



IMPACT OF GROWING GIG ECONOMY ON TAX POLICY

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KEY TAKEAWAYS:

Over the last decade, the exponential growth of technology in our daily life has made the so called “gig economy” a household term. While there is no single generally accepted definition, one thing for certain is that the gig economy continues to increase its importance in the U.S. and global economies. There are widely differing estimates for the size of the gig economy, indicating that between 25 and 30 percent of workers are involved in non-traditional or gig work. Gig workers are generally younger and use gig work for supplemental income. These wide-ranging estimates have become an important focus due to their potential impact on policy making, especially tax policy.

There are two important areas of concern that may need to be addressed:

- **The lack of benefits for workers in the gig economy:** Employer-based benefits, like health insurance and retirement plans, are very important for the financial wellness of many traditional workers. Unfortunately, many gig economy jobs do not provide these important benefits. In addition, many labor protections, such as minimum wages and overtime provisions, are not available for gig workers. The same is generally true for unemployment compensation that is financed by the taxes paid by businesses.
- **The tax consequences of changing work dynamics:** The gig economy has a significant impact on tax filing for individuals and tax administration for the government:
 - *Gig Workers:* Tax filing requires greater involvement of the taxpayer under gig economy. For many gig workers, income taxes are not withheld by employers, which may require additional time spent on quarterly tax payments or lead to surprise tax bills at the end of the year. Freelancers are also responsible for the payroll taxes that are normally paid by the employer. In addition, understanding what constitutes a business expense, keeping track of detailed business income and expenses, combined with a younger and financially less experienced workforce could translate into unintended noncompliance by gig workers.
 - *Tax Administration:* The current U.S. Administration has been paying close attention to the tax gap, the difference between the true tax liability for a given tax year and the amount that is paid,¹ to generate additional revenue for policy priorities. The portion of the annual tax gap due to underreported self-employment income amounts to \$45 billion for tax years 2011-2013.² As the gig economy continues to expand, underreporting of self-employment may become a bigger issue. Information reporting increases tax compliance, but up until this year, Treasury Regulations did not require certain gig economy businesses to issue Form 1099-K if work-

¹ For a detailed discussion of type of tax gaps and statistics, please see Pinar Cebi Wilber, “Internal Revenue Service: Increasing Workload Under Strained Budgets,” May 2021, ACCF, https://accf.ftlbcn.net/wp-content/uploads/2021/05/ACCF_IRS_Report_051221V3.pdf

² IRS, “Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2011-2013,” September 2019. <https://www.irs.gov/pub/irs-pdf/p1415.pdf>

ers earned less than \$20,000 and engaged in less than 200 transactions annually. The American Rescue Plan Act of 2021 reduces the Form 1099-K reporting threshold to \$600 regardless of the number of transactions. Still, not everyone receives their information through 1099-K and this has ramifications both for workers (making tax filing more difficult and increasing the risk of mistakes) and the IRS (making enforcement of the tax rules more difficult). In addition, the IRS has faced an increased workload with funding that has changed very little over the years, making decreasing the tax gap in an efficient manner more difficult.

Underpayment of income and self-employment taxes may also have a negative impact on efforts to fund Social Security. This could lead to lower Social Security benefits for gig workers and a greater burden on the government to support these individuals.

As the problems outlined above grow, there have been a growing body of research and policy suggestions. The IRS has been proactive in offering tools to help the gig workers with their tax filing, with the introduction of the Gig Economy Tax Center.³ The website is, in part, a response to 2019 recommendations of Treasury Inspector General for Tax Administration (TIGTA) to (1) Raise awareness about federal tax obligations and (2) ease burdens by identifying improvements to instructions, guidance, or forms that platform workers are likely to use.⁴

In addition to IRS's educational efforts, some of the main policy suggestions put forth by government agencies and other researchers are:

- Increase third party reporting requirements and/or lower thresholds for reporting requirements
- Improve the Automated Underreporter System to effectively evaluate and catch non-compliance geared towards self-employment taxes
- Implement voluntary withholding for estimated taxes for gig workers
- Simplify the tax process for gig workers by:
 - Creating a standard business deduction
 - Require platform companies to inform workers of tax obligations
 - Require platform companies to provide expense information
 - Make electronic delivery of Forms 1099 the default

In summary, as the gig economy grows policies need to be reshaped to deal with emerging issues in a cost-effective manner. The first step should be a consistent definition and reliable measurement of the size of the gig economy and its active participants. This should provide a good starting point for the tax administration. The next steps should make tax filing easier for the gig workers to increase tax compliance and lower the tax gap without further burdening taxpayers.

³ The website is: <https://www.irs.gov/businesses/gig-economy-tax-center>

⁴ GAO, "Tax Compliance: More Income Reporting Needed for Taxpayers Working Through Online Platforms," May 2020, <https://www.gao.gov/assets/gao-20-366.pdf>

IMPACT OF GROWING GIG ECONOMY ON TAX POLICY

INTRODUCTION:

Over the last decade, the exponential growth of technology in our daily life has made the so-called “gig economy” a household term. In simple terms, the gig economy is “economic activity that involves the use of temporary or freelance workers to perform jobs typically in the service sector.”⁵ Up until the start of the pandemic, there were conflicting views on whether these nontraditional work arrangements were here to stay and whether they would expand their reach, due to increasing regulation in recent years.⁶ However, due to the increased uncertainty during the pandemic, as well as changing attitudes and the desire for a more flexible work environment, a recent survey by Monster shows that 92% of respondents “think now is a good time to look into the gig economy.”⁷ While some individuals use these short term/contract based jobs to supplement their income, others depend on it as their sole source of income.

There is extensive research on the reasons for the increased popularity of the gig economy for workers and businesses, such as greater flexibility and independence for workers, lower costs and access to a diverse pool of talents for businesses, creating a more agile business model. But the policy ramifications of this economic trend are as important as these aspects. It is no surprise that governments around the world have begun crafting policies to keep up with the changing employment landscape. Some of these policies are still in the planning stage and will continue to take shape as the economy evolves.

This short report starts with the definition of and data on current trends in the gig economy to understand the extent of its impact on the overall economy, as well as the demographic characteristics of gig workers, and continues with related tax and policy issues.

WHAT IS THE GIG ECONOMY?

The U.S. economy has been going through a significant transformation over the last decade. One example of this is the rise of the “gig economy.” While there is no single generally accepted definition, one thing for sure is that the gig economy continues to increase its importance in the U.S. and global economies. There are various definitions of what constitutes a gig worker and the gig economy based on a number of criteria:⁸

- **Work Arrangement:** In a traditional work arrangement, a worker is paid by the hour or year, earning a wage or salary based on a long-term employer-employee relationship. But some arrangements, known as alternative or non-standard work arrangements, are temporary or project based. These arrangements include freelancing, self-employment, and subcontracted work.
- **Legal Classification of the Worker:** Legally, there is a difference between employees and independent contractors. Employees receive Form W-2, and are entitled to certain benefits, their payroll taxes are deducted from their compensation, and they are covered by minimum wage and anti-discrimination laws.

⁵ <https://www.merriam-webster.com/dictionary/gig%20economy>

⁶ TechRepublic, “Why the gig economy is in danger,” December 16, 2019. https://www.techrepublic.com/article/why-the-gig-economy-is-in-danger/?_amp_linker=1*ywzvop*id*VVpHM3E1dVVHbWfING9jaDljUOF1QTZwajhwVnRzWTBfd2IxeTY4TUs5RFp1Y1lqNdydzdoU-OJSbzExYOFWVw..#ftag=CAD-00-10aag7f

⁷ Monster, “The gig economy: strategies for recruiting temporary workers,” 2021, <https://hiring.monster.com/employer-resources/recruiting-strategies/talent-acquisition/the-gig-economy-in-2021-predictions-and-strategies-for-recruiting-temporary-workers/>

⁸ Gig Economy Data Hub, “What is a Gig Worker?” Gig Economy Data Hub website, <https://www.gigeconomydata.org/basics/what-gig-worker>

Contractors on the other hand, receive Form 1099 for the work they perform without being considered a direct employee. Payroll taxes are not withheld at the source for contractors who, like self-employed individuals, are required to pay their own payroll taxes.

- **Nature of Work:** Definitions of the gig economy based on the nature of work consider different characteristics of the work performed, such as scheduling, flexibility, or lack of direct oversight.

The lack of consensus on the definition means that estimates of the economic footprint of the gig economy, whether its employment or value added, also vary considerably. Private estimates suggest that between 25 and 30 percent of workers are involved in non-traditional or gig work.⁹ These numbers include individuals who use gig work both to supplement their income or as their primary source of income. Government estimates are also sizeable: According to the Bureau of Labor Statistics (BLS), alternative work arrangements represent 10.1 percent of the American workforce,¹⁰ while Federal Reserve estimates are more in line with private estimates suggesting that nearly a third of American adults are involved in the gig economy.¹¹

However, there is a growing consensus that the size of the gig economy is underestimated due

to the nature of the surveys used for the various estimates. For example, the BLS's 2017 Alternative Arrangement Survey found that the share of U.S. gig/contract workers in the U.S. workforce had declined since 2005.¹² This statistic can be misleading because the BLS survey only covers people whose sole income is generated by gig work and excludes people who use gig work to supplement their income. It also has a narrow definition of an independent contractor, excluding gig workers outside the service sector. This point is highlighted in a recent paper by researchers from the University of Maryland and the Upjohn Institute, which concluded that "our preliminary findings support concerns that household surveys like the Current Population Survey may be missing a significant amount of work activity, particularly in the form of secondary jobs, and thus may have missed a significant shift towards self-employment or non-employee work."¹³

This measurement issue is becoming an important focus for the gig economy due to its potential impact on policy making. Many experts believe that if the numbers underestimate the importance of the gig economy, policymakers might miss important policy decisions that could have significant impacts on the financial well-being of individuals involved in nontraditional work environments,¹⁴ as well as on the future of the overall economy.

⁹ Gig Economy Data Hub, "How many gig workers are there?" Gig Economy Data Hub website, <https://www.gigeconomydata.org/basics/how-many-gig-workers-are-there>

¹⁰ BLS numbers classify the workers as persons holding contingent jobs (persons who do not expect their jobs to last or who report that their jobs are temporary) and persons with alternative work arrangements. 10.1 percent only represents people with alternative work arrangements. When contingent workers added the figures increase to 13.9 percent. BLS, "Contingent and Alternative Employment Arrangements -- May 2017," June 7, 2018. <https://www.bls.gov/news.release/pdf/conemp.pdf>

¹¹ Federal Reserve, "Report on the Economic Well-Being of U.S. Households in 2019, Featuring Supplemental Data from April 2020," May 2020. <https://www.federalreserve.gov/publications/files/2019-report-economic-well-being-us-households-202005.pdf>

¹² BLS, 2018.

¹³ Katharine Abraham, Brad Hershbein and Susan Houseman, "Independent Contract and Informal Work: Preliminary Evidence on Developing Better Measures in Household Surveys," December 2018. https://www.google.com/url?sa=t&rct=j&q=&esrc=s&source=web&cd=&ved=2ahUKewilu7GjpMrxAhWRAZOJHZDBD9EQFjAAegQIAxAD&url=https%3A%2F%2Fwww.aeaweb.org%2F-conference%2F2019%2Fpreliminary%2Fpaper%2FkGEN73Ns&usg=AOvVaw14tgWFol_cl3At807YF0IA

¹⁴ Marcela Escobari and Sandy Fernandez, "Measuring American gig workers is difficult, but essential," July 2018, Brookings, <https://www.brookings.edu/blog/up-front/2018/07/19/measuring-american-gig-workers-is-difficult-but-essential/>

A CLOSER LOOK AT THE AVAILABLE DATA: GIG WORKERS:

A few data sources are helpful in terms of getting a sense of the demographic characteristics of gig workers, as well as the type and importance of income generated by gig work. The Federal Reserve’s 2021 Report on the Economic Well-Being of U.S. Households¹⁵ has some of this information. Considering specifically paid childcare, house cleaning, ride sharing, selling of goods and renting out property as gig activities, the report states that in 2020, 27 percent of people earned some money from gigs and 8 percent were regular gig workers (they spent 20 or more hours in the prior months on gigs).

The data show that the majority of gig workers used their gig work to supplement their income: 47 percent of gig workers had full-time jobs and 22 percent had part-time jobs, leaving 31 percent without a traditional job. Given these numbers, it is not unexpected to see that few relied on gigs as their primary source of income: “Since many

gig workers had other jobs, few relied on gigs as a primary source of income. Three percent of all adults (11 percent of gig workers) earned at least half of their income in the past year from gigs. Even among regular gig workers, slightly less than one-fourth earned at least half of their income in the past year from gig work.”¹⁶

A 2018 paper¹⁷ by Katharine Abraham and Susan Houseman using the Federal Reserve’s Survey of Household Economics and Decisionmaking (SHED), pools 2016 and 2017 survey results to look at the characteristics of gig workers. They found that 28.1 percent of the individuals surveyed were involved in informal work. As shown in **Figure 1-A**, this ratio is higher for younger individuals than for older individuals: Among people between ages 18 and 25, 41.3 percent generated income from gig economy, the ratio is 13.4 percent for people aged 75 and over. When divided by gender, females are slightly more involved in the gig economy compared to their male counterparts: 28.7 percent versus 27.5 percent (see **Figure 1-B**). The researchers also

Figure 1-A. Percent with Informal Work Arrangements, by Age

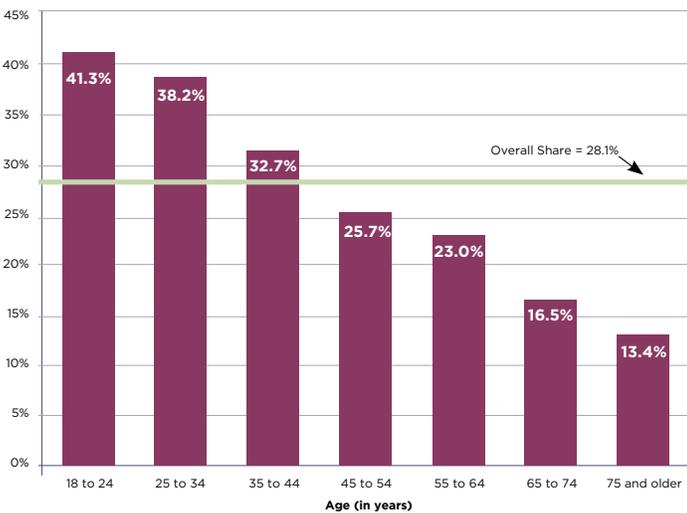
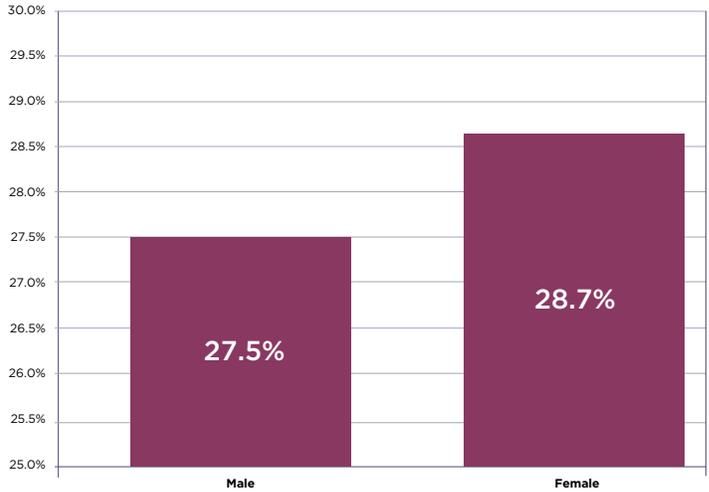


Figure 1-B. Percent with Informal Work Arrangements, by Gender



Source: Katharine Abraham and Susan Houseman, “Making Ends Meet: The Role of Informal Work in Supplementing Americans’ Income,” December 2018. Table 2a. <https://www.aeaweb.org/conference/2019/preliminary/paper/QreAaS2h>

¹⁵ Federal Reserve, “Report on the Economic Well-Being of U.S. Households in 2020,” May 2021, <https://www.federalreserve.gov/publications/2021-economic-well-being-of-us-households-in-2020-employment.htm>

¹⁶ Federal Reserve, May 2021.

Figure 1-C. Percent with Informal Work Arrangements, by Race/Ethnicity

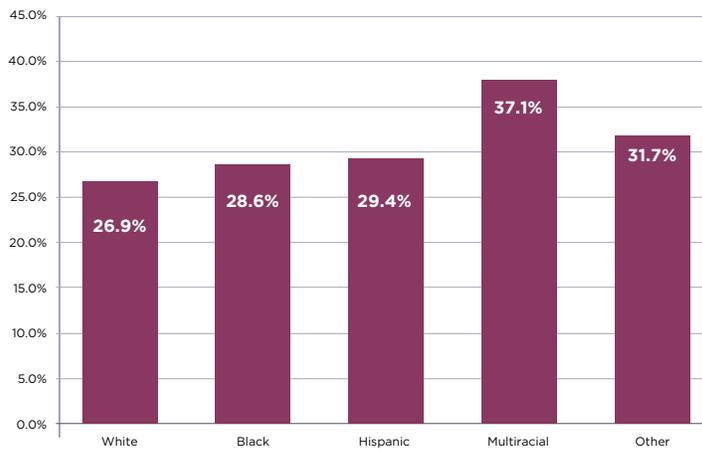
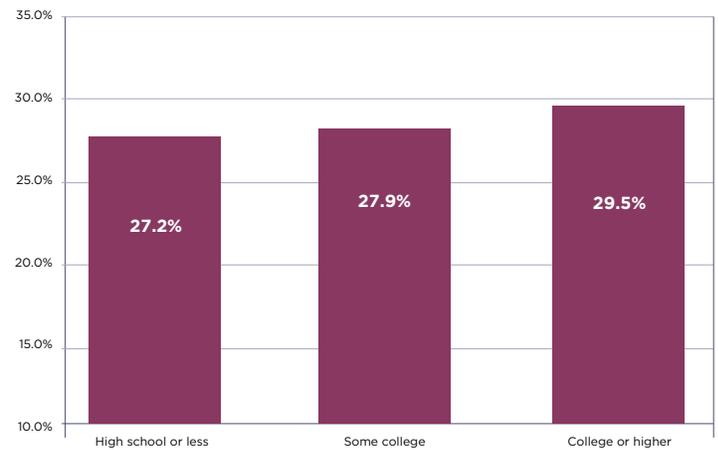


Figure 1-D. Percent with Informal Work Arrangements, by Level of Education



Source: Katharine Abraham and Susan Houseman, “Making Ends Meet: The Role of Informal Work in Supplementing Americans’ Income,” December 2018. Table 2a. <https://www.aeaweb.org/conference/2019/preliminary/paper/QreAaS2h>

provided data by race and ethnicity. **Figure 1-C** shows that Hispanic, multiracial, and other races are more involved in the gig economy than their white and black counterparts. When divided by educational attainment, participation in the gig economy rises slightly as the level of education increases (see **Figure 1-D**). However, use of gig work as the primary source of income declines with the level of education (6.1 percent for individuals with a high school diploma or less compared to 2.7 percent for individuals who completed college).

Gig Economy Data Hub, a joint project by the Aspen Institute’s Future of Work Initiative and Cornell University’s ILR School, uses the 2017 BLS survey to compare the composition of the contingent workforce with the traditional workforce.¹⁸ The BLS defines contingent workers as workers who do not have an explicit or implicit contract for continuing employment. Contingent work is temporary, lasting only for a limited time such as until completion of a given project.¹⁹ According to **Figure 2-A**, younger workers (those between ages 16 and 35) make

up a greater share of the contingent workforce than the traditional workforce. There is no difference between the two workforces when classified by gender (see **Figure 2-B**). The BLS survey has more detail on education level and type of work. **Figure 2-C** shows that a greater share of contingent workers does not have a high school degree than traditional workers. Interestingly, the share of contingent workers with at least some graduate school education is also slightly higher than for traditional workers.

Due to the nature of gig work and probably many other factors involved (like expenses accrued or motivation for the work), we do not have detailed earning data for the gig economy. There is some information based on types of non-traditional work, such as independent contractors’ earnings being similar to traditional workers and temp agency workers having lower earnings.²⁰ However, academic research has begun looking into various aspects of gig earnings using private data sources. For example, a recent paper²¹ by a group of researchers uses Uber’s records to investigate the general belief that the gig econ-

¹⁷ Figures based on data from Table 2a. Katharine Abraham and Susan Houseman, “Making Ends Meet: The Role of Informal Work in Supplementing Americans’ Income,” December 2018. <https://www.aeaweb.org/conference/2019/preliminary/paper/QreAaS2h> <https://www.merriam-webster.com/dictionary/gig%20economy>

¹⁸ Gig Economy Data Hub, “Who Participates in the Gig Economy?” <https://www.gigeconomydata.org/basics/who-participates-gig-economy>

¹⁹ It is important to note that the concepts of contingent work and alternative work arrangements are different. While a contingent worker may also be involved in an alternative work arrangement, it is not always the case.

²⁰ BLS, 2018

²¹ Cody Cook, Rebecca Diamond, Jonathan V. Hall John A. List, and Paul Oyer, “The Gender Earnings Gap in the Gig Economy: Evidence from over a Million Rideshare Drivers,” May 2020, <http://www.restud.com/wp-content/uploads/2020/11/MS26715manuscript.pdf>

omy might favor women. The paper documents that there remains a 7 percent earnings gap among male and female drivers.

The authors attribute this to three main factors:

- Experience on the platform (learning by doing)
- Preferences and constraints over where to work (driven largely by where drivers live and, to a lesser extent, safety)
- Preferences for driving speed.

The authors reach an interesting conclusion, stating that “Our results suggest that, in a “gig” economy setting with no gender discrimination and highly flexible labor markets, women’s relatively high opportunity cost of non-paid-work time and gender-based differences in preferences and constraints can sustain a gender pay gap.”²²

GIG ECONOMY: TAX ISSUES AND OTHER POLICIES FOR THE GOVERNMENT TO CONSIDER

As the economic footprint of the gig economy widens and policymakers and researchers dig deeper into various aspects of gig data, various policy issues emerge. There are two important areas of concern that may need to be addressed

by policy makers: The lack of benefits for workers in the gig economy and the tax consequences of changing work dynamics.

- **Gig Economy Protections and Employer Provided Benefits:** Employer-based benefits, like health insurance and retirement plans, are very important for the financial wellness of many traditional workers. Unfortunately, many jobs associated with the gig economy do not provide these important benefits. According to recent research by Prudential Financial, over half of gig-only workers do not have access to employer-based benefits, “leaving them vulnerable to the key financial risks of premature death in family, disability, or critical illness.”²³ Another important issue is the lack of access to a systematic savings program for gig workers, endangering their financial wellbeing in retirement. According to the same research, significantly fewer gig-only workers have assets in employer-sponsored retirement plans (16 percent) compared to traditional workers (52 percent).

In addition to the lack of employer-provided benefits discussed above, many labor protections, such as minimum wages and overtime provisions, provided by federal and state law to wage and salary workers are not available

Figure 2-A. Composition of Contingent and Traditional Workforces, by Age

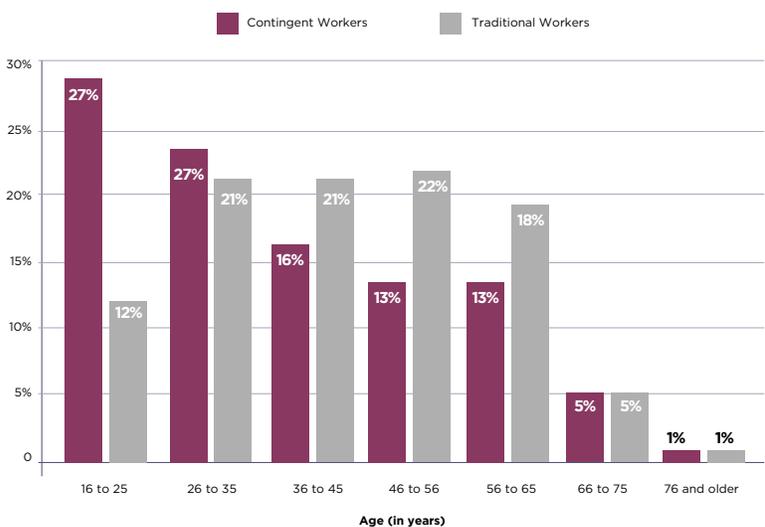
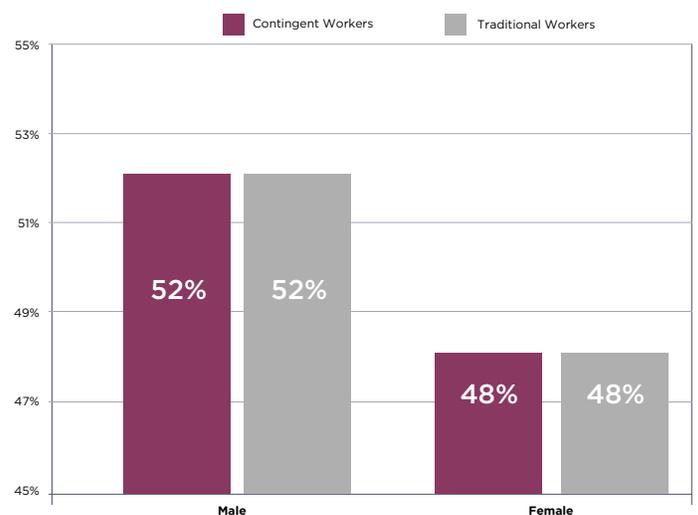


Figure 2-B. Composition of Contingent and Traditional Workforces, by Gender

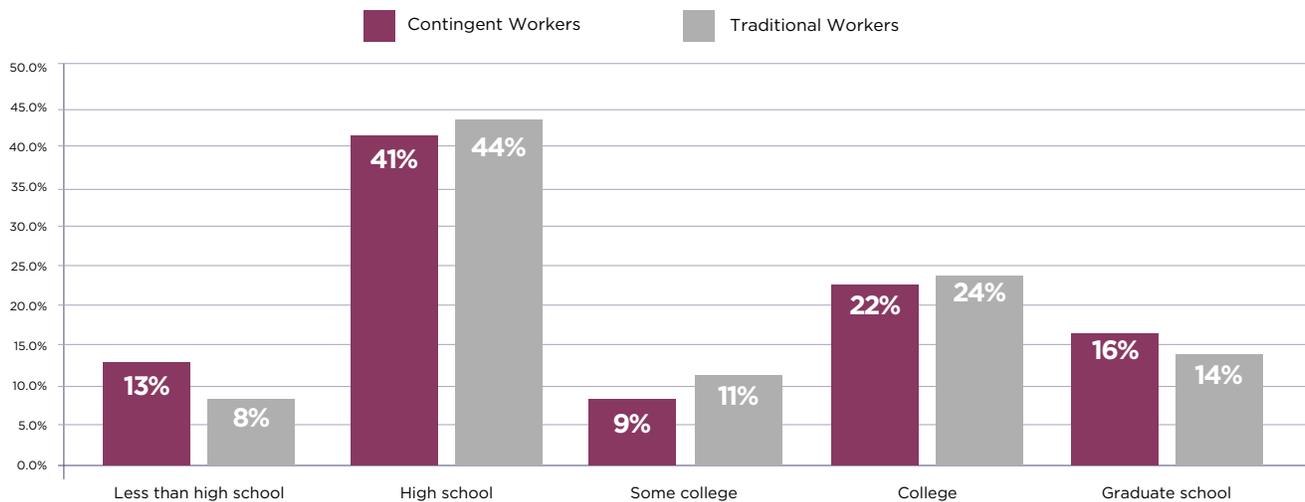


Source: Gig Economy Data Hub, Who participates in the gig economy? <https://www.gigeconomydata.org/blog/new-interactive-data-tools-added-gig-economy-data-hub>

²² Cook et al. (2020)

²³ Prudential Financial, “Gig Workers in America,” 2019, pg 2. <https://www.prudential.com/wps/wcm/connect/4c7de648-54fb-4ba7-98de-9f0ce03810e8/gig-workers-in-america.pdf?MOD=AJPERES&CVID=mD-yCXo>

Figure 2-C. Composition of Contingent and Traditional Workforces, by Education



Source: Gig Economy Data Hub, Who participates in the gig economy? <https://www.gigeconomydata.org/blog/new-interactive-data-tools-added-gig-economy-data-hub>

for gig workers. The same is true for unemployment compensation that is financed by the taxes paid by businesses. However, during the pandemic, the Department of Labor stated that gig workers qualify as “unemployed” under the Pandemic Unemployment Assistance when they lose a significant amount of income due to Covid-19. Given the worldwide attention gig workers are garnering, some of these policies might evolve and become a permanent fixture. However, the issue becomes who will finance these social protections for gig workers, and how?²⁴

On the benefits side, there is an increased interest in creating and increasing portable benefits. The Affordable Care Act (ACA), passed in 2010, provides health insurance for self-employed through the individual health insurance marketplace. Some private firms, like Prudential, launched web-based tools to help individuals to purchase insurance products. Individual Retirement Accounts (IRA) are also a good option for gig workers to accumulate savings for their retirement. However, inertia is a big handicap for gig workers to self-start these accounts, creating a

missed opportunity to take advantage of the time value of money.²⁵

- **Tax Administration and Gig Economy:** The rise of the gig economy has important implications for both an individual’s management of his/her taxes and the government’s tax administration.
- *Gig Workers:* On the individual side, tax filing requires somewhat more involvement of the taxpayer under gig economy: For many gig workers, income taxes are not withheld by employers, which may require additional time spent on quarterly tax payments or lead to surprise tax bills at the end of the year. Freelancers are also responsible for the payroll taxes that are normally paid by the employer. If the individuals are expected to owe at least \$1,000 in taxes (factoring in both income and self-employment taxes minus any refundable credits they are entitled), they are required to make quarterly tax payments. However, a younger and financially less experienced workforce (as described above) translates into a minimal knowledge of tax

²⁴ Sarah A. Donovan, David H. Bradley and Jon O. Shimabukuro, “What Does the Gig Economy Mean for Workers?” February 2016, Congressional Research Service, <https://fas.org/sgp/crs/misc/R44365.pdf>

²⁵ For discussion regarding the behavioral aspects of retirement savings, see Pinar Cebi Wilber, “DOL’s Retirement Advice Rule: Helping or Harming Sound-Retirement Planning?” November 2015, <https://accf.ftlbcn.net/wp-content/uploads/2016/08/DOL-fiduciary-rule-FINAL.pdf>

rules. In fact, a survey conducted by Professor Bruckner highlights this specific point: “Our survey revealed that among respondents who had earned income working with an on-demand platform company in 2015, 34% did not know whether they were required to file quarterly-estimated payments with the IRS on that income.”²⁶

Depending on the type of work, gig workers could incur additional costs associated with their job, such as vehicle mileages, computers, and expenses associated with rentals. The cost of these items can be classified as a business expense and will again have tax consequences. However, the rules associated with what counts as a business versus personal expense is also complicated. In some cases, this leads to improper reporting. Individuals need to carefully keep track of their expenses for an accurate year-end accounting.²⁷

Another issue highlighted by the Government Accountability Office (GAO) is the difficulty associated with estimating one’s taxes when their income and expenses are unstable, as is the case for gig workers: “Because earnings of some platform workers may be low and earnings and expenses may fluctuate, they can have difficulty estimating their taxes owed and setting aside money to pay the taxes.”²⁸ This could lead to “risk of falling into a cycle of noncompliance.”²⁹

- *Tax Administration:* In the U.S., tax reporting and collection is based on a voluntary compliance system, whereby taxpayers prepare and file their annual tax returns on their own or with the help of a tax preparer. They are responsible for reporting all their income, as described by the law, and make the allowable adjustments based on specific criteria (such as marital status, number of children, age, etc.) to take advantage of tax incentives provided by the Internal Revenue Code. These tax incentives have been used as a means to achieve certain social and economic policy goals, which makes the tax code more complex and tax filing more of an individual affair based on one’s knowledge of their own personal details.

Despite the complexity of the U.S. tax code, the overall voluntary compliance rate was at 84 percent for tax years 2011-2013. The voluntary tax compliance rate for the individual income tax was 78 percent for the same period.³⁰ It is hard to achieve 100 percent compliance, but governments around the world are continuously looking for ways to improve tax administration. For example, the current U.S. Administration has been paying specific attention to the tax gap, the difference between the true tax liability for a given tax year and the amount that is paid.³¹ According to the most recent estimates, for tax years 2011-2013, the gross tax gap associated with the individual income tax was \$314 billion and

²⁶ Carol Bruckner, “Shortchanged: The Tax Compliance Challenges of Small Business Operators Driving the On-Demand Platform Economy,” June 2016, Kogod Tax Policy Center, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2784243, pg 11.

²⁷ H&R Block, “The Six Most Common Tax Problems For Gig Economy Workers,” <https://www.hrblock.com/tax-center/irs/audits-and-tax-notice/tax-problems-for-gig-economy-workers/>

²⁸ GAO, “Tax Compliance: More Income Reporting Needed for Taxpayers Working Through Online Platforms,” May 2020, <https://www.gao.gov/assets/gao-20-366.pdf>

²⁹ Ibid.

³⁰ IRS, “Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2011-2013,” Sept. 2019, Table 3. <https://www.irs.gov/pub/irs-pdf/p1415.pdf>

³¹ For a detailed discussion of type of tax gaps and statistics, please see Pinar Cebi Wilber, “Internal Revenue Service: Increasing Workload Under Strained Budgets,” May 2021, ACCF, https://accf.ftlbcn.net/wp-content/uploads/2021/05/ACCF_IRS_Report_051221V3.pdf

³² IRS, “Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2011-2013,” September 2019. <https://www.irs.gov/pub/irs-pdf/p1415.pdf>

net tax gap was \$271 billion. The portion of the annual tax gap due to underreported self-employment income amounts to \$45 billion for tax years 2011-2013.³²

As the gig economy continues to expand, underreporting of self-employment may become a bigger issue. As shown in prior work,³³ information reporting increases tax compliance, but up until this year, Treasury Regulations did not require certain gig economy businesses to issue Form 1099-K (Payment Card and ThirdParty Network Transactions) to report payments to each payee if workers earned less than \$20,000 and engaged in less than 200 transactions annually. However, the American Rescue Plan Act of 2021, passed in March, reduces the Form 1099-K reporting threshold to \$600 regardless of the number of transactions. This provision will take effect next year and is expected to raise \$8.8 billion of tax revenue between 2022 and 2031.³⁴ But, not everyone receives their information through 1099-K and this has ramifications both for workers who do not get earning reports (making tax filing more difficult and increasing the risk of mistakes) and the IRS (making enforcement of the tax rules more difficult).

Whether it is self-employment or other taxes, “completely closing the tax gap is not feasible, as it would entail more intru-

sive enforcement and more burdensome recordkeeping or reporting than the public is willing to accept, and more resources than IRS is able to commit.”³⁵ However, decreasing the tax gap in an efficient manner may be difficult under the IRS’s current budget: The Agency has faced an increased workload with funding that has changed very little over the years. According to some estimates, its budget has fallen by 20 percent in inflation adjusted dollars since 2010, resulting in the elimination of 22 percent of its staff. In addition to other duties, in line with budget cuts, the chances of being audited has decreased, increasing the tax gap and reducing the revenue collected by the agency.³⁶ IRS funding has been the focus of recent Congressional discussions with no resolution at the time of writing of this short report.³⁷

There is also another important issue attached to underpayment of income and self-employment taxes: the potential negative impact on efforts to fund Social Security. This could mean potentially lower Social Security benefits for these workers upon retirement, according to research by Professor Bruckner and Dr. Hungerford.³⁸ Adding this to the lack of other benefits associated with traditional employment, such as health insurance and access to workplace retirement accounts, could spell trouble for the financial well-being of individuals who earn their primary income

³³ Pinar Cebi Wilber, “Internal Revenue Service: Increasing Workload Under Strained Budgets,” May 2021, ACCF, https://accf.ftlbcnd.net/wp-content/uploads/2021/05/ACCF_IRS_Report_051221V3.pdf

³⁴ Baker Institute Blog, “Recent changes to sharing economy tax reporting,” May 25, 2021. <https://blog.bakerinstitute.org/2021/05/25/recent-changes-sharing-economy-tax-reporting/>

³⁵ James R. McTigue, Jr., “Tax Gap: Multiple Strategies Are Needed to Reduce Noncompliance,” Testimony Before the Committee on Ways and Means, House of Representatives, May 9, 2019, GAO, <https://www.gao.gov/assets/gao-19-558t.pdf>

³⁶ For a detailed discussion, see Pinar Cebi Wilber, 2021.

³⁷ Yahoo Finance, “A ‘no-brainer’: Why Democrats will keep pushing for increased IRS funding,” July 21, 2021. https://finance.yahoo.com/news/democrats-will-keep-pushing-for-increased-irs-funding-150401793.html?guccounter=1&guce_referrer=aHR0cHM6Ly93d-3cuZ29vZ2xlMnVbS8&guce_referrer_sig=AQAAAEYdK2t4DU4zS8ZfuYkO3l4POjNLUw5oipsCuMM1kSxQaFvB1rflCxz0mIE_ufA9z-slf80WoRUMpeF9DChx6j_j9tb-ULCKjBcU2prT6LWwwsmD8HzCOXqj120kvrwbkA8EDOcDv4E3tAjz3fEz6iZ7cnliSrxqTlwwLLe8lSoct

³⁸ Caroline Bruckner and Thomas L. Hungerford, “Failure to Contribute: An Estimate of the Consequences of Non- and Underpayment of Self-Employment Taxes by Independent Contractors and On-Demand Workers on Social Security,” January 2019, Center for Retirement Research Boston College. https://crr.bc.edu/wp-content/uploads/2019/01/wp_2019-1.pdf

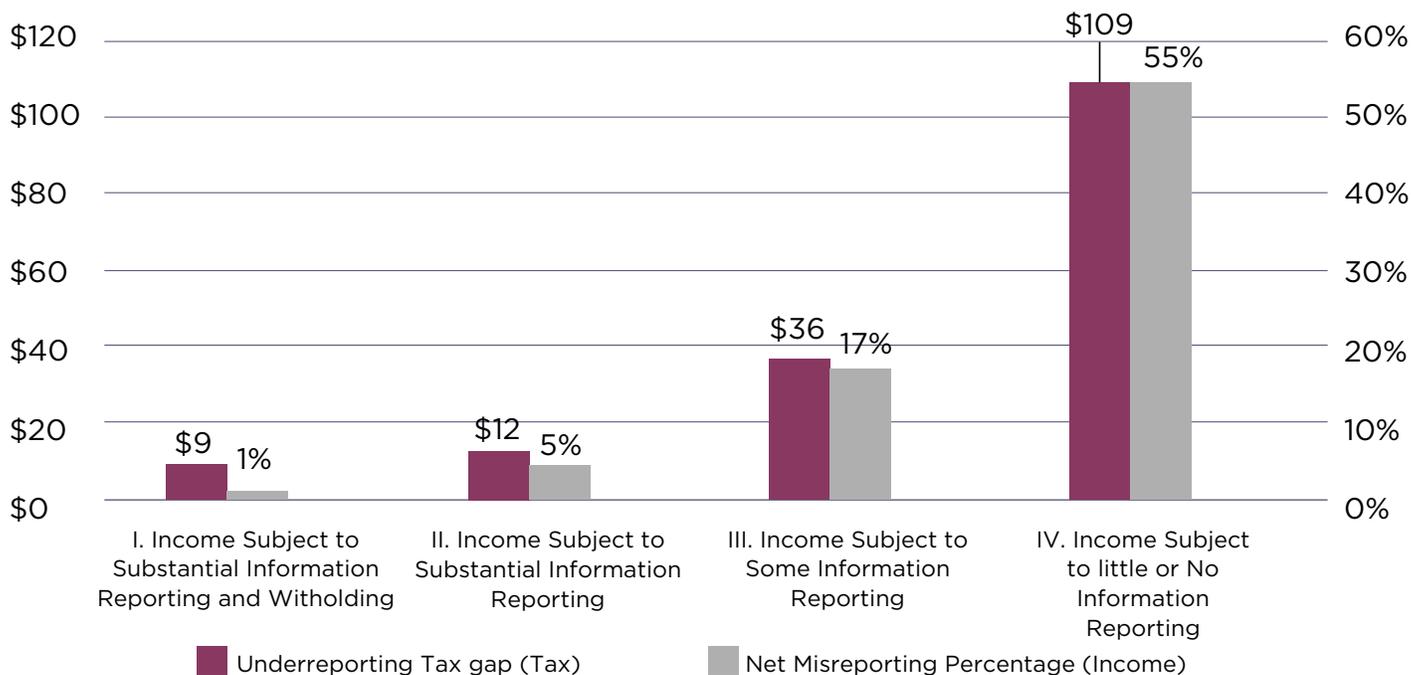
from the gig economy and a potentially greater burden for government to support these individuals.

- On-Going Work/Policy Recommendations to Improve Tax Compliance for Gig Workers:** As the problems outlined above grow, there has been a growing body of research and policy suggestions for addressing different parts of the problem. The IRS has also been proactive in offering tools to help gig workers with their tax filing. For example, in February 2020, it launched the Gig Economy Tax Center, a website to inform/guide workers and businesses on gig economy-related tax issues.³⁹ The website, in part, is a response to 2019 recommendations by the Treasury Inspector General for Tax Administration (TIGTA) to accomplish two goals:⁴⁰ (1) Raising awareness

about federal tax obligations and (2) easing the tax burden by identifying improvements to instructions, guidance, or forms that platform workers are likely to use.

TIGTA has also been studying the issue of self-employment tax compliance and, in 2019, released a report with 11 recommendations for the IRS, including improvements in tax administration for the gig economy (assessment and collection of self-employment tax), improvements to the Automated Underreporter System to effectively evaluate and catch non-compliance geared towards self-employment taxes, and working with the Treasury’s Office of Tax Policy to pursue regulatory or legislative changes to third-party reporting thresholds.⁴¹

Figure 3. Effect of Information Reporting on Individual Income Tax Reporting Compliance (Tax Year 2011-2013)



Notes: I. includes wages and salaries, II. includes pensions and annuities, unemployment compensation, dividend income, interest income, taxable social security benefits, III. includes partnership/S.corp income, capital gains, alimony income, and IV. includes nonfarm proprietor income, other income, rents and royalties, farm income, and income from Form 4797.

Source: IRS, “Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2011–2013,” September 2019. <https://www.irs.gov/pub/irs-pdf/p1415.pdf>

³⁹ The website is: <https://www.irs.gov/businesses/gig-economy-tax-center>

⁴⁰ GAO, “Tax Compliance: More Income Reporting Needed for Taxpayers Working Through Online Platforms,” May 2020, <https://www.gao.gov/assets/gao-20-366.pdf>

⁴¹ TIGTA, “Expansion of the Gig Economy Warrants Focus on Improving Self-Employment Tax Compliance,” February 14 2019. <https://www.treasury.gov/tigta/auditreports/2019reports/201930016fr.pdf>

Table 1. Forms 1099-K Issuances Using Various Reporting Requirements for Three Gig Economy Platf

	Number of Forms	Total Amount
Actual Forms 1099-K Issued	2,401,813	\$10,738,487,079
\$20,000 Reporting Threshold	130,682	\$4,898,548,602
\$600 Reporting Threshold	1,471,289	\$10,547,421,534

Source: TIGTA, “Expansion of the Gig Economy Warrants Focus on Improving Self-Employment Tax Compliance,” February 14, 2019. <https://www.treasury.gov/tigta/auditreports/2019reports/201930016fr.pdf>

The reporting threshold requirements have been at the center of a number of policy proposals, given their impact on compliance. According to **Figure 3**, tax compliance is positively impacted by third-party information reporting. When information is combined with tax withholding (as is the case for wages and salaries) compliance is the highest. The net misreporting percentage is the highest for income subject to little or no information reporting, at 55 percent with a corresponding tax gap of \$109 billion.

The TIGTA report gives the information reporting history of just three gig economy platform companies that did not strictly follow the \$20,000 reporting threshold, to highlight the importance of reporting for the gig economy. **Table 1** shows how many 1099-K forms were issued and how many would have been issued if they had followed the threshold guidelines at the time. For tax year 2016, these three companies filed 2.4 million 1099-K forms covering close to \$11 billion of income. If they strictly followed the reporting requirements of \$20,000, they would only have issued 130,682 forms corresponding to less than \$5 billion of income. If they had only filed for workers with \$600 of income, they would have filed just 1.5 mil-

lion forms covering \$10.5 billion dollars of income. As highlighted before, recent changes in the law regarding the 1099-K reporting threshold should improve the situation.

Like other government Agencies, the GAO put forth recommendations to improve tax compliance for gig workers.⁴² In addition to increased information reporting, some policy suggestions highlighted in the report are:

- Withhold estimated taxes owed (implement voluntary withholding)
- Simplify process for platform workers by:
 - Creating a standard business deduction
 - Require platform companies to inform workers of tax obligations
 - Require platform companies to provide expense information
 - Make electronic delivery of Forms 1099 the default

Creating a standard business deduction for workers could simplify the complexities associated with keeping track of business expenses described above and make com-

⁴² GAO, “Tax Compliance: More Income Reporting Needed for Taxpayers Working Through Online Platforms,” May 2020, <https://www.gao.gov/assets/gao-20-366.pdf>

⁴³ See *supra* note 38.



pliance easier, especially for financially inexperienced workers.

Other researchers have put forth similar policy recommendations. Bruckner and Hungerford (2019), for example, suggests “modernizing information reporting, updating timing requirements for estimated payments, and developing distribution information on the tax requirements for independent contractors and on-demand economy workers on the payment of self-employment taxes.”⁴³

There are also calls at the state level for more fundamental changes to reclassify gig workers and treat them as traditional employees with requirements to withhold taxes similar to W-2 workers. All these suggestions have a potential for increased costs on gig economy businesses and it is important to consider how changing the rules might impact the wages and employment of gig workers.

CONCLUSION:

The evolution of the gig economy, with rapidly improving technology, is having wide-ranging impacts on the global economy and these impacts are expected to grow and potentially reshape the labor markets. These changes also require new policy making to address emerging issues especially in the tax administration arena. Taking both advantages and disadvantages into consideration, government policies could be tweaked to help deal with these issues in a cost-effective manner before they turn into significant problems. But the first step should be a consistent definition and reliable measurement of the size of the gig economy and its active participants. This should provide a good starting point for tax administration. The next steps should make tax filing easier for gig workers to increase tax compliance and lower the tax gap in order to help finance policy priorities without further burdening taxpayers.



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