRS makes available:

> Determining gross income with the cash method is merely a matter of adding up the cash, checks, and fair market value of property and services you receive during the year. Using this method, your income for the year includes all checks you receive. . . . You cannot avoid tax by not depositing checks or credit card charge slips.[98]

The text zeroes in on a secondary issue: whether you have income when you receive the check or when you cash it. Perhaps these materials avoid disagreeable information about paying tax on cash income because they aim to build a cooperative or responsive regulatory relationship; perhaps the materials telegraph that the IRS believes that the user of its free calendar is compliant until proven otherwise. Still, the materials fail to highlight the most important information; they bury the lead.

Much IRS guidance aimed at self-employed and small business taxpayers with significant cash revenue lacks salience. The stylistic approach of correcting taxpayer misunderstandings about the requirements of the law obscures the central point. The problem is not lack of understanding of a complicated legal provision.[99] The problem is a norm of not paying tax on cash income.

2. Influential content

A simpler message would have more salience, as would a message delivered by more easily accessible media, such as video instead of single-spaced text. Such a message could grab the taxpayer's attention and cue the decision process that relates to the taxpayer's tax evasion behavior. Influence principles can help the government determine the content of its message.[100]

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98. *See* Success by Design: 2007 IRS Tax Calendar for Small Businesses and Self-Employed (text accompanying the month of February) (on file with author).

99. In contrast, a text-based FAQ approach to disseminating information on complicated issues that come up in connection with home foreclosure and debt cancellation makes some sense. *See* IRS, *Home Foreclosure and Debt Cancellation*, Dec. 11, 2008, *available at* http://www.irs.gov.newsroom/article/0,,id=174034,00.html.

100. The IRS might also consider tapping resources such as the Advertising Council, which donates advertising talent to the cause of public service campaigns. *See* Seymour H. Fine, *A Generic Social Marketing Plan*, *in* SOCIAL MARKETING: PROMOTING THE CAUSES OF PUBLIC

In a 1989 paper, Professor Robert Cialdini used his lexicon of influence principles, including social proof, commitment and consistency, reciprocation, liking, authority and scarcity, as a basis for outlining a series of proposals to improve tax compliance. This Part III uses his principle of social proof to outline how the government could craft a simple and influential message about paying tax on cash income.

Social proof means that we "use the actions of others to decide on proper behavior for ourselves, especially when we view those others to be similar to ourselves."[101] As outlined in Part I, social science work has shown that social proof is important to tax compliance. Taxpayers' compliance behavior correlates with the perceived compliance behavior of peers with which taxpayers self-identify, and some work suggests that such perceived group norms have not only a correlative relationship, but also a causal effect.[102]

The scope of relevant norms, however, is uncertain. Studies agree that the compliance norm of a taxpayer's small circle is relevant, but they split on the question of whether the perceived compliance norms of the broader population are also important.[103] For example, in one real-life experiment, 20,000 taxpayers each received a letter from the Minnesota Department of Revenue explaining that nearly all taxpayers—ninety-three percent—were compliant. This experiment tested the impact of information about a general taxpaying public norm, rather than a small peer group norm. The researchers reported a small, positive impact on compliance and disagreed about whether the result had statistical significance.[104] In another experiment, UK taxpayers

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AND NONPROFIT AGENCIES 289, 298 (Seymour H. Fine ed., 1990) (describing the Ad Council).

101. CIALDINI, *supra* note 87, at 120.

102. *See supra* text accompanying notes 8–9 (discussing the relationship between social norms and noncompliance). It is possible that tax preparers' norms also have a causal effect on taxpayers' behavior, although research on this point is mixed. For example, one survey of Australian taxpayers suggests that taxpayers choose tax advisers whose views are consistent with the taxpayers' attitudes toward compliance. *See* Yuka Sakurai & Valerie Braithwaite, *Taxpayers' Perceptions of Practitioners: Finding One Who Is Effective and Does the Right Thing?*, 46 J. BUS. ETHICS 375, 385 (2003) (reporting results based on a survey of Australian taxpayers). Another study suggests that once taxpayers have chosen a tax preparer, they tend to follow the advice of that tax preparer. *See* Lin Mei Tan, *Taxpayers' Preference for Type of Advice from Tax Practitioner: A Preliminary Examination*, 20 J. ECON. PSYCHOL. 431, 445 (1999). This Article focuses on tactics intended to tap into taxpayer-to-taxpayer small group norms rather than interactions between tax preparers and taxpayers.

103. *See* Richardson & Sawyer, *supra* note 6, at 175–76 (describing literature showing that income source is an important tax compliance factor).

104. *See* Marsha Blumenthal et al., *Do Normative Appeals Affect Tax Compliance? Evidence from a Controlled Experiment in Minnesota*, 54 NAT'L TAX J. 125, 130–34 (2001) (reporting results of the experiment). *But see* Stephen Coleman, *The Minnesota Income Tax Compliance Experiment State Tax Results* 18 (1996), *available at* http://www.taxes.state.mn.us.legal_policy/

who received letters from Inland Revenue emphasizing the general link between taxpaying and citizenship reported statistically significant higher rates of compliance.[105]

One risk of publicizing the compliance behavior of a vast majority of the taxpaying public is that the audience may interpret the information to mean that "a clever minority cheats" rather than "virtually no one cheats." If the audience self-identifies with the clever minority, the social proof strategy backfires.[106] Social proof, then, would not necessarily endorse a slogan like "90% of Americans Pay Their Taxes. Put Yourself in the Majority." It prefers the slogan offered by Professor Rosenberg: "I pay my taxes. Pay yours,"[107] or perhaps the similar "Don't Cheat Me. Pay Your Taxes." Both of these slogans target the taxpayer-to-taxpayer norm central to individuals' compliance decisions.[108]

A slogan alone, however, does not offer a complete solution. The task remains of showing the target audience that *similar* taxpayers comply.[109] The surest way is to access and change small-group norms. Although much of the relevant group, by definition, cheats,[110] some

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research_reports/content/complnce.pdf (noting that although a variance analysis yielded no statistically significant effect, a different test indicated that the letter produced more variance than would have been expected from a control group; and also noting that the letter produced a greater uptick in tax compliance than a separate letter linking tax payments to public services and goods).

105. *See* John Hasseldine et al., *Persuasive Communications: Tax Compliance Enforcement Strategies for Sole Proprietors*, 24 CONTEMP. ACCT. RES. 171, 189 (2007) (reporting compliance increases for letters that emphasized taxpayer service, letters that emphasized citizenship, and letters that emphasized enforcement).

106. *See* Blumenthal et al., *supra* note 104, at 135 (stating that a statement of high but not one-hundred-percent compliance "may be interpreted to mean that the revenue department is unable to detect cheating"); Cialdini, *supra* note 94, at 214–15 (noting a similar possibility).

107. Rosenberg, *supra* note 29, at 530.

108. *See, e.g.*, Frey & Torgler, *supra* note 9, at 146, 152 (noting correlation and apparent causal link between taxpayers' perception of others' compliance and taxpayers' compliance decisions).

109. Rosenberg proposes a series of television commercials featuring "American hero[es] and heroine[s]" delivering a similar message. Rosenberg, *supra* note 29, at 530. Kornhauser considers a similar celebrity-endorsement proposal. *See* Kornhauser, *supra* note 24, at 743 (suggesting that actors might "sell" taxes and public goods as they sell other products). This approach falls under the "authority" category of influence techniques in Cialdini's lexicon. *See* CIALDINI, *supra* note 87, at 179–84 (considering advertising tactics including the celebrity print ad campaign developed by a milk industry group). Because the social science research indicates that taxpayers' close peer groups appear to have the most impact on tax compliance decisions, I choose here to emphasize the social proof influence tactic instead.

110. *See supra* Part I.A (presenting data on misreporting by small business and self-employed taxpayers). Some such taxpayers apparently cheat more than others. *See* GAO SOLE PROPRIETOR REPORT, *supra* note 4, at 3 (reporting that the upper ten percent of understatements were much larger on average than the lower half, and accounted for sixty-one percent of all sole proprietor understated taxes).

group members do not. One strategy would use an individual easily identifiable as a self-employed or small business taxpayer who explained why he or she paid taxes.[111] Consider the following script:

> I run my own construction business. Sure, I get cash income, but I pay every dime of my taxes. Why? Well, I think about those teachers at my kids' school. I know they depend on federal funding. I pay my taxes. Pay yours.

Scripts might also tap into different public goods in an effort to describe a commitment perhaps more likely to be shared by the target audience—although it is important to seriously consider whether the target audience does in fact value the highlighted public goods.[112] For example, a script might read, "Every year we pile in the car and go tenting at a national park" or "My mother couldn't make it without Social Security and Medicare." Others have generated similar ideas.[113] Alternatively, a communication campaign could call on broader personal integrity values with lines such as, "It's the honest thing to do," or "I pay my employees fairly and my suppliers fairly. I'm not going to cheat the government out of what I owe."[114] The goal is to emphasize positive points of similarity between the speaking taxpayer and the audience.

B. Publicity of Audit and Whistleblower Initiatives

Attention to salience and influence in communications might also improve audit publicity. The audit rate stands at about 1.03% on

111. Several public interest campaigns have begun to use peer-to-peer Internet strategies to build social norms. *See, e.g.*, RICHARD H. THALER & CASS R. SUNSTEIN, NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS 180–81 (2008) (describing the strategy of the Illinois First Person Consent registry designed to build organ donor lists); Donate Life Illinois Home Page, http://www.donatelifeillinois.org/ (last visited Jan. 25, 2009) (featuring photos and "stories" of Illinois citizens who have registered as donors).

112. *See* Kornhauser, *supra* note 24, at 164 (noting the "grave dangers in linking taxation to specific expenditures," including the possibility of fostering an exchange view of taxation that can prompt taxpayers to feel even more strongly that a tax is unfair or that the government wastes money).

113. *See id.* at 163–64 (noting the need for more education on the benefits of taxation); Rosenberg, *supra* note 29, at 530 ("[B]rief shots of hospitals, schools, roads, jetfighters, people eating wholesome food, taking safe drugs, etc. could make us understand some of the thousands of ways that our taxes contribute to our lives in ways we typically ignore.").

114. However, care should be taken when crafting appeals that rely on the fairness of the tax system. There is a positive correlation between tax compliance and the perceived fairness of the tax system, *see* TAXPAYER COMPLIANCE, *supra* note 5, at 127; *see also* Joel Slemrod, *Cheating Ourselves: The Economics of Tax Evasion*, 21 J. ECON. PERSP. 25, 39 (2007) (discussing what is currently known about tax evasion), but an ad strategy that relies on the perceived fairness of the tax system might backfire if the target audience does not share that perception.

average for individuals;[115] it is so low that even a significant increase of resources or improved audit selection strategies cannot make an audit truly likely for self-employed and small business taxpayers.[116] But if the government could publicize enforcement activities so that the *perceived* likelihood of audit increased for sole proprietor taxpayers, it could get more benefit out of an admittedly low audit rate.[117]

This is due to the well-established cognitive availability bias, which prompts us to estimate the "likelihood of an event on the basis of how quickly instances or associations come to mind."[118] Availability causes individuals to overestimate the likelihood of an event occurring to them if they have recently heard about it happening to someone else. Thus, it is linked to the indirect audit effect—audits have a positive impact on tax compliance, in addition to resulting in increased collections from the audited taxpayers.[119]

The IRS has made concerted efforts in recent years to improve the publicity of its enforcement activities. The criminal investigation division, for example, assigns a publicity point person in every field office, and the head of the criminal investigation division recently reported that the publicity rate on sentenced criminal cases had increased to 78.1% in 2007 from 54% in 2000.[120] In addition, the IRS website publicizes compliance and enforcement news, generally released in the form of text notices. However, the twenty-one items in the "Compliance and Enforcement News" section of the IRS small business and self-employed (SBSE) taxpayer web page as of March 2008 did not include any items referring to the successful audit of a small cash business.[121]

The Department of Justice does offer a significant number of tax-related press releases—more than fifty, for example, for the period May

115. *See* IRS, FISCAL YEAR 2007, *supra* note 55, at 3 (listing statistics for individual audit rates).

116. *See supra* Part I.C (discussing limitations of increased audit strategies).

117. *See, e.g.*, Andreoni et al., *supra* note 5, at 846 (summarizing numerous tax compliance studies that find that a high subjective probability of detection is associated with significantly more compliance behavior).

118. Hanson & Yosifon, *supra* note 83, at 40 (quoting SUSAN T. FISKE & SHELLEY E. TAYLOR, SOCIAL COGNITION 384 (2d ed. 1991)). *See also* Jolls et al., *supra* note 82, at 1537 (noting that salient advertising is persuasive in part because it plays into the availability heuristic).

119. *See* PLUMLEY, *supra* note 52, at 35 (citing estimates of indirect audit effect).

120. *See* Jeremiah Coder, *Conversations: Eileen Mayer*, 116 TAX NOTES 738, 740 (Aug. 27, 2007).

121. IRS Compliance and Enforcement News, http://www.irs.gov/newsroom/content/0,,id=137869,00.html (last visited Mar. 3, 2008).

through December 2007.[122] Perhaps officials refer to this press release coverage when they cite their criminal case "publicity rate." The list includes items featuring small business or self-employed taxpayers or their preparers, and could be used for a broader press campaign. One item, for example, reports that "Randy L. Bragg, the operator of employee leasing company Consolidated Human Resources Arizona," pled guilty to criminal charges of failing to pay federal employment taxes.[123] Another states that "[a] federal judge in Portland, Maine, has permanently barred Carol East Palesky of Topsham, Maine, from preparing federal tax returns for others" because she claimed inflated deductions and credits for customers.[124]

However, the Justice Department's press releases do not seem to yield much media coverage. In the Bragg and Palesky cases, for example, top results from Google searches for the defendant's name turned up few relevant news stories. The Bragg case prompted one entry on *topix.com/phoenix* reporting on his guilty plea. The *Portland Press Herald* picked up an Associated Press story in August 2007 about Palesky's criminal charges, and *webcpa.com* ran a similar story.

A comprehensive survey of media reporting of tax fraud and evasion is beyond the scope of this Article. But a brief survey of articles posted by *Reuters* and *U.S. News and World Report* over the 12-month period from May 2007–May 2008 reveals results for "tax fraud" or "tax evasion" that mainly feature famous people and/or egregious offenses.[125] There may be more reporting of typical tax-evading taxpayers in local media.[126] But overall, it appears the government has

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122. *See* U.S. Dep't of Justice, Tax Div., Tax Div. Press Releases 2007, http://www.usdoj.gov/tax/taxpress2007.htm (last visited Sept. 8, 2008) (listing 2007 press releases).

123. Press Release, U.S. Dep't of Justice, Tax Div., Phoenix Businessman Pleads Guilty to Charges of Failing to Pay Federal Employment Payroll Taxes (Nov. 6, 2007), *available at* http://www.usdoj.gov/tax/txdv07896.htm.

124. Press Release, U.S. Dep't of Justice, Tax Div., Federal Court Bars Maine Woman from Preparing Tax Returns for Others (Dec. 12, 2007), *available at* http://www.usdoj.gov/tax/txdv07990.htm.

125. *See, e.g.*, Barbara Liston, *Wesley Snipes Jailed for 3 Years in Tax Case*, REUTERS, Apr. 25, 2008, *available at* http://www.reuters.com/article/peopleNews/idUSN24190884200804 26?sp=true (reporting that actor had earned $38 million but failed to file tax returns from 1999–2001); Carey Gillam, *U.S. Sues Two for Making Millions "Disappear,"* REUTERS, Feb. 21, 2008, *available at* http://www.reuters.com/article/domesticNews/idUSN2150033920080221 (reporting allegations that a Kansas City lawyer and accountant had fabricated large deductions and set up sham companies to further tax fraud schemes for their wealthy clients).

126. *See, e.g.*, Robert E. Kessler, *Businessman Gets 6-Month Sentence in Tax Evasion*, NEWSDAY, Apr. 25, 2008, WL 2008 WLNR 7735090 (reporting that the owner of a Long Island construction business who employed undocumented carpenters and paid them off the books was sentenced to a $400,000 fine, three years supervised release, and six months residence in a

not chosen to push a social proof-based campaign featuring owners of local corner stores and similar local taxpayers.

The government has tried to focus attention on particularly egregious taxpayers in a categorical way, such as through the IRS "Dirty Dozen" list and the Department of Justice Tax Defier Initiative.[127] These lists paint a picture of tax evaders more willful than the average small business or self-employed taxpayer. For example, the IRS list warns of tax preparers who are "scam artists" and will "skim" taxpayers' returns.[128] The Department of Justice explains that "the tax defier is someone who rejects the legal foundation of the tax system, despite decades of legal precedent upholding the system's constitutional and statutory validity, and who takes specific and concrete action to violate the law."[129]

These approaches, and related tax protestor and other publicity, may effectively reduce the ranks of determined protestors or "scam artists." But they lack a social proof link to the experience of small business and self-employed taxpayers who may simply be in the habit of not recording how much cash they earned in a particular year and may not see themselves as tax evaders in the same way tax protestors defending their home against federal agents are tax evaders. A publicity campaign featuring more typical taxpayers would have more salience.

A more personal audit publicity campaign directed at less egregious tax cheating could have a crowding-out effect.[130] In other words, news of harsh IRS sanctions might jolt compliant taxpayers out of their

halfway house). Online comments to Kessler's article emphasized the immigration compliance angle of the story. Tax blogs sometimes pick up this news. *See, e.g.*, Taxable Talk, http://www.taxabletalk.com/tax_evasion/ (last visited Feb. 10, 2009) (blog of Russ Fox, an enrolled agent with Clayton Financial in Irvine, Cal., including posts of numerous tax-fraud tidbits).

127. *See* IRS News Release IR-2008-41 (Mar. 13, 2008) [hereinafter IR-2008-41], *available at* http://www.irs.gov/newsroom/article/0,,id=180075,00.html ("urging" taxpayers to avoid "schemes" including constitutionally-based tax protestor arguments, hiding income offshore, and "scam artist" fraudulent return preparers); Press Release, Nathan J. Hochman, Tax Division's Assistant Attorney General, Announces the Creation of the National Tax Defier Initiative (Apr. 8, 2008) [hereinafter TAXDEF Press Release], *available at* http://www.usdoj.gov/opa/pr/2008/April/08_tax_275.html. *See generally* Rifkin, *supra* note 50, at 32 (describing the tax defier initiative).

128. IR-2008-41, *supra* note 127.

129. TAXDEF Press Release, *supra* note 127.

130. *See, e.g.*, Kornhauser, *supra* note 24, at 151 ("The commoditization of a behavior crowds out positive normative influences on that behavior.") (citing Ernst Fehr & Armin Falk, *Psychological Foundations of Incentives*, 46 EUR. ECON. REV. 687 (2002)); Mark Lubell & John T. Scholz, *Cooperation, Reciprocity, and the Collective-Action Heuristic*, 45 AM. J. POL. SCI. 160, 173–74 (2001); Ann E. Tenbrunsel & David M. Messick, *Sanctioning Systems, Decision Frames, and Cooperation*, 44 ADMIN. SCI. Q. 684, 691–94 (1999).

reciprocal tit-for-tat game with the government, and prompt them to treat the IRS as an uncooperative party from which they should exact every advantage through economically rational aggressive tax return positions and audit lottery games. For example, relatively compliant taxpayers who fail to report some cash revenue might instead adopt more aggressive evasion strategies involving hiding assets in offshore accounts[131] or tax protestor arguments.

But it seems that the possibility of this shift would be minimized if taxpayers thought that the publicized sanctions were proportional to the crime. For example, the government might also counteract any possible movement of good-faith taxpayers to marginal tax evaders or marginal tax evaders to dedicated tax evaders by pursuing effective publicity about all groups' treatment by the government. The government might portray the good-faith taxpayers as recipients of exceptional service and respectful treatment.[132] The marginal tax evaders might suffer bad consequences: monetary civil penalties whose size varies with the amount and nature of the tax evasion. The dedicated tax evaders should suffer worse consequences: perhaps even criminal conviction.

A related constraint of an audit publicity campaign is that if the IRS is perceived by the public to overreach its authority or act in bad faith, it faces the possibility of public and congressional backlash.[133] This happened, for example, in 1998, when public perception of an overzealous IRS contributed to the passage of a law curtailing the agency's power.[134] This concern also supports the approach of publicizing penalties that correspond to the severity of the offense.

A taxpayer testimonial approach might also minimize the chance of backlash against the IRS by presenting the regrets of audited taxpayers, rather than the vindicated authority of the government. They might tell their story for the record as part of a settlement offer.[135] The taxpayer

131. The practice of placing individuals' assets in offshore bank accounts for the purpose of hiding the existence of the principal and/or income plainly constitutes tax evasion, and the aggressive use of offshore trusts where individuals retain control of the corpus may as well. *See, e.g.*, IR-2008-41, *supra* note 127 (naming "hiding income offshore" as one of the top twelve tax scams). The consideration of offshore planning techniques used by corporations falls outside the scope of this article.

132. *See* Kornhauser, *supra* note 24, at 152 (noting the "crowding-in" effect that procedural fairness and good examples can produce).

133. *Cf.* Leviner, *supra* note 25, at 364 ("[R]are and extreme punishments can provoke community outrage.").

134. *See* Bryan T. Camp, *Tax Administration as Inquisitorial Process and the Partial Paradigm Shift in the IRS Restructuring and Reform Act of 1998*, 56 FLA. L. REV. 1, 79 (2004) (noting debate over "pendulum" swings between service and enforcement at the IRS in the wake of the 1998 Act).

135. The IRS has occasionally made publicity permission part of a taxpayer settlement. *See,*

might explain, "I thought I was doing my family a favor, paid for a trip to Hawaii by not turning over income taxes to the feds. Now I'm in debt for five times the cost of the trip."

Some other possible tax gap closing strategies rely, like audit, on the concept of identifying and disciplining evading taxpayers, without undermining the compliance behavior of good-faith taxpayers. Proposals for expanded whistleblower and *qui tam* provisions[136] present influence challenges similar to those presented by audit publicity. The goal is to persuade target audience taxpayers that they are really vulnerable to whistleblower disclosure—without giving the impression that the IRS is inappropriately mean.

Such publicity campaigns deserve respect as challenging and subtle exercises. A successful campaign would realistically portray audited taxpayers sufficiently similar to the targeted group in order to affect the small-circle social norm that is most closely related to such targeted taxpayers' compliance behavior. It would publicize sanctions proportional to the offense to avoid prompting a congressional restriction of IRS powers or crowding out compliant taxpayers who might defect from their pattern of reciprocity with the IRS if they thought the government acted unfairly. Moreover, such a campaign must comply with taxpayer confidentiality limitations and budgetary constraints. Nevertheless, it is likely a worthwhile exercise. The indirect deferral benefits of an audit can yield many times the tax revenue resulting from the audit itself[137]—but only if people know about it.

C. Shaming

Another social proof strategy would aim to communicate society's disapproval of tax cheating, and raise public awareness of the government's successful efforts to find noncompliant taxpayers, by publishing the names of delinquent taxpayers or using other shaming techniques.[138] Many states publish such lists, and the U.S. government has used the technique in certain narrow circumstances.[139] Reputational

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e.g., IRS News Release IR-2004-151 (Dec. 16, 2004), *available at* http://www.irs.gov/newsroom/article/0,,id=132350,00.html ("Hercules [taxpayer] has further agreed to a limited waiver of the taxpayer privacy and anti-disclosure rules in connection with this press release.").

136. *See supra* Part I.D (outlining whistleblower and *qui tam* recommendations).

137. *See* PLUMLEY, *supra* note 52 (describing quantifications of indirect compliance benefits).

138. *See, e.g.*, Jay A. Soled & Dennis J. Ventry, Jr., *A Little Shame Might Just Deter Tax Cheaters*, USA TODAY, Apr. 10, 2008, at A11 (discussing the benefits of tax shaming strategies).

139. *See* Michael S. Kirsch, *Alternative Sanctions and the Federal Tax Law: Symbols,*

sanctions (or the perceived threat thereof) might serve as a powerful deterrent to cheating for taxpayers or tax preparers,[140] although shaming may most effectively deter those already inclined to comply.[141] Put differently, shaming might facilitate changes in the norm of tax compliance by encouraging citizens who are susceptible to social influence to gather around an expressed collective norm.[142]

Salient and influential communication could improve a shaming strategy's effectiveness. For example, a shaming strategy might have greater social proof influence if it featured certain individuals and included photos or links to business websites, so long as this approach were consistent with confidentiality requirements and Constitutional limitations.[143] The idea of featuring individuals has elements in common with the audit publicity proposals discussed above.[144]

However, shaming strategies raise separate concerns unrelated to the salience and influence of the particular shaming tactic employed. First, because the government cannot actually identify many underreporting self-employed and small business taxpayers, any delinquent taxpayer list would necessarily be incomplete. This could produce a concern about presenting caught tax cheats as the unfortunate minority and the vast majority of uncaught tax cheats as free, clear and richer. The government might hedge against this concern by presenting the list as a partial list of the tax delinquents it knows about.

In addition, if a shaming strategy produces a public perception that the government is being mean, it could have an adverse effect on the overall public perception of the approachability of the IRS, and it could therefore undermine tit-for-tat strategies directed at good-faith taxpayers.[145] This concern is related to Professor Dan Kahan's

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Shaming, and Social Norm Management as a Substitute for Effective Tax Policy, 89 IOWA L. REV. 863, 913–21 (2004) (noting the federal publication of lists of expatriating individuals and corporations); Rifkin, *supra* note 50, at 35 (noting a rule requiring government contractors to report outstanding tax debt in excess of $3000).

140. *See* Soled, *supra* note 62, at 288–90; (noting the potential of shaming techniques for tax practitioners) (citing Toni M. Massaro, *Shame, Culture, and American Criminal Law*, 89 MICH. L. REV. 1880 (1991)).

141. *See* Massaro, *supra* note 140, at 1916–17 (noting that psychological studies demonstrate that shaming most affects strongly socialized non-offenders).

142. *See* Kirsch, *supra* note 139, at 913–21 (considering the expressive function of shaming on tax compliance norms) (citing Richard H. McAdams, *The Origin, Development, and Regulation of Norms*, 96 MICH. L. REV. 338 (1997) and Cass R. Sunstein, *On the Expressive Function of Law*, 144 U. PA. L. REV. 2021 (1996)).

143. For example, the government should carefully avoid any appearance of intent to discriminate. *See infra* Part V.C (discussing possible equal protection concerns).

144. *See supra* Part III.B (discussing audit publicity).

145. *See supra* text accompanying 130 (discussing possible adverse reactions to

argument that shaming strategies lack expressive ambiguity, since they so plainly and strongly communicate strong public disapproval of the individual shamed. The unambiguous nature of shaming makes it difficult for individuals with different world views to develop a consensus that shaming is an appropriate sanction. A "hierarchist," for example, may approve of shaming but an "egalitarian" may not.[146]

If individuals with delinquent tax payments are shamed, and some good-faith taxpayers, perhaps because of their world views, consider the shaming sanction mean-spirited, the good-faith taxpayers may move away from a cooperative relationship with the IRS. At the same time, at least for individuals who are strongly socialized, shaming may constitute an effective sanction.[147] The government could mitigate the crowding-out risk by shaming determined tax cheats only. One might, for example, post only the names of taxpayers who owed a significant amount, such as $25,000,[148] and had refused to respond to repeated government inquiries. Still, it is a delicate balance and the crowding-out concern may even exist for shaming techniques that focus on egregious stories; more limited tactics would still "degrad[e] and moraliz[e]."[149] Perhaps the best course is to research the impact of shaming sanctions on taxpayer morale—as well as tax revenue—in those states that have such sanctions before proceeding with a federal program.

D. Tax Preparer Due Diligence

Salience and influence tactics could also inform the delivery of guidance about tax preparers' due diligence requirement. As discussed above, it is currently unclear whether a cash business preparer is required to inquire extensively about a client's cash income.[150] Perhaps there is concern that a strengthened diligence requirement could cause taxpayers to switch to more aggressive preparers, or crowd tax preparers

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disproportionately harsh sanctions in the context of audit publicity).

146. *See* Dan M. Kahan, *What's Really Wrong with Shaming Sanctions*, 84 TEX. L. REV. 2075, 2090 (2006) (contrasting hierarchists' and communitarians' approval of shaming sanctions with egalitarians' and individualists' disapproval of them).

147. *See* Massaro, *supra* note 140, at 1900–04 (describing the "gravity" and "isolation" of shame for a person to whom group or community membership is important).

148. Some state websites post taxpayers who owe smaller amounts. Wisconsin, for example, has a $5000 cutoff. *See* Wisconsin Department of Revenue, Wisconsin Delinquent Taxpayers, http://www.revenue.wi.gov/html/delqlist.html (last visited Aug. 29, 2008).

149. Kahan, *supra* note 146, at 2090.

150. *See supra* text accompanying notes 75–77 (discussing existing guidance regarding tax preparer diligence).

out of the "don't ask, don't tell" category[151] and into a situation where they actively aided and abetted their clients' efforts to evade tax on cash income.[152]

This possibility of taxpayers' or tax preparers' migration between categories suggests that any attempt to address the problem of "don't ask, don't tell" preparers should be accompanied by publicity about the worst adverse consequences that active aiders and abettors can, and do, suffer. A parallel publicity campaign could emphasize that an active aider and abettor would face far worse penalties (perhaps criminal charges) than a don't ask, don't tell preparer who violated the diligence requirement, while still conveying the information that a don't ask, don't tell preparer would also suffer painful consequences (perhaps significant monetary penalties and a loss or suspension of license).

If the IRS decided to clarify and strengthen the diligence requirement, it faces a communication problem analogous to the challenge of effectively communicating the simple message that cash is taxable. Here, the message would be, "Ask about the cash." To maximize salience and influence, consistent with the social proof principle, the content of the guidance ought to closely reflect tax preparers' experience. For example, the IRS might create a video that shows an interaction between a small business owner and his tax preparer. It might show a "wrong way" scenario subject to penalties and license suspension: "So, Joe, I have all the credit card receipts from your restaurant here. Let me just run through the program [clickety clickety clack], looks like this is the number." Then it could demonstrate a "right way" scenario: "So, Joe, I have all the credit card receipts from your restaurant here. How about your cash take? What's the ratio like on most nights?"

E. Content Distribution

There remains the question of how to distribute the content in taxpayer testimonials or video guidance, whether it relates to cash revenue, audits, tax preparer diligence or other items. The IRS has invested heavily in its relationships with industry tax preparer groups, and those relationships, together with meetings offered by the government to tax preparers, offer one communication avenue. But the

151. *See supra* text accompanying note 78 (describing "don't ask, don't tell" tax preparer behavior).

152. *See generally* Morse et al., *supra* note 13, at text accompanying n.67 (suggesting that the immorality and social disutility of involved preparers is clearer than that of "don't ask, don't tell" preparers).

IRS still needs ways to reach individual taxpayers and unaffiliated tax preparers. Accordingly, mass market distribution may be necessary.

With respect to mass-market distribution, conventional television, radio, and print advertising can be expensive.[153] Research has used letters from government tax authorities; that is one relatively low-cost option. But if demographic research confirmed that the target taxpayers were regular internet users, the cheapest way to distribute content might be to simply post it on the IRS SBSE page[154] and seek some parallel media coverage. If the content is effective, it will likely get follow-on media stories and independent distribution, such as through You Tube, which the IRS has already used as a video guidance outlet.[155]

IV. TIT FOR TAT, RECIPROCITY, AND COMMITMENT AND CONSISTENCY

A. Why Tit for Tat Needs Help

Advocates of cooperative and responsive regulation envision a tax system where taxpayers respond with honesty and compliance to a "fair and respectful" tax administration.[156] It is a tit for tat concept grounded in game theory—taxpayers and tax administrators exchange positive

153. Media outlets such as television stations need not comply with any requirement to donate time to public service advertisements, but many do so anyway. *See* THE HENRY J. KAISER FOUNDATION, SHOUTING TO BE HEARD: PUBLIC SERVICE ADVERTISING IN A CHANGING TELEVISION WORLD 2 (2008) (explaining that donating time may help non-cable television stations meet their obligation to act in the "public interest"). Data from 2005 indicate that broadcast and cable television stations donated an average of seventeen seconds an hour to public service advertisements. *See id.* at 5 (citing study results). Some public service campaigns are fully or partly paid. *See id.* at 3 (citing federal Office of National Drug Control Policy campaign as a partly paid program).

154. Internal Revenue Serv., Small Business and Self-Employed Tax Center, http://www.irs.gov/businesses/small/index.html (last visited June 25, 2007).

155. In 2008 the IRS posted three thirty-second spots on YouTube explaining how taxpayers could get their economic stimulus tax rebates and avoid phishing scams in 2007. *See* Internal Revenue Service, Get Your Tax Rebate: General Taxpayers, http://www.youtube.com/watch?v=_LBfEKCKkSk&NR=1 (last visited Feb. 7, 2009); Internal Revenue Service, Get Your Tax Rebate: Beware of Rebate Scams, http://www.youtube.com/watch?v=TUYxAbd7NVo&feature=PlayList&p=0D12A5B897B0BDC0&index=1 (last visited Feb. 7, 2009); Internal Revenue Service, Get Your Tax Rebate: Taxpayers Who Normally Don't File, http://www.youtube.com/watch?v=lRSPwX2kNic&feature=PlayList&p=0D12A5B897B0B DC0&index=0 (last visited Feb. 7, 2009). Comptroller of Maryland Peter Franchot also used YouTube to post an engaging clip intended to encourage e-filing in January 2009. Maryland Comptroller, Maryland Comptroller—Taxpayers of Genius, http://www.youtube.com/watch?v=HvbRj-XdhRc (last visited Feb. 18, 2009).

156. *See, e.g.*, Braithwaite, *supra* note 89, at 1–11 (describing Australian responsive regulation model); Leviner, *supra* note 25, at 371 (describing tit-for-tat strategy); Ventry, *supra* note 89, at 445–47 (describing cooperative regulation concept).

information and reinforce each others' good behavior.[157] Under this model, the government needs opening lines—overtures that communicate to taxpayers that it is interested in starting cooperative relationships.

Professor Dennis Ventry, for example, offers several possible government overtures, including rewarding taxpayer compliance, offering participation in rulemaking, and giving taxpayers better access to government information.[158] This Part builds on the idea that the government should make its willingness to cooperate known using salient and influential reciprocity tools. Then it considers ways in which the government could encourage taxpayers to affirm and strengthen their commitment to tax compliance.

B. Reciprocity

As Professor Cialdini explains, the reciprocity influence principle describes our compulsion to repay favors and gifts.[159] Reciprocity often triggers unequal exchanges, so that "[a] small initial favor can produce a sense of obligation to agree to a substantially larger return favor."[160] Cialdini provides a vivid example of the reciprocity principle when he describes the behavior of a traveler who is unable to turn away or resist making a donation when presented with a flower by a Hare Krishna member at an airport.[161]

The IRS already gives taxpayers things for free, such as its numerous service and outreach products.[162] For example, it has produced a narrated PowerPoint workshop for small business owners[163] and a "Small Business Resource Guide,"[164] each available as a DVD (or CD) or online, in addition to a wall calendar with important tax dates.[165] It

157. *See* Leviner, *supra* note 25, at 374 (linking tit-for-tat strategy to game theory).

158. *See* Ventry, *supra* note 89, at 445 (suggesting rewards for filing correct and timely returns and open communication as an initial strategy); *id.* at 448 (exploring taxpayer input for rulemaking).

159. CIALDINI, *supra* note 87, at 20.

160. *Id.* at 33.

161. *Id.* at 23 (describing airport incident).

162. Cialdini's reciprocity recommendations focused on possible service and outreach offerings. *See* Cialdini, *supra* note 94, at 212–13 (recommending emphasis of the value of such services, such as by noting their market price).

163. *See* Internal Revenue Service, Small Business Products Online Ordering, http://www.irs.gov/businesses/small/article/0,,id=101169,00.html (last visited June 25, 2007) (listing Publication 1066C, A Virtual Small Business Tax Workshop (DVD)).

164. *See id.* (listing Publication 3207, Small Business Resource Guide (CD)).

165. *See id.* (listing Publication 1518, Tax Calendar for Small Businesses and Self-Employed).

also offers a number of hotlines,[166] and annual tax forums at reasonable prices for tax professionals.[167] This kind of information offering, in which the IRS has already invested considerable time and energy, may already trigger a reciprocal reaction that encourages the target audience to increase their compliance.

Some items, such as the calendar,[168] move away from the straightforward delivery of information and into the category of classic reciprocity influence gifts. But these gifts are more complex than the typical stress ball. Despite efforts to avoid legalese and offer genuinely helpful information using plain language, the style of the content is typically dense and complex.[169] Moreover, the IRS delivers bad news: you have to pay taxes and there are a lot of forms to fill out.[170] The government could attempt to increase the salience of its offerings by making their message simpler. For example, it could put a web address[171] and a tagline, perhaps a variation of "I pay my taxes. Pay yours," on some swag.

But there is a problem with swag such as branded stress balls or magnets, at least based on the anecdotal collection of reactions to these proposals. The problem is that taxpayers may experience these "gifts"

166. *See* Internal Revenue Service, IRS Hotlines and Toll-Free Numbers, http://www.irs.gov/businesses/small/article/0,,id=161104,00.html (last visited June 25, 2007).

167. *See* Internal Revenue Service, IRS Nationwide Tax Forum 2007, http://www.taxforuminfo.com/index.php?module=content&section_id=13 (last visited June 25, 2007).

168. Even the calendar, however, retains the bland and out-of-touch patina of conventional public service advertising. Its cover features the only illustration, a drawing of a six-employee team meticulously coloring in the word "SUCCESS" on a backdrop of rolling golden hills and blue skies. This likely does not resemble the day-to-day struggle experienced by many small businesses. Contrast the post office's postcard advertising campaign featuring the hapless cartoon characters Cathy and Dilbert and the post office's solutions to their shipping woes. Press Release, United States Postal Service, "Dilbert," "Cathy" Help Postal Service Talk with Customers, (Feb. 27, 2006), *available at* http://www.usps.com/communications/news/press/2006/pr06_014.pdf.

169. *See supra* text accompanying note 98 (describing IRS calendar content).

170. An entry entitled "Filing Requirements for the Self-Employed" states, dauntingly, "As a self-employed individual, you may be responsible for completing multiple tax forms, depending on your type of business." *See* Internal Revenue Service, Publications and Forms for the Self-Employed, http://www.irs.gov/businesses/small/article/0,,id=115044,00.html (last visited Jan. 22, 2009) (listing nine publications and seven forms that self-employed individuals may have to use).

171. Ideally, the IRS could clean up its web links to the relevant small business page. It has established the "Small Business and Self-Employed Tax Center" as an index of information, and this link is featured as a result of a keyword search for "small business," "smallbiz" and "self employed" (but not "small biz" or "sbse") on www.irs.gov. However, the address for the one-stop resource itself is hardly catchy: http://www.irs.gov/businesses/small/index.html. Internal Revenue Service, Small Business and Self-Employed Tax Center, http://www.irs.gov/businesses/small/index.html (last visited Jan. 22, 2009). How about www.irs.gov/smallbusiness, or www.irs.gov/smallbiz, or www.irs.gov/sbse?

as unneeded stuff that the IRS forces them to purchase with their own tax dollars. Even though private sector firms may pass on the cost of reciprocity gifts to consumers in the form of higher prices, the coercive element in taxpayers' obligation to fund the IRS seems to cause adverse reactions to apparently frivolous increases in the agency's cost base.

Another reciprocity idea follows from others' proposals to offer rewards or discounts for timely and correct tax filing.[172] The IRS could offer a coupon, such as ten dollars off your taxes, expiring on the day your taxes are due. If delivered via a click-through on the IRS website or offered after the completion of a survey, the strategy would bring in the commitment and consistency principle as well, because it asks a taxpayer to affirmatively choose to associate with the IRS.[173]

However, an economic incentive may raise a crowding-out problem in that it may "commoditiz[e]" the taxpayer relationship and decrease the positive compliance effect of values like good citizenship.[174] In addition, the coupon concept at least appears expensive. Even if limited to Schedule C filers,[175] a ten dollar coupon applied to every Schedule C return would appear to cost $215 million.[176] A lottery, say for forgiveness of a year's tax liability, might provide another, cheaper possibility of delivering money to taxpayers,[177] but this idea, like the stress balls, could open the IRS to accusations of spending taxpayer time and money on frivolous ideas.

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172. *See* Ventry, *supra* note 89, at 445–46 (recommending discounted rates of tax for taxpayers who pay taxes accurately and on time). *See also* Rosenberg, *supra* note 29, at 527–28 (recommending rewards for taxpayers who sign up for automatic reporting).

173. *See infra* Part IV.C (discussing commitment and consistency).

174. *See* Kornhauser, *supra* note 24, at 170 (noting commoditization risk).

175. Such a limitation would presumably pass the applicable constitutional rational basis test. *See, e.g.*, Romer v. Evans, 517 U.S. 620, 632 (1996) ("In the ordinary case, a law will be sustained if it can be said to advance a legitimate government interest, even if the law seems unwise or works to the disadvantage of a particular group, or if the rationale for it seems tenuous."). If viewed as a reduction in otherwise applicable late-filing and other penalties, which the IRS has the discretion to adjust, *see* I.R.C. § 6652(e) (2008) (imposing a penalty unless "reasonable cause" can be shown), it would likely not present a tension with statutory rate schedules, *see, e.g.*, I.R.C. § 1 (2008) (listing the tax rates for individuals), and Congressional action would not be required. *See* I.R.C. § 6652(e) (2008) (allowing the IRS to waive late-filing penalties for "reasonable cause").

176. *See* JEFF CURRY & JUSTIN BRYAN, SOLE PROPRIETORSHIP RETURNS, 2005, SOI BULLETIN, Summer 2007, at 6, 6, *available at* http://www.irs.gov/pub/irs-soi/05solep.pdf (reporting that sole proprietors filed about 21.5 million Schedule C tax returns in 2005). Of course, the reciprocity idea is that the Schedule C filers who used the coupon would end up paying more to the government even taking the coupon into account, just as the reciprocity principle prompts a coupon-using shopper to spend more at the store with the coupon than without.

177. Like a coupon, the lottery idea could include a commitment and consistency component if participation in the lottery were linked to a survey on the IRS website.

If taxpayers perceive traditional swag as wasteful of taxpayer money and economic incentives as (perhaps) undermining their citizenship values, how can the IRS use the reciprocity principle to help foster cooperative relationships with taxpayers without worrying about backlash? The safe approach is to stick to the project of trying to make taxpayers' lives easier through service and guidance, and approach the project with greater sensitivity to the influence principle of reciprocity. Perhaps more compliant taxpayers could receive better service, for example.[178] More broadly, the IRS should continue its efforts to make guidance simple, accessible, and timely.[179]

C. Commitment and Consistency

1. How the IRS Already Uses Commitment and Consistency

Under Professor Cialdini's definition, commitment and consistency refers to "our desire to be (and to appear) consistent with what we have already done."[180] This desire ties to our evolved understanding that life goes better if we honor the commitments we have made to other people, and it is stronger if our indications of agreement are public.[181] Small initial gestures can spark a much more substantial involvement later.[182] The most important difference between a commitment and consistency strategy and a social proof or reciprocity strategy is that a commitment and consistency strategy involves the taxpayer's confirming action, while a social proof or reciprocity strategy can be executed through a unilateral government communication or gift.

The government already uses tools that invite taxpayers and tax preparers to confirm their commitment to a tax compliance norm. For example, taxpayer service programs may succeed in motivating taxpayers to commit to tax compliance through the semipublic act of reaching out to the government for help. Two other specific tactics are requiring signed statements on tax returns, and surveying taxpayers about their tax compliance beliefs. The government could build on each of these existing activities in a way that specifically targeted the known issue of tax evasion by self-employed and small business taxpayers. It

178. *See* Kornhauser, *supra* note 24, at 170 (suggesting rewards like "special phone lines that have a shorter wait").

179. *See, e.g.*, *supra* note 155 (noting 2008 video guidance in relation to economic stimulus tax rebates).

180. CIALDINI, *supra* note 87, at 53.

181. *See id.* at 72–74 (noting the importance of public commitments).

182. *See, e.g.*, *id.* at 65–66 (noting the substantially increased inclination of individuals who sign Sierra Club petitions to give money or participate in demonstrations).

could also attempt to encourage taxpayers' commitment to other public goods, and then draw the connection between such public goods and the value of tax compliance.[183]

2. Tax Return Statements

First, consider statements on tax returns.[184] Currently, an individual taxpayer must sign his or her income tax return, swearing "under penalties of perjury" that the information reported is complete and correct.[185] The government also uses this approach to bolster its effort to keep taxpayers honest by regulating tax preparer gatekeepers: a tax preparer must sign each tax return he or she prepares.[186] From a commitment and consistency perspective, these signature requirements may serve as a semi-public statement in support of tax compliance. The concept is similar to the idea of taxpayers signing an honor code before completing their returns.[187]

This idea of asking taxpayers and tax preparers to sign tax returns could be more closely tailored to the current tax gap problem. For example, the government's tax gap data show that Schedule C misreporting by sole proprietors yields a disproportionate amount of cheating.[188] It could accordingly ask each Schedule C taxpayer and tax preparer to sign a statement on Schedule C stating that reported income includes all revenue, cash and otherwise, and that deductions are accurately reported.

One might object that because such a strategy alludes to possible methods of tax cheating (i.e., not reporting cash revenue) it might backfire, by prompting a taxpayer to conclude that the smart minority

183. Cialdini, *supra* note 94, at 209 (proposing a three-step process for a commitment and consistency tax compliance campaign, consisting of "(a) identifying existing norms/values within the citizenry that can be conceptualized as related to issues of tax payment; (b) focusing attention on these norms/values as existing personal commitments and (c) sensitizing the citizenry to the inconsistency between possessing such personal commitments and failing to be fully tax compliant").

184. *See, e.g.*, IRS Form 1040 (U.S. individual income tax return containing oath).

185. *See id.* (relaying an oath that individuals must sign when completing their tax return to verify the accuracy of their statements).

186. *See id.* (containing a line for paid preparers to sign). *Cf. supra* note 64 (citing a 2008 budget proposal to increase preparer penalty for, among other things, failing to sign tax return).

187. *See* Nina Mazar & Dan Ariely, *Dishonesty in Daily Life and its Policy Implications*, 25 J. PUB. POL'Y & MKTG. 117, 123 (2006) ("[T]he IRS could slightly change its forms by making them more personal or asking people to sign an honor code of sorts before they begin filling out the forms.").

188. Schedule C lists sole proprietorship business profits or losses. *See* IRS Form 1040, Schedule C (titled "Profit or Loss From Business (Sole Proprietorship)").

reduces taxes by cheating, and that he or she should cheat too.[189] One could also object that such a tax return statement is inherently suspect as a true statement of positive commitment, because the enormous disincentive to state on one's tax return that one does not believe in tax compliance, and hence invite an audit, makes it easy for a taxpayer to rationalize her decision to sign as a decision to avoid an audit rather than a statement embracing tax compliance with which she must then conform her behavior.[190] If there is sufficient uncertainty about the likely success of this strategy, it might make sense to run an experiment to see if it works.[191]

3. Taxpayer Surveys

The IRS Oversight Board conducts an annual telephone survey through an independent firm, which consistently shows that the vast majority of Americans think that paying taxes is the right thing to do. For example, in the 2006 survey, eighty-six percent of respondents said that it was not acceptable to cheat at all on income taxes, and ninety-four percent "completely" or "mostly" agreed that "[i]t is every American's civic duty to pay their fair share of taxes."[192] These survey results agree with other studies done by independent organizations.[193] However, they contrast with results from various other developed countries, whose citizens are significantly less likely to think that tax compliance is a moral or civic responsibility.[194]

A survey with the goal of increasing tax compliance through commitment and consistency would target suspected tax cheaters,[195]

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189. *See supra* text accompanying note 106 (discussing possibility of identification with a clever minority).

190. *See, e.g.*, Hanson & Yosifon, *supra* note 83, at 123–24 (noting that cognitive dissonance more strongly prompts behavior to change attitude if the subject lacks an independent reason for the behavior).

191. *See infra* Part V.A (discussing measurement).

192. IRS OVERSIGHT BD., 2006 TAXPAYER ATTITUDE SURVEY 2 (2007), *available at* http://www.treas.gov/irsob/reports/2006_taxpayer_attitude_survey.pdf (charting responses to various questions posed regarding taxes, whereby eighty-six percent of people surveyed protested any amount of cheating on taxes, seventy-three percent completely agreed that paying taxes is a civic duty, and twenty-one percent mostly agreed that paying taxes is a civic duty).

193. *See, e.g.*, PEW RESEARCH CTR., A BAROMETER OF MODERN MORALS: SEX, DRUGS AND THE 1040, at 1 (2006) (reporting that seventy-nine percent of survey respondents believed that "[n]ot reporting all income on your taxes" was morally wrong).

194. *See, e.g.*, James Alm & Benno Torgler, *Cultural Differences and Tax Morale in the United States and in Europe*, 27 J. ECON. PSYCHOL. 224, 243 (2006) (reporting that U.S. citizens report stronger beliefs that paying taxes is a moral and civic duty compared to citizens from fourteen European countries).

195. Developing web-based individualization strategies designed to tailor internet offerings to individuals' preferences and needs could help in the formulation of a small business-focused

and make it as easy and attractive as possible for taxpayers to check the box marked tax compliance. For example, the survey might consist of only one or two questions and reward the participating taxpayer with a small prize.[196] An online survey tool could minimize costs.

An anonymous survey would follow the format adopted by the Oversight Board, which uses an independent firm. This approach is consistent with research that shows that it is more likely that we will change our behavior and beliefs to match prior commitments if we lack an excuse—such as, "I only said that on the poll because I didn't want the IRS to think I was a tax cheat and audit me." But it is inconsistent with the principle that a public commitment exerts a stronger pull to produce consistent behavior.

This problem of anonymity is similar to a problem faced by the proposal to add signature requirements to Schedule C, in that a public signed statement, generally the strongest commitment and consistency tool, may permit the taxpayer to dodge a commitment in the tax compliance case because it can be explained by the excuse of avoiding audit. In the case of the signature requirement, it is inevitable that the IRS will know whether the taxpayer signed the line. In the survey case, the taxpayers' statements to an independent firm might be public enough to spark a commitment response, even though they would not be revealed to the IRS, so that the audit avoidance cognitive excuse would not be as available to responding taxpayers. But, as discussed in the section below on measurement,[197] another layer of design difficulty is added by the desirability of matching tax return information with survey results so as to measure whether the survey tool actually worked.

4. Public Goods Propaganda and Earmarking

Americans' support for the public goods provided by the federal government might provide another avenue for commitment and consistency influence to work. World War II propaganda provides a good example of a tax compliance campaign that emphasized the public goods provided by the federal government. As Professor Carolyn Jones

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survey or other strategy, if consistent with taxpayer confidentiality and the government's interest in keeping the information on its website open to all without the need to, for example, enter a username and password. *See* WARD A. HANSON & KIRTHI KALYANAM, INTERNET MARKETING AND E-COMMERCE 131–38 (2007) (describing authentication, association, and interaction elements of a web-based individualization strategy).

196. *See* Hanson & Yosifon, *supra* note 83, at 122–23 (reviewing experimental literature showing that smaller prizes can foster more acute cognitive dissonance between stated beliefs and previous attitudes, prompting a change in attitude to conform to the stated belief and resolve the cognitive dissonance).

197. *See infra* Part V.A (discussing measurement issues).

has related, President Roosevelt and his Treasury Secretary, Henry Morgenthau, regarded the project of persuading Americans to pay their taxes as akin to the project of convincing them to buy war bonds.[198] They used techniques including radio ditties, pamphlets and posters, and Donald Duck cartoons, and prompted taxpayers to demonstrate their patriotism by properly filing their taxes.

With a majority of American voters calling for withdrawal of U.S. troops from Iraq,[199] the Donald Duck cartoon does not directly translate into a good current support-the-war-effort ad campaign. Indeed, the *New Yorker* ran a cover in April 2007 that showed 1040s and other familiar tax forms folded into paper airplanes and tanks, which illustrated that emphasizing federal spending can result in dissatisfied taxpayers unhappy with how the government spends tax revenue.[200] But even if defense spending is not popular, other federal spending might be. Perhaps we would feel more positive about paying taxes if we imagined those dollars going to preserve national parks, maintain a federal highway we rely on, or provide the Social Security benefits that offer some subsistence to the elderly.

A public goods campaign presents the challenge of selecting a level of generality when describing the public goods. Should the campaign highlight a good that target taxpayers are thought to value highly, in an effort to increase the salience of the communication? Or should it appeal more generally to the value of unspecified public goods?[201] In addition, a public goods campaign that aims to take advantage of the commitment and consistency principle of influence must include a way for taxpayers to publicly affirm that they value the public goods (or at least some of them) supplied by the government and accordingly pay their taxes willingly, perhaps even with pride.

One real-world experiment has tested the ability of a public goods appeal to improve taxpayer compliance.[202] In its 1995 study, the Minnesota Department of Revenue sent 20,000 taxpayers a letter explaining that "your income tax dollars are spent on services that we

198. *See* Carolyn C. Jones, *Class Tax to Mass Tax: The Role of Propaganda in the Expansion of the Income Tax During World War II*, 37 BUFF. L. REV. 685, 687–88, 699–703 (1989) (describing the tax propaganda campaign).

199. *See, e.g.*, Pew Research Center, Public Attitudes Toward the War in Iraq: 2003–2008, http://pewresearch.org/pubs/770/iraq-war-five-year-anniversary (Mar. 19, 2008) (reporting that fifty-four percent believe that the decision to enter the war in Iraq was wrong).

200. Christoph Niemann, *T-Day*, NEW YORKER, Apr. 9, 2007, *available at* http://www.newyorker.com/magazine/toc/2007/04/09/toc_20070402.

201. *See* Kornhauser, *supra* note 24, at 164 (noting the pitfalls of focusing on specific public goods).

202. *See* Coleman, *supra* note 104, at 5 (discussing the Minnesota survey).

Minnesotans depend on."[203] The letter mentioned important services including law enforcement, parks, and highways.[204] Taxpayers receiving the letter submitted tax payments exceeding those of a control group by about 0.8% of average income, but the results were not statistically significant.[205]

The Minnesota study included fairly broad descriptions of public goods, but it is not clear that factor led to the lack of a statistically valid result. Other factors such as the salience of the letter format may have had relevance. In addition, the study did not ask taxpayers to take any action demonstrating their commitment to tax compliance.

One way to finesse the conflict between making a salient communication about relevant public goods and avoiding alienating taxpayers who do not care for the identified good is to have the taxpayers confirm their commitment to a good of their choice. For example, the government could permit taxpayers to earmark a small portion of their tax payments for projects they support.[206] It could also invite taxpayers to create their own tax compliance content.[207]

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203. *Id.* (internal quotation marks omitted).

204. *Id.* The letter stated in part: "Over 30 percent of state taxes go to support education. Another 18 percent is spent on health care and support for the elderly and the needy. Local governments get about 12 percent of the state tax money, supporting services in your community such as law enforcement, parks, libraries and snow removal." *Id.*

205. *See* Blumenthal et al., *supra* note 104, at 125, 128, 131, 134, 137 (describing the study and results).

206. *See* IRS Form 1040 ("Check here if you, or your spouse if filing jointly, want $3 to go to this fund"). The federal government currently allows earmarking up to $3.00 per individual taxpayer for the Presidential Election Campaign Fund. *Id. See also* Cialdini, *supra* note 94 at 210 (considering the possibility of allowing earmarking for a fund to combat tax cheating). California takes a different approach: if a Californian wishes to add to his or her tax bill, he or she may pay extra to support one of fifteen funds ranging from the California Sea Otter Fund to the Alzheimer's Disease/Related Disorders Fund. *See* State of California Franchise Tax Board Form 540, *available at* http://www.ftb.ca.gov/forms/2008/08_540.pdf (listing various funds that can be donated to under a "Contributions" section).

207. There is some precedent. In 2007, TurboTax sponsored a tax rap video contest, which included an original Vanilla Ice clip, resulted in the submission of 370 homemade rap videos through YouTube, and garnered more than 2.5 million views. *See* Press Release, BusinessWire EON, "It's Just a Breeze" Delivers 25 Gs!: Grand Prize Winner Takes Home $25,000 in TurboTax TaxRap Contest (Apr. 14, 2007), *available at* http://www.prweb.com/releases/intuit/turbotax/prweb518806.htm (discussing a contest where TurboTax gave away money to the best "homemade rap video"). The IRS could sponsor a contest with a subject like "Don't Cheat Me." And the Tax Foundation announced a similar video contest to raise awareness of the high U.S. corporate tax rate and its impact on global "competitiveness." See Press Release, Tax Foundation, Win $5,000 in the Tax Foundation's CompeteUSA Video Contest (Sept. 10, 2008), *available at* http://www.taxfoundation.org/press/show/23592.html (discussing a contest where the Tax Foundation awarded money to videos aimed at raising "awareness of America's high business tax rates and how those taxes have an impact on our competitiveness, wages, and living standards").

V. COMPLICATIONS

A. Measurement and Cost-Benefit Analysis

Adding salience and influence to the reporting, audit, and other strategies already populating the tax gap toolbox raises a cost-benefit question: which strategy will make the most progress in closing the tax gap at the least cost?[208] As to costs, although they should be quantified and budgeted, many of the strategies, including audit and other publicity, and the taxpayer survey idea, could be executed with relatively modest investment, so long as the IRS website and direct mail or email are used as the main avenues of content distribution. A handful of employees could create and post a testimonial video or run a survey. Other ideas would cost more. A ten dollar coupon applied to the tax return of every Schedule C filer appears more expensive—about $215 million—although this figure does not account for the increases in tax payments prompted by the coupon reciprocity strategy. The upfront costs of a lottery could be less expensive.

As to benefits, because noncompliance by self-employed and small business taxpayers produces such a large tax revenue shortfall, strategies that succeed in increasing compliance only modestly could have a significant positive revenue effect. Moreover, the strategies described below might help to measure the impact of different influence programs so that the government could direct resources at the most promising ideas. In addition, testing and measuring strategies could minimize the possibility that a message or method backfires and worsens the public perception of the IRS or target taxpayers' inclination to comply.

One measurement approach would examine actual filed returns.[209] For example, the IRS could distribute the social proof testimonial approaches described above[210] by email or direct mail to a sample group of Schedule C filers; initiate a relationship of reciprocity with a sample group by sending a sample group a gift;[211] or, with the help of tax software companies, allocate forms to some taxpayers forms bearing additional signature lines on Schedule C while giving other taxpayers

208. See Colleen E. Medill, *Transforming the Role of the Social Security Administration*, 92 CORNELL L. REV. 323, 352–53 (2007) (setting forth principles including understanding the target audience, hiring creative professionals, developing a brand, and using peer focus testing groups).

209. *See* Blumenthal et al., *supra* note 104, at 128–30 (outlining experiment design).

210. *See supra* Part III.A (describing testimonial strategies).

211. *See supra* Part IV.B (describing reciprocity strategies).

forms with no additional signature lines.[212] In each case, compliance could be measured based on actual tax returns filed.

Other tactics, notably commitment and consistency approaches such as surveys and contests, depend on participation by the taxpayer.[213] It would be more difficult to tie the results of such tactics to filed tax returns, because, in order to do so, taxpayers who voluntarily respond would also need to provide their taxpayer identification number or similar information.[214] In addition, taxpayers who participate may be taxpayers who are more likely to pay their taxes in the first place, creating a thorny bias problem.

Measuring compliance based on actual tax returns filed would generate satisfying empirical data, but it would be slow.[215] Focus group measurement could provide a quicker response, and focus groups could help develop the message while providing useful data about the likely success of the campaigns.[216] For example, one might survey group members before and after viewing advertising content relating to cash income, audit publicity, or tax preparer diligence, or before and after responding to surveys about their tax compliance views.

B. Politics

Could legislation directing the IRS to use influence tools to increase tax compliance achieve a positive revenue score, and therefore a boost in the legislative process? Lawmakers sometimes subtly delegate spending increases to administrative agency action to keep them out of a budget process constrained by PAYGO rules.[217] These rules consider it

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212. *See supra* Part IV.C.2 (describing tax return signature strategy).

213. *See supra* Part IV.C (describing commitment and consistency strategies).

214. The success of phishing scams provides some evidence that taxpayers would readily supply IRS with their personal information. *See* IRS, BEWARE OF PHISHING SCHEMES (2008), *available at* http://www.irs.gov/pub/irs-pdf/p4523esp.pdf (warning taxpayers about potential identity theft emails and phone calls). But the taxpaying public may also become more concerned about the risks of identity theft. *See, e.g., id.* (exemplifying the warnings that the IRS is publishing).

215. *See* Blumenthal et al., *supra* note 104, at 131–32 (reporting 1995 data in 2001). The researchers in the Minnesota study, for example, published their results in 2001, six years after 1995, when the letters were sent and the related tax returns filed. *Id.*

216. Testing through peer focus groups has been called a "best practice" of public service advertising. *See* Medill, *supra* note 208, at 353 (recommending that public service ad campaigns "use[] peer focus groups to test the target audience's reaction to various marketing messages").

217. *See* Elizabeth Garrett, *Harnessing Politics: The Dynamics of Offset Requirements in the Tax Legislative Process*, 65 U. CHI. L. REV. 501, 530–36 (1998) (citing the example of language in a 1993 Congressional report that implicitly urged the Treasury to adopt hedging regulations permitting ordinary loss rather than capital loss treatment in the wake of *Arkansas Best Corp. v. Commissioner*, 485 U.S. 212 (1988)).

out of order[218] to present a measure that increases a budget deficit or decreases a budget surplus.[219] Because administrative regulatory action affects the baseline for the analysis of the impact of a piece of legislation on the budget, an administrative tax cut does not require reconciliation under the PAYGO rules of the budget process.[220] Moreover, a later legislative endorsement of an administrative position is also costless under PAYGO, because the previous regulatory action will already have been incorporated into the baseline.[221]

The potential use of influence strategies by the IRS to help close the tax gap presents the opposite problem. Revenue increases resulting from an IRS decision to adopt one or more influence strategies would generally not yield revenue-raiser credit under PAYGO, although they provide a politically attractive way to pay for other policies without raising taxes or violating PAYGO.[222] If Congress wished to count the revenue and receive some credit for a stepped-up program of influence, it might need to change the method of computing revenue raisers and losers. Non-substantive provisions with significant compliance power,

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218. *See* Cheryl D. Block, *Pathologies at the Intersection of the Budget and Tax Legislative Processes*, 43 B.C. L. REV. 863, 880–81 (2002) (explaining the workings of procedural budget reconciliation rules, including the process for waiving such rules).

219. PAYGO rules were reinstated by the newly installed Democratic House in January 2007. *See* Lori Montgomery, *House Adopts Pay-as-You-Go Rules*, WASH. POST, Jan. 6, 2007, at A4 (characterizing rules as targeting deficit spending). A similar Senate bill introduced by Majority Leader Harry Reid in January 2007 did not pass. *See* Restoring Fiscal Discipline Act of 2007, S. 10, 110th Cong. (2007) (proposing "[t]o reinstate the pay as you go requirement"). The House rule specifies that the House Committee on the Budget determines the impact of proposed legislation on the budget deficit or surplus using CBO baselines as a starting point. *See* H.R. Res. 6, 110th Cong. § 405 (2007).

220. *See* Garrett, *supra* note 217, at 535 (describing ordinary loss hedging regulations as "a fix that for budget purposes was free"). Regulatory actions are incorporated into the baseline score used by the Congressional Budget Office "[i]f it is clear, under current law, that an action will take place." Letter from Peter R. Orszag, Director, Cong. Budget Office, to Hon. John M. Spratt Jr., Chairman, House Comm. on the Budget 2 (May 2, 2007), *available at* http://www.cbo.gov/ftpdocs/80xx/ doc8060/05-02-LetterOnRegs.pdf. They are not incorporated "if it appears unlikely that an action will take place or that it will have any significant budgetary effect." *Id.* Infrequently, a regulatory action may be discounted, for example by fifty percent, if "it is unclear whether there will be an action." *Id.*

221. *See* Garrett, *supra* note 217, at 535 (noting that a legislative response to litigation claiming the invalidity of the ordinary loss hedging regulation would not produce a revenue loss for budget purposes).

222. *See* Edmund L. Andrews, *Democrats Seek Unpaid Taxes, Inviting Clash*, N.Y. TIMES, Feb. 5, 2007, at A1 (reporting the response of Senator Max Baucus, chairman of the Senate Finance Committee, to one set of Treasury proposals aimed at the tax gap, which estimated to generate less than $10 billion annually). Senator Baucus stated: "I know they can't recover every dollar of the tax gap, but the I.R.S. needs to make an aggressive effort, and an honest one. . . . Treasury shouldn't lowball their estimate." *Id.* (internal quotation marks omitted).

such as e-filing requirements[223] and information sharing,[224] typically earn a zero revenue score.

C. Nondiscrimination

The strategies proposed in this Article would acknowledge that taxpayers are behavioral creatures, not rational individuals. This presents a tension with government actors' obligation to treat all citizens—or taxpayers—equally.[225] Behavior is influenced by different factors for different people, and protected classifications such as race and gender are surely among the most powerful influence factors.[226]

Consider the social proof strategies outlined in Part III above. One might execute these tactics—whether applied to honest cash business taxpayer testimonials, audit publicity, or tax preparer diligence guidance —through a spokesperson who belonged to the same demographic group, as organized by type of business, location, race, religion, gender, socioeconomic grouping, and so forth. This presents at least three concerns.

First, the designers of a campaign must research and choose the right demographic. Second, there are likely to be quite a few appropriate demographics. Third, this kind of approach involves a certain degree of stereotyping which the government might find awkward.[227] For example, a social proof testimonial campaign that featured a female manicurist and a male construction contractor, each explaining why they paid their taxes, might tap into de facto labor force splits, increasing the strength of the social proof strategy, but might also create the impression that the government endorses those splits, and the wage gaps that accompany them.

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223. *See* 2009 BLUEBOOK, *supra* note 42, at 75 (giving a "[n]o revenue effect" score for a proposal to require e-filing for large organizations).

224. *See id.* at 78 (giving a "[n]o revenue effect" score for a proposal that would improve computerized data matching abilities by providing employment data to the IRS and permitting the IRS to share data with the NDNH—National Directory of New Hires).

225. *See* U.S. CONST. amend. XIV, § 1 (equal protection clause).

226. *Cf.* Kornhauser, *supra* note 24, at 166 (considering public service campaigns that target specific markets with forms that "match the target audience in language and media use").

227. Absent an intention to discriminate or a focus on members of a protected class, however, the use of social proof advertising strategies should not violate the equal protection clause. *See, e.g.*, Washington v. Davis, 426 U.S. 229, 245–48 (1976) (validating, in the absence of other evidence of an intent to discriminate, a written police test that had a disparate impact on blacks in that a disproportionate number of blacks failed to pass the test); Kotch v. Bd. of River Port Pilot Comm'rs for Port of New Orleans, 309 U.S. 552, 564 (1947) (upholding licensing scheme that, through its apprenticeship requirement, favored pilots who were related to or friends of existing pilots).

An influence campaign would have to navigate between the importance of tapping into salient influence factors for its target audience and the risk that a campaign that recognizes racial, gender, age, socioeconomic, and other differences in its audience may have the appearance of discrimination. But it is possible to transcend the stereotyping problem. The advertising industry has developed the art of offering images with which many different audience members can connect.[228] The potential of salient and influential communication could make the effort worthwhile.

CONCLUSION

Salient communications and greater attention to principles of influence would better target the existing norm of tax noncompliance among small business and self-employed taxpayers. Salient and influential communications could also enhance existing strategies for closing the tax gap, including third-party reporting, audit, and gatekeeper proposals. This Article has described social proof strategies that would improve the relevance and power of government communications about taxpayers' obligations to pay tax on cash income, the risk of audit, and the due diligence requirements for tax preparers. It has also outlined how the influence tools of reciprocity and commitment and consistency could help launch a cooperative tit-for-tat partnership between taxpayers and tax administrators. Though the prospect of improving the salience and influence of IRS interactions with the taxpaying public involves complications, policymakers should make use of this powerful category of tools in their effort to close the tax gap.

228. *See* Medill, *supra* note 208, at 353 (noting the success of "stark, graphic images about death and disease caused by tobacco usage").