

# The Effects of IRS Enforcement on State Tax Revenues

Presented at the Multistate Tax Commission's  
Fall Meeting of the Uniformity Committee

New Orleans, LA  
November 18, 2025

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# About ITEP

## The Institute on Taxation and Economic Policy (ITEP)

- Non-profit, non-partisan
- Federal, state, and local tax policy issues
- Research and data focused
- ITEP Microsimulation Tax Model



**This work starts from a simple premise:**

**Less IRS funding**



**Lower compliance with the tax law**



**Smaller federal tax base**



**Smaller state tax bases (and less tax revenue)**

# What I can offer today:

- Overview of the issue
- Framework for thinking about what matters to states
- A reason to sign up for ITEP's email list

# What I CAN'T offer today:

- Firm estimates of state revenue at risk

The image depicts a theater stage with red curtains and black seats. The text is centered on the stage.

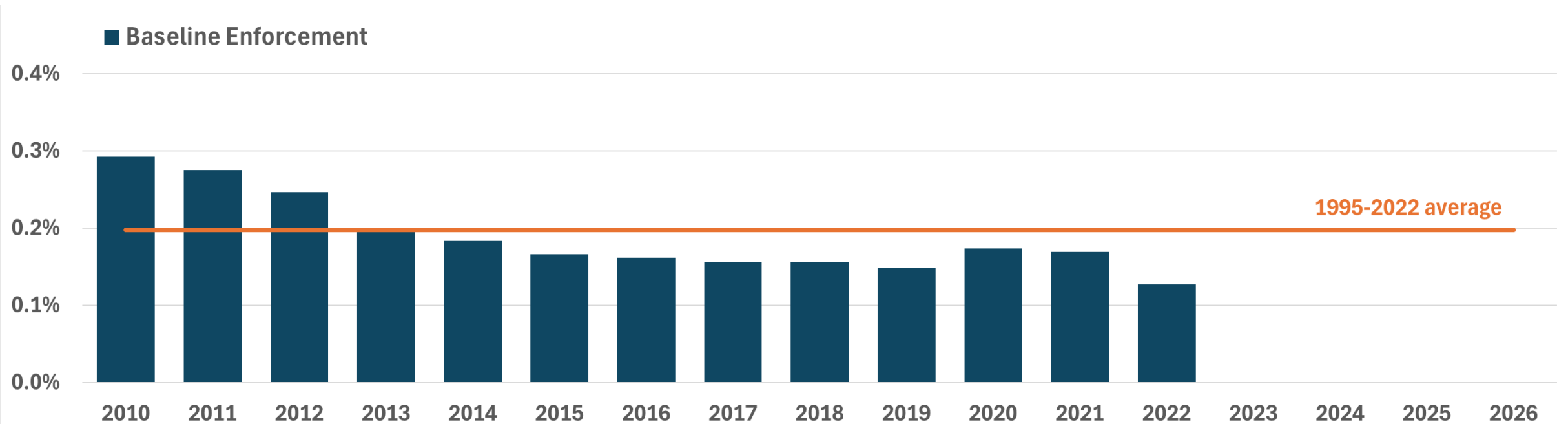
*Presenting:*

**A HISTORY OF THE  
IRS ENFORCEMENT BUDGET**

**IN 4 ACTS**

# Act 1: IRS enforcement budget in decline

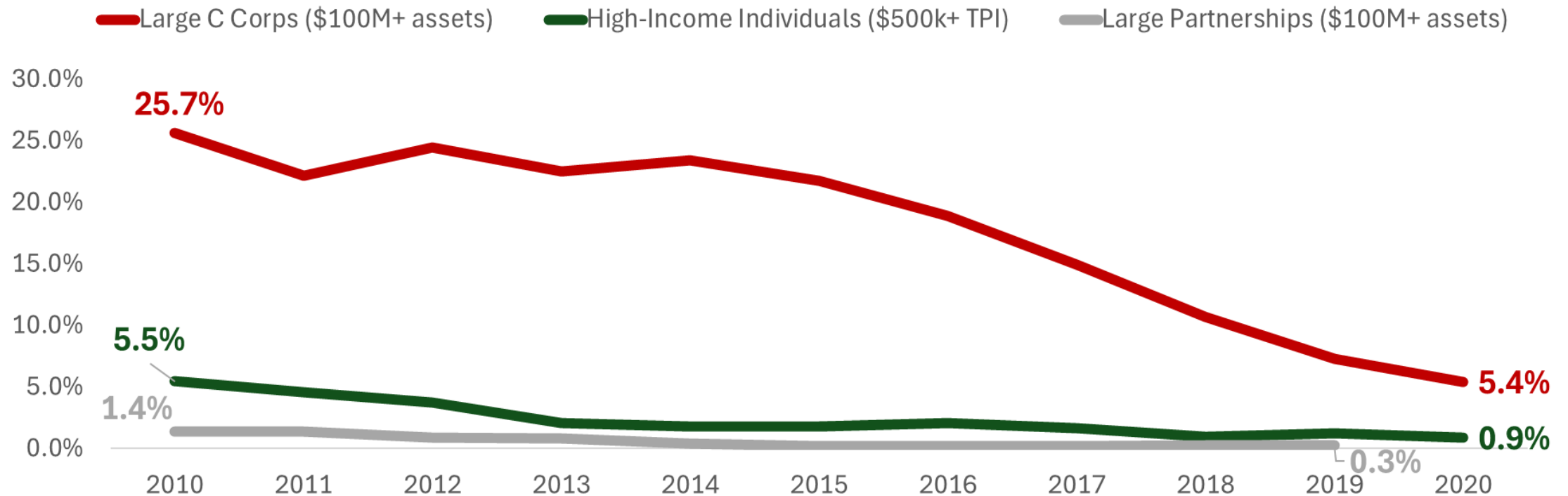
Share of IRS-collected revenue spent on tax law enforcement



Source: ITEP analysis of IRS data

# Chance of Being Audited has Dropped Dramatically for High-Income Filers and Large Companies

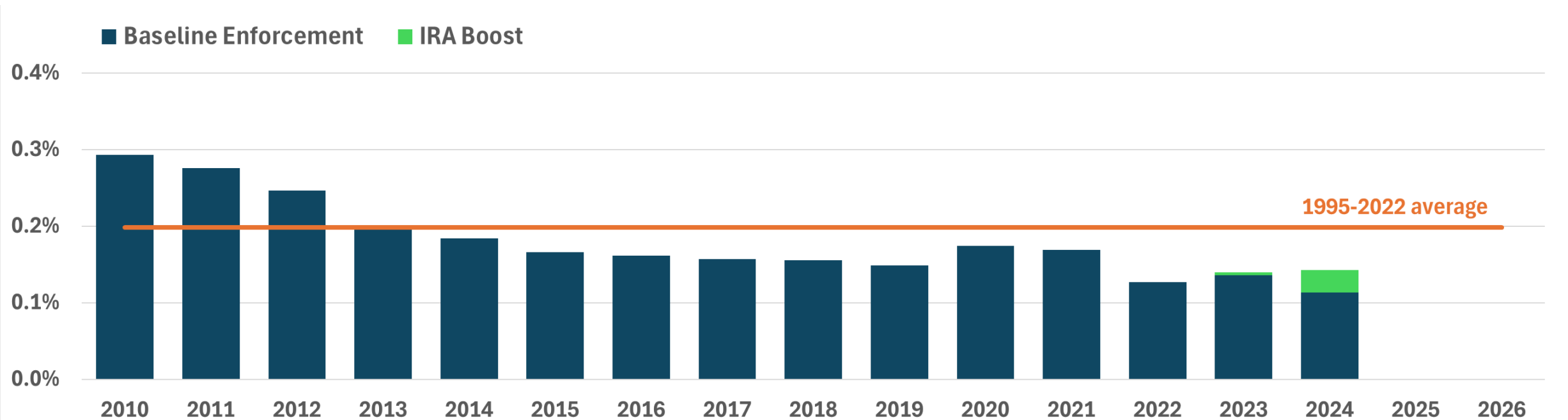
Audit coverage rates for select return types, 2010-2020



Source: ITEP analysis of data reported by IRS and GAO

# Act 2: Inflation Reduction Act stems the tide

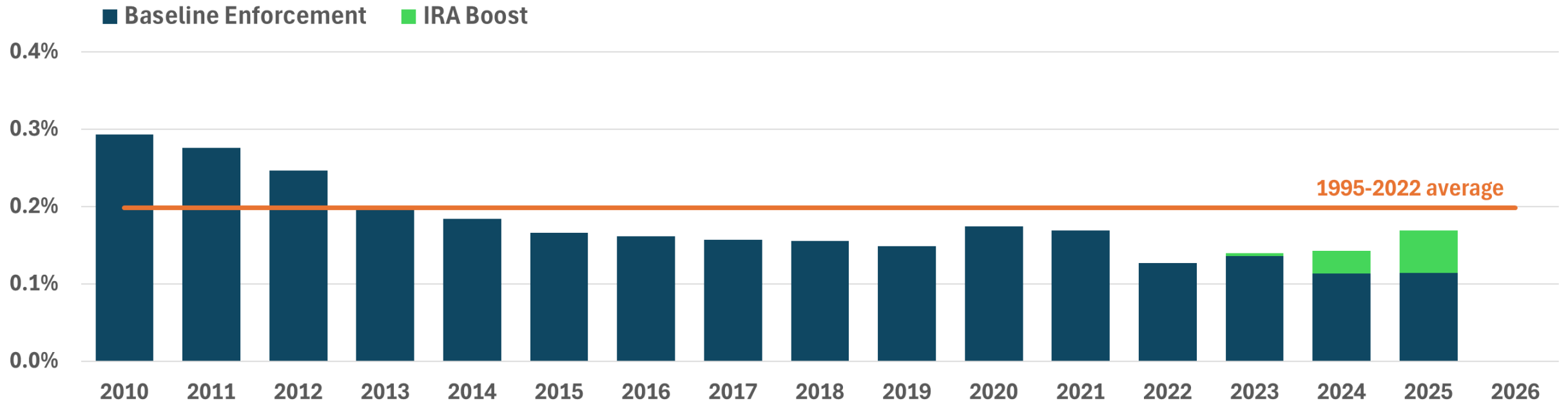
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# Act 3: Biden intends to continue post-IRA trend

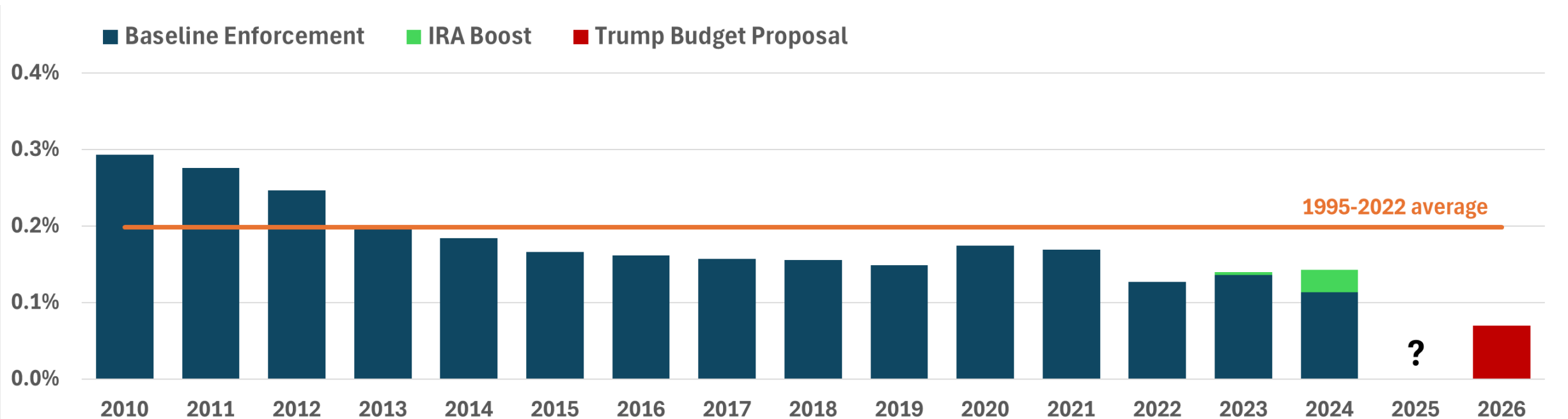
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# Act 4: Trump reverses course

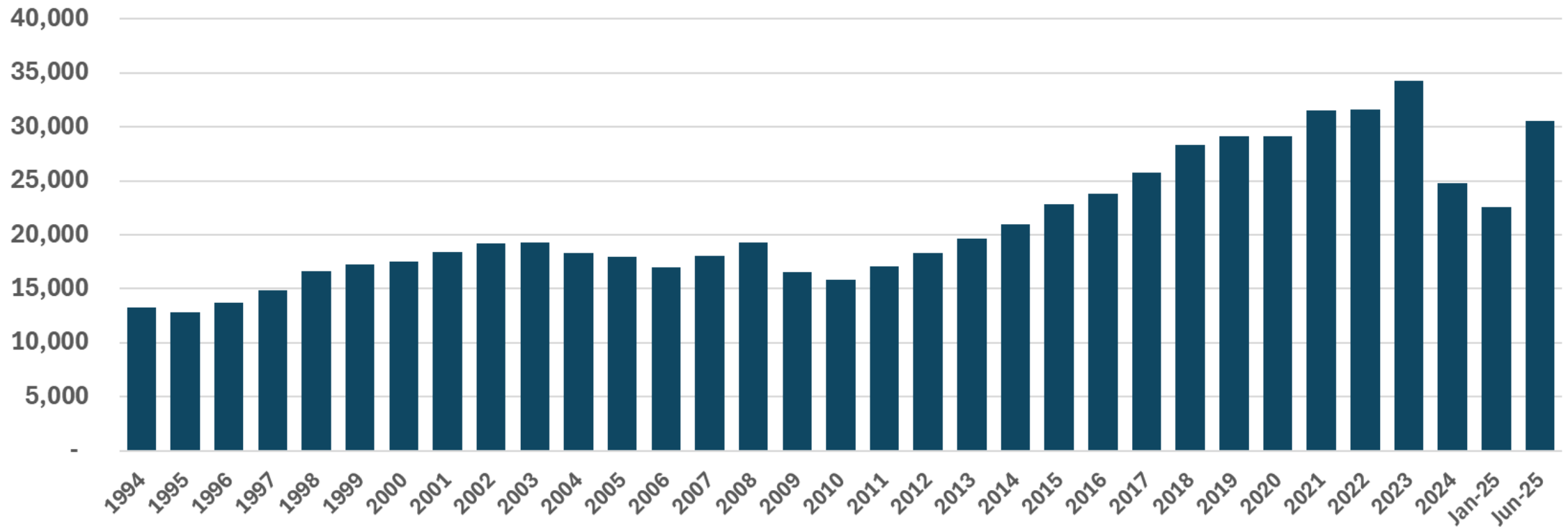
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# Auditors stretched increasingly thin

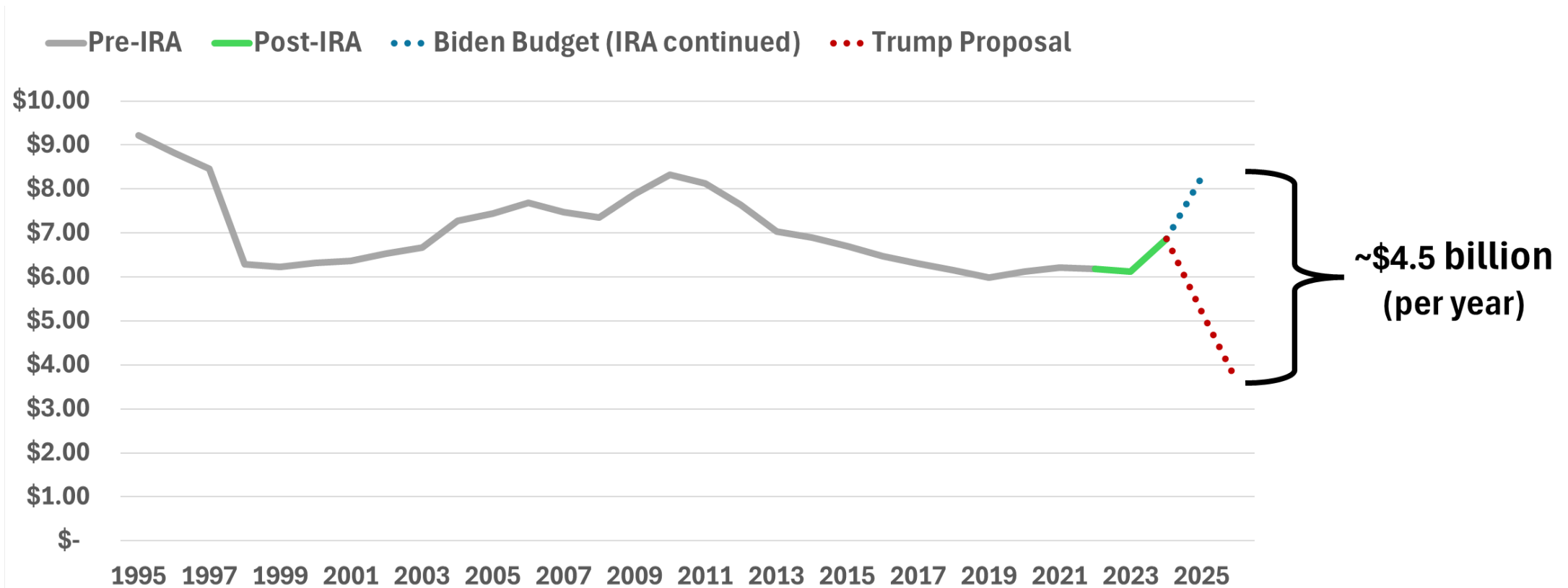
Returns filed per revenue agent



Source: ITEP analysis of IRS data

# Federal policy shift brings massive change to trajectory of IRS enforcement budget

IRS enforcement budget, inflation-adjusted 2026 dollars



# IRS funding impacts on federal tax collections:

**Nonfiling  
Enforcement**

**Underpayment  
Enforcement**

**Underreporting  
Enforcement**

**Taxpayer  
Services**

# IRS funding impacts on state tax collections:

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Enforcement**

**Underpayment  
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**Underreporting  
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**Taxpayer  
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\* Not a focus in today's remarks

# Audits yield a high return on investment (ROI)

## Direct ROI

### Individuals, by income level\*

2.17 to 1	Overall
0.96 to 1	Bottom 50%
3.2 to 1	99 to 99.9th percentile
6.29 to 1	Top 0.1%

4.25 to 1	Top 1% as a group
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Sources:

\* Boning et al. (2025). "A Welfare Analysis of Tax Audits Across the Income Distribution." *The Quarterly Journal of Economics* 140(1), 63-112.

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### C Corporations, by asset level\*\*

5.0 to 1	Overall
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2.9 to 1	\$1B to \$5B
5.4 to 1	\$5B to \$20B
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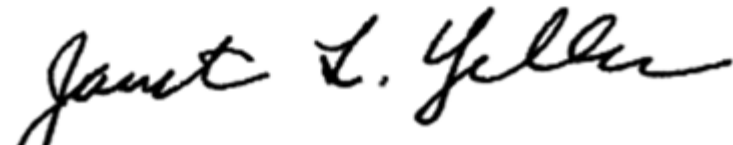


DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C.

August 10, 2022

... I direct that any additional resources—including any new personnel or auditors that are hired—shall not be used to increase the share of small business or households below the \$400,000 threshold that are audited relative to historical levels...

Sincerely,



Janet L. Yellen

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## Indirect ROI

3 times the direct effect\*\*\*

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\*\*\* Boning et al.; U.S. Treasury Department

# IRS enforcement cuts have been widely publicized:



- ***IRS Retreats From Some Audits as Agency Slashes Workforce***



- ***IRS faces massive cuts as audit rates plunge***



- ***IRS cutting its workforce by 25%, eliminating agency's civil rights office***



- ***Stalled Audits and a Skeleton Staff: Inside Trump's War on the I.R.S.***



# An example:

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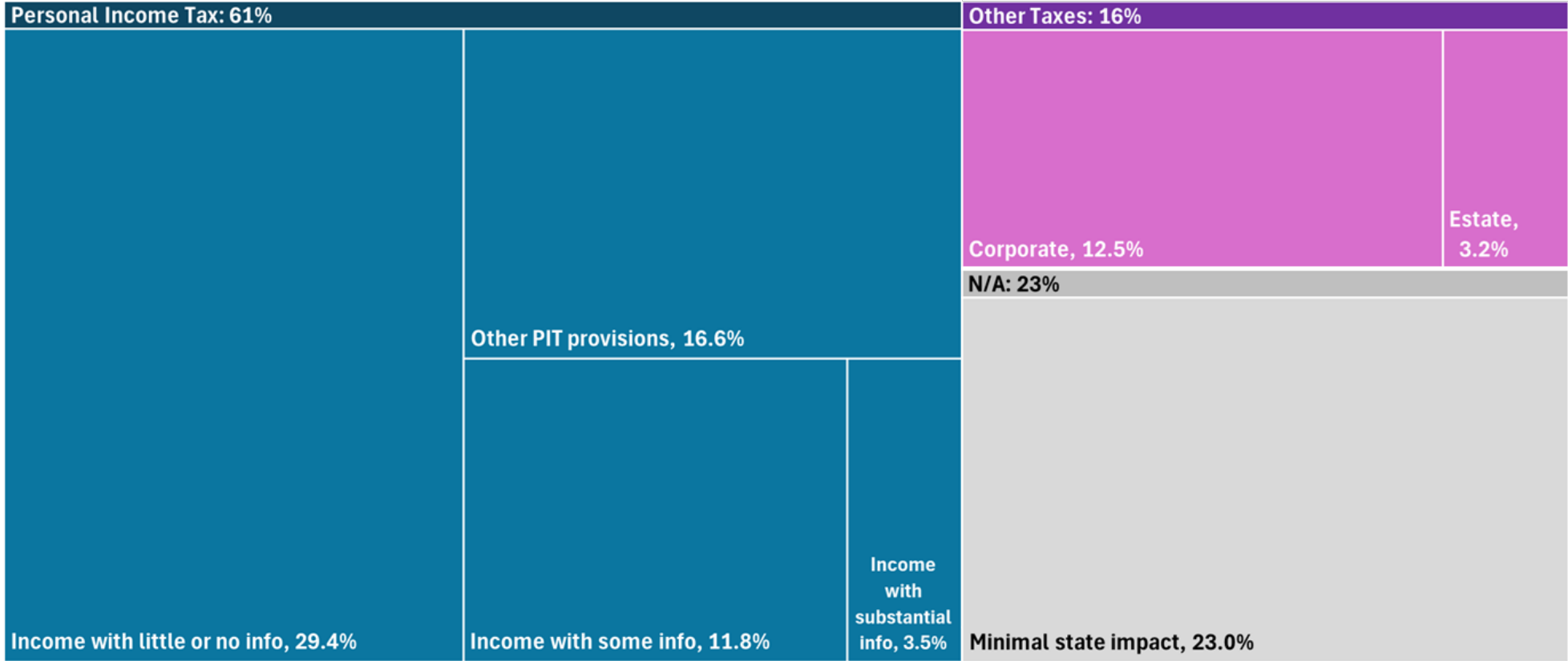
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**\$56.8 Billion**

# How much this matters to each state depends on...

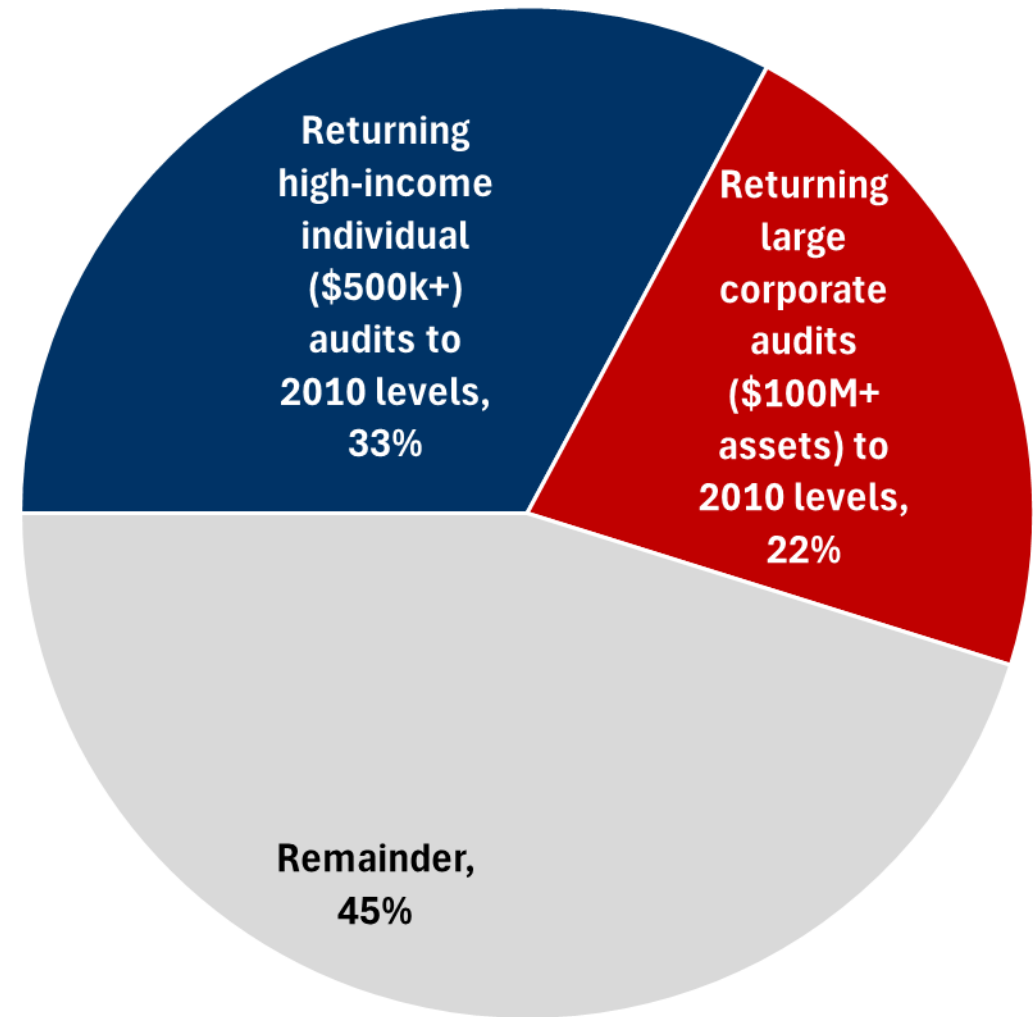
1. What kind of noncompliance IRS is finding.
2. Character of state economy / potential tax base.
3. State tax laws.

# Enforcement dollars raised from examinations



**Source:** Preliminary analysis of IRS data by the Institute on Taxation and Economic Policy. Not for citation.

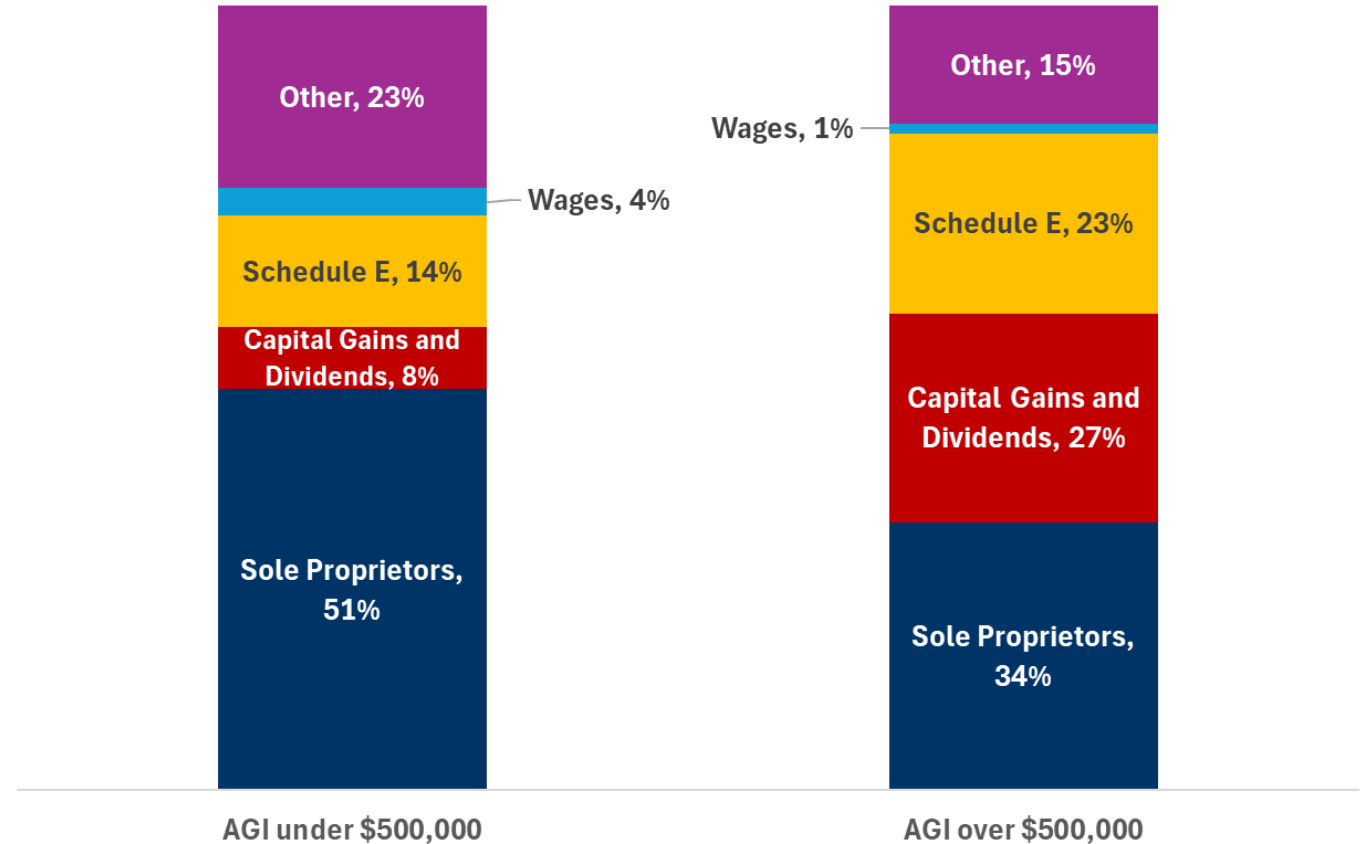
What kinds of audits could the IRA have funded?



**Source:** Preliminary ITEP analysis of data from IRS, CBO, Boning et al. Projection for FY2026. Not for citation.

High-income (and business) audits uncover different issues than other audits.  
For example:

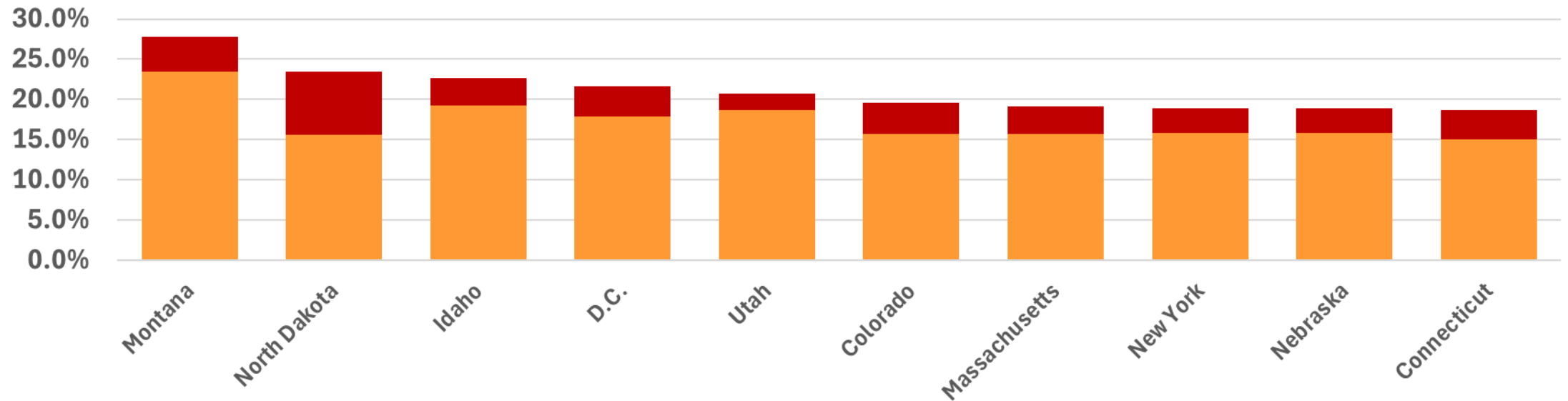
## Composition of Underreported Income Discovered on Audit, by Income Level



**Source:** Preliminary ITEP analysis of data published in DeBacker et al. (2020). "Tax Noncompliance and Measures of Income Inequality." *Tax Notes State*.

## Top 10 States with Income Taxes where Income Composition Tilts Most Heavily Toward Frequently-Underreported Types of Income

Some Info Reporting Little or No Info Reporting



**Source:** Preliminary analysis of IRS data by the Institute on Taxation and Economic Policy. Not for citation.

# Preliminary results from generic \$4 billion enforcement cut (not for citation):

- \$12.7 billion loss to state and local revenue
- This suggests that:
  - States lose 22 cents for every \$1 the federal government loses
  - States lose roughly \$3 for every \$1 cut from federal enforcement budget

# Work left to do before publishing estimates:

- Finish disentangling IRA vs. non-IRA enforcement cuts
- Refine timing considerations (some effects occur with lag)
- Add analysis of taxpayer services
- Refine application of state tax parameters



**INSTITUTE ON TAXATION AND ECONOMIC POLICY**