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As IRS funding shrinks, California's wealthiest can breathe a bit easier

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WASHINGTON —

California millionaires and billionaires who were set to face the full auditing firepower of a revamped Internal Revenue Service can breathe a bit easier, thanks to congressional Republicans.

This week, President Biden signed a bill that slashes \$21 billion from a planned \$80-billion increase in the agency's funding — a key GOP demand as part of the bipartisan deal to lift the federal debt ceiling.

The audits that would have been funded by that new money could have hit rich Californians hard. Around half of the \$80 billion would have gone toward increasing tax compliance among Americans with incomes over \$400,000 a year, with the rest of the money earmarked for improving the agency's taxpayer services and modernizing its archaic technologies. California, which has more millionaire households and more billionaires than any other state and holds 17% of the nation's wealth despite having only 12% of its population, was due to face an outside share of the new enforcement actions.

"These cuts are great news for wealthy tax evaders and bad news for the rest of us," wrote Vanessa Williamson, a senior fellow at Brookings, a public policy think tank in Washington, in an email.

The IRS funding cuts will likely shrink government revenues by \$2.3 billion over the next 10 years, triggering a \$900-million spike in the federal deficit, according to a report from the nonpartisan Congressional Budget Office.

That money will instead stay in rich Americans' pockets. Without adequate enforcement funding, government officials struggle to collect taxes from the super-rich, explained Joe Hughes, Federal Policy Analyst for the Institute on Taxation and Economic Policy. Many wealthy households' filings are complicated, and auditors have to navigate "enormously complex business entities" with hundreds or thousands of sub-entities.

"That's a jigsaw that's really hard for an IRS agent to put together," Hughes said.

Some experts argue that spending more money poring over wealthy Americans' taxes is a waste of energy.

“High-earning taxpayers are more likely to receive expert tax advice, and thus less likely to make errors,” Chris Edwards, a policy scholar at the libertarian Cato Institute, wrote in congressional testimony that urged lawmakers to not spend so much money on additional tax enforcement as part of the debt-ceiling deal. “More aggressive IRS enforcement would increase taxpayer costs, as they would invest more time and energy defending themselves.”

Americans already spend some \$14.4 billion per year on tax-preparation services alone, according to one recent estimate.

But the fight to collect the taxes that the richest Americans owe is especially fierce in California, a hot spot for what author and Oscar Mayer heir Chuck Collins calls the wealth defense industry, the complex of law, accounting and money management firms that work to ensure that the richest Americans stay that way. The government is “completely outgunned,” argues Collins, who gave away his fortune at 26 and is now a senior scholar at the Institute for Policy Studies, a progressive think tank based in Washington.

Heirs to J. Paul Getty, the oilman who assembled one of California's most famous fortunes, maneuvered their wealth in an effort to limit the amount of taxes they paid, the New Yorker reported in January. Kendalle and Sarah Getty, according to the magazine, made an effort to convince tax collectors that they did not live in or conduct business in the Golden State to avoid state taxes. The Getty trusts were established in California, but Kendalle and Sarah's trust moved to Nevada. Robert Leberman, an administrator for the Gettys' trust, told the magazine at the time of publication that the family intended to “fulfill any and all tax obligations.”

California's tax collection service, the Franchise Tax Board, lacks “the expertise” to keep up with to that sort of “innovation” in the industry, Collins said. A fully-funded IRS is necessary for that, he said.

“California has a tax base that is incredibly volatile, so we are at the mercy of high-wealth individuals,” said Rep. Sydney Kamlager-Dove of Los Angeles, a Democrat who voted against the president's deal with Republicans. “And now, on top of that, we're coupling that with crippling the federal government's ability to go after them to just make sure that they're paying what they owe.”

Republicans, however, have vowed to go further in cutting the agency's funding.

“We're not going to stop until we get the rest of the IRS agents repealed,” House Speaker Kevin McCarthy (R-Bakersfield) told reporters in a triumphant speech after the House passed the bill partially repealing the new funding. “I promise you, I'll be back next year and next year and next year. Because I believe government should be here to help you — not go after you.”

Now the tax-collecting agency has been thrust into a state of uncertainty. In the immediate term, the bill rescinded \$1.4 billion already granted to the agency; it also asks lawmakers to divert \$20 billion to other nondefense spending programs over the next two years. Supporters of IRS

funding hikes say Democrats should fight to keep the dollars alive, especially because the agency has only recently emerged from a decade of devastating cuts. The IRS budget fell by \$2 billion from 2010 to 2017, a loss that in turn reduced government revenue by tens of billions of dollars, according to an estimate by ProPublica.

Without clear indicators of where its funding stands, the IRS is left with little impetus to kick off a crackdown, said Janet Holtzblatt, a senior fellow at the Urban-Brookings Tax Policy Center. After all, next year's funding is uncertain — especially given that Republicans have made it a priority to continue pushing for additional cuts. That uncertainty is heightened by the fact that cuts have come less than a year after the original \$80 billion was given to the agency, she added.

“Nine months later, you're already seeing a 27% reduction from that \$80 billion funding,” Holtzblatt said. “Is there any guarantee that Congress won't come back again and cut the funding? ... From a managerial perspective, that kind of uncertainty may curb enthusiasm for hiring additional staff and for making investments in technology.”

The fate of the IRS will ultimately be tied to the fate of Democrats' ability to control Congress. Rep. Adam B. Schiff (D-Burbank) said that if his party manages to take back the House in 2024, the tone of negotiations over government spending could shift, with IRS funding expansions back on the table.

Schiff has his own suspicion — that as the IRS takes on the ultra-wealthy, the ultra-wealthy are taking on the IRS. In America, tax avoidance is a bipartisan pastime. But Schiff claimed that Republicans in particular are at the mercy of ultra-wealthy donors, and that those donors don't want to be audited.

“If you defund the IRS, like Republicans are trying to do, it helps their wealthy and corporate donors all over the country,” Schiff said. “And that's really what they're all about.”