Changes to IRS Funding in the Debt Limit Deal

Updated June 6, 2023

President Joseph Biden and House Speaker Kevin McCarthy brokered a deal that would reduce federal spending in FY2024 and FY2025 and raise the statutory debt limit through January 2025. P.L. 118-5, the Fiscal Responsibility Act of 2023, enacts many of the components of the deal between the President and the Speaker. President Biden signed the bill into law on June 3, 2023. If lawmakers had not raised the statutory debt limit by June 5, 2023, according to Treasury Secretary Janet Yellen, the debt limit would bind and the Treasury would have legal authority only to expend as much as it collects in revenue. Among the cuts to federal spending this deal makes are reductions in federal outlays for the Internal Revenue Service (IRS).

Background

Normal IRS Appropriations

Congress funds the IRS through annual appropriations for four primary categories of spending:

1. Enforcement ($5.4 billion in FY2023), which refers to enforcing the tax code;
2. Operations support ($4.1 billion in FY2023), which refers to the agency's ordinary operating expenses (including information systems);
3. Taxpayer services ($2.8 billion in FY2023), which refers to efforts to help taxpayers voluntarily pay their tax burdens in a timely fashion and resolve taxpayer issues; and
4. Business system modernization ($0 in FY2023), which refers to the ongoing effort to update the IRS's legacy information technology systems.

IRS-Related Funds in the Inflation Reduction Act

Congress provided the IRS with $78.9 billion in mandatory funding from FY2022 to FY2031 in P.L. 117-169, commonly referred to as the Inflation Reduction Act. The law dedicated $45.6 billion of that amount to enforcement, $25.3 billion to operations support, $3.2 billion to taxpayer services, and $4.8 billion to

Congressional Research Service
https://crsreports.congress.gov
IN12172

business system modernization. The law also provided roughly $700 million to related agencies to assist with the administration and enforcement of the tax code.

Uses of Funds

These funds were meant to supplement regular appropriations and provide the agency with stable funding for long-term projects. The IRS says it plans to use some of the funds to hire additional auditors and improve its technical capabilities for selecting returns for audit, particularly for high-income individuals and corporations, as well as within emerging tax issues such as cryptocurrency and complex international transactions. IRS Commissioner Danny Werfel has said the agency intends to avoid increasing audit rates above 2018 levels for households and businesses with annual incomes up to $400,000.

The agency also plans to use some of the IRA funds to expand its use of technologies that identify issues with taxpayers' returns before they file, conduct outreach to groups that qualify for tax benefits but fail to claim them, and make taxpayer data more accessible to customer service representatives. The agency also hopes to replace its Individual Master File and Business Master File, the core components of its IT system, which are decades old.

Opposition

The IRA funding has been controversial. Supporters contend it is necessary to counteract a decline in the IRS's total budget authority, which fell by 20% from its peak in FY2010 through FY2022, after adjusting for inflation. Spending on enforcement fell by 26% over that period. However, critics argue that expanding enforcement will put an excessive burden on taxpayers. On January 9, 2023, the House of Representatives passed H.R. 23, the Family and Small Business Protection Act, to repeal the IRA's funding for the IRS's enforcement and operations support accounts.

Fiscal Responsibility Act

Among other changes, the Fiscal Responsibility Act rescinds $1.4 billion that the IRA made available to the IRS for enforcement and operations support. While the legislation also identifies the sections of the IRA that funded related agencies as possible sources of such funding, it clarifies that the rescission must come from funds "appropriated or otherwise made available for activities of the Internal Revenue Service," suggesting that funds for other agencies would not qualify. The Congressional Budget Office estimates that this rescission will reduce revenues by $2.3 billion through 2033, and raise the federal deficit by $900 million over that period.

Deal on Appropriations

In addition to this rescission, the White House says it agreed with House leadership to reduce the IRS's annual appropriations in each of FY2024 and FY2025 by $10 billion. This change would represent a 79% reduction relative to the Congressional Budget Office's projection of the IRS's discretionary budget authority over those two fiscal years. The White House says it intends to use IRA funds to compensate for that decline in appropriations, but added that the Administration intends to move forward with the IRS's planned uses for the IRA funds.

Author Information

Brendan McDermott
Analyst in Public Finance

Disclaimer