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INSIGHT

The Proposed $600 Bank Reporting Requirement: Frequently Asked Questions

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A proposal to require financial institutions to report information to the Internal Revenue Service (IRS) on personal and business accounts has garnered significant publicity and congressional attention. The proposal is commonly referenced as the "new $600 bank reporting requirement." This Insight addresses a number of frequently asked questions about the proposal.

What is the proposal and where did it come from?

The proposal referenced in media reports was included in the President's FY2022 budget request and is described as being part of a "comprehensive" financial account information reporting regime. The *General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals*, which accompanies the President's budget request, states that

> Financial institutions would report data on financial accounts in an information return. The annual return will report gross inflows and outflows with a breakdown for physical cash, transactions with a foreign account, and transfers to and from another account with the same owner. This requirement would apply to all business and personal accounts from financial institutions, including bank, loan, and investment accounts, with the exception of accounts below a low de minimis gross flow threshold of $600 or fair market value of $600.

The *General Explanations* also mention similar reporting requirements for cryptocurrency and state that payment settlement entities would be covered by the new regime. Additionally, crypto asset exchanges and custodians, as well as crypto transactions exceeding $10,000, would require information reporting.

Is the proposal included in legislation?

The new $600 bank reporting requirement proposal is not currently a legislative proposal. Some have suggested that it may be considered as Congress develops modifications to either the reconciliation bill (H.R. 5376), known as the Build Back Better Act, or the infrastructure bill (H.R. 3684, as amended and passed by the Senate on August 10, 2021).

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The Senate-passed version of H.R. 3684 includes a separate information reporting requirement that would require a party facilitating the transfer of cryptocurrency to file an information return as a broker with the IRS. The Senate-passed version of H.R. 3684 would also require a business that receives cryptocurrency worth more than $10,000 in a single transaction to report the transaction to the IRS. The Joint Committee on Taxation (JCT) estimates that these information reporting requirements would raise $28 billion over 10 years. For more information on this proposal, see CRS In Focus IF11910, *Cryptocurrency Transfers and Data Collection*, by Mark P. Keightley and Andrew P. Scott.

What is the purpose of information reporting?

There are two general purposes of information reporting. The first is to increase tax compliance and to reduce money laundering and illicit financial activity. The second is to provide information to taxpayers to allow them to accurately calculate their tax liability. When an information return is filed, a copy of the return is sent to the IRS and a copy is sent to the taxpayer. This allows the IRS to double-check the information reported by a taxpayer. Additionally, the IRS can use the information to flag returns for audit. At the same time, the copy sent to taxpayers provides them with information that they may need when completing their tax return. Taxpayers may also be more likely to accurately report their income if they know the IRS has this information. Information returns typically must be sent to the IRS and taxpayer early in the calendar year.

What are the current information reporting requirements?

A significant number of transactions are currently subject to information reporting requirements. The IRS's *Guide to Information Returns* identifies transactions in the following categories: general, education, health insurance, transfers of stock, and retirement. Financial institutions are currently required to file information returns for any account for which interest payments or dividends are $10 or more throughout the year. They are also required to report the amount of mortgage interest paid, student loan interest paid, amount of canceled debt, distributions from certain retirement accounts, and certain transactions in which they serve as a payment settlement entity, among others.

Taxpayers are legally required to pay the appropriate tax regardless of whether they receive an information return. For example, an individual who receives $9 of interest on a savings account is required to pay tax on that income, even if an information return is not received.

Is the proposal a new tax?

The proposed bank reporting requirement would not be a new tax. Information reporting, as the name suggests, provides more information to both the IRS and taxpayers. If, however, the additional information results in taxpayers making additional payments in compliance with existing tax laws, taxpayers may pay more in taxes.

What are the trade-offs involved with information reporting?

Information reporting raises a number of general policy considerations. One concern is the appropriate balance between government data collection and the rights of individuals. Information reporting may

assist the IRS in fulfilling its statutory obligation to administer the tax code, but it also subjects individuals and businesses to greater government scrutiny. Another consideration is that increased information reporting would place an administrative burden on financial institutions required to make reports. The magnitude of such a burden is not necessarily clear given that financial institutions are already required to report certain information. At the same time, increased information reporting may assist individuals in completing their tax returns and more easily complying with the law. With regard to the proposed bank reporting requirement, it is not clear how knowing one's financial *flows* throughout the year would help in determining taxable *income*.

How could increased information reporting reduce the tax gap?

The proposed $600 bank reporting requirement would likely decrease the tax gap by increasing tax collections. The tax gap is the difference between the aggregate amount of taxes legally owed and the aggregate amount of taxes collected. The latest IRS estimates suggest that the gross tax gap costs the federal government $441 billion in lost tax revenue per year. Late payments and enforcement actions reduce this gap to $381 billion. In an April 13, 2021, Senate Committee on Finance hearing, IRS Commissioner Charles P. Rettig raised the possibility that the tax gap may now be closer to $1 trillion per year once the rise in popularity of cryptocurrency, foreign-source income, taxable illegal income, and more recent estimates regarding high-income taxpayers are accounted for. Some have questioned the accuracy of this estimate. Still, the IRS's tax gap estimates clearly demonstrate that income subject to little or no information reporting is more likely to be underreported for tax purposes than income subject to more information reporting. About $245 billion (56%) of the gross tax gap is attributable to underreporting of income on the individual side. Income that is subject to little or no information reporting accounts for $109 billion (55%) of the $245 billion shortfall. Income subject to substantial reporting and withholding accounts for just $9 billion (1%) of the shortfall.

Author Information

Mark P. Keightley
Specialist in Economics

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