

## Transparency in Revenue Estimating

By Thomas F. Field

Thomas F. Field is the founder of Tax Analysts, a nonprofit publisher located in Arlington, Virginia. For more than 30 years, Tax Analysts has played a prominent role in litigating disclosure questions relating to tax information.

In this article, Field reviews current transparency practices at the three federal agencies that produce revenue estimates. He concludes that the U.S. Treasury Department is very secretive with respect to its revenue estimates, that the Congressional Budget Office is quite transparent, and that the Joint Committee on Taxation occupies a middle ground.

Field then reviews the arguments for and against greater transparency in the revenue estimating process. He also examines state and international estimating practices to see if they provide any guidance about the appropriate degree of transparency for revenue estimates. At the conclusion of the article, he advances a set of proposals to improve the transparency of the federal estimating process.

This article is based on interviews with scores of individuals both in and outside of government. Most asked not to be identified, but Field wishes to thank each of them for their assistance. Their comments helped to correct errors and substantially improved the recommendations. Thanks to these comments, this article has truly become a collective effort by dozens of individuals who share a common interest in the improvement of the estimating process. The article's errors, however, remain Field's own.

This article is part of an ongoing series of articles in *Tax Notes* on the revenue estimating process. The series was funded by a consortium of sponsors headed by the Lone Star and Heritage Foundations. For an introduction to the series, see *Tax Notes*, Nov. 22, 2004, p. 1141.

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### I. The Current Situation

Revenue estimates state the changes in expected revenues associated with changes in the tax law. Thirty years ago, they were an afterthought in the process of formulating tax policy. Today, because of a series of laws designed to contain federal spending,<sup>1</sup> revenue estimates occupy center stage — the numbers can make or break otherwise worthy tax initiatives.

Meanwhile, there have been some very significant improvements in revenue estimating techniques.<sup>2</sup> As a result, revenue estimators are better positioned today to produce both dynamic scores that take into account economic feedback effects and improved distributional estimates that show the effect of tax changes by income

<sup>1</sup>The relevant spending legislation, enacted starting in 1974, required revenue neutrality for tax legislation and imposed annual caps on discretionary spending. Revenue estimates played a crucial role in calculating the tax-revenue neutrality required by the acts. The most important of those statutes were the Congressional Budget and Impoundment Control Act of 1974, P.L. 93-344, 88 Stat. 297; the Balanced Budget and Emergency Deficit Control Act of 1985, P.L. 99-177, 99 Stat. 1038 (commonly known as the Gramm-Rudman-Hollings Act); and the Budget Enforcement Act of 1990, P.L. 101-508, Title XIII, 104 Stat. 1388-573 (1990).

<sup>2</sup>The congressional Joint Committee on Taxation (JCT), after careful study, has produced revenue estimates that successfully take into account the feedback effects of major tax proposals on budget aggregates (dynamic scoring). Also, the Treasury Department has made significant improvements in the distributional analysis of tax proposals (although, regrettably, it has not made much use of those improvements). These developments are discussed later in this report.

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class. Other changes include the use of linked spreadsheets, more powerful computers, and multiyear tax models using longitudinal data.

Despite those developments, the revenue estimating process is nearly as much a mystery today as it was when estimates were much less important policy desiderata. Now and then a ray of sunshine gets thrown on the estimating process, but in general it remains shrouded in secrecy.

This report examines the pros and cons of that ongoing secrecy and concludes that it is time to consider some modest changes that, on balance, will make the estimating process more transparent. Enhanced transparency, in turn, should make it possible to address other revenue estimating issues that demand attention.<sup>3</sup>

### A. Transparency Differences Between Agencies

The staffs of three federal agencies prepare revenue estimates on a regular basis. They are, specifically:

- **The OTA Staff.** The revenue estimating staff in the Office of Tax Analysis (OTA) in the U.S. Treasury Department<sup>4</sup> has about 13 financial economists who are supported by a separate 8-person modeling and computer applications staff.<sup>5</sup> Also, OTA's individual, business, and international staffs assist with revenue estimates in their areas of expertise.
- **The JCT Staff.** The revenue estimating staff of the congressional Joint Committee on Taxation (JCT)<sup>6</sup>

<sup>3</sup>Those issues include dynamic scoring (discussed in a separate article in this series); the truncation of the estimating time horizon (by restricting estimates to periods of 5 or 10 years), which makes it difficult to deal with issues such as retirement savings and depreciation; the possibility of using accrual and present-value accounting when making estimates; the need to account for the interest costs associated with tax changes; and questions relating to probabilistic scoring. Another issue requiring attention relates to sensitivity analysis and the provision of range estimates in addition to point estimates. As a leading private-sector estimator put it, "I would gladly trade off knowing the gory details of an estimating model for a sense of the professional judgments about the reasonable range of possibilities around an estimate." Cost benefit analysis and inclusion of compliance costs in revenue estimates also require consideration. In the words of another private-sector economist, "If Treasury and JCT provided a benefit/cost analysis, including compliance costs, in their estimates, then the economists on the revenue estimating staffs would be used to their fullest potential and public policy would be debated on the basis of more complete information. I would be willing to exchange 1000 simple revenue estimates," he continued, "for 20 good benefit/cost analyses of existing and proposed tax provisions."

<sup>4</sup>A description of Treasury's Office of Tax Analysis is available on the Web at <http://www.treas.gov/offices/tax-policy/offices/ota.shtml>.

<sup>5</sup>Names and phone numbers for the Treasury revenue estimating staff appear in Chart 2134 of *The Tax Directory* (Arlington, Va.: Tax Analysts, updated quarterly).

<sup>6</sup>A description of the "Joint Committee Revenue Estimation Process" appears on the Web at <http://www.house.gov/jct/revhist.htm>.

has about 16 economists and senior economists, as well as 5 supporting statistical and computer specialists.<sup>7</sup>

- **The CBO Staff.** The Budget Analysis Division in the Congressional Budget Office (CBO) has about 45 analysts in four operating units who prepare spending projections and cost estimates for legislation. Also, the CBO's Tax Analysis Division has about 11 tax analysts, as well as managers and supporting staff, who estimate future tax receipts and prepare studies of the U.S. tax structure.<sup>8</sup>

Although there are three revenue estimating staffs, only two estimates are typically prepared for a given tax proposal: one by Treasury and the other by either the JCT or the CBO. As explained in more detail later in this report, revenue estimates from the JCT relate to individual and corporate income taxes, Social Security and Medicare taxes, estate and gift taxes, and excise taxes. CBO revenue estimates relate to tariffs, offsets, and user charges.

OTA and JCT (or CBO) revenue estimates become important at different stages of the legislative process. Treasury estimates matter when the president's budget is being prepared or when a tax proposal is being readied by Treasury for submission to Congress. Later, during the consideration of a tax bill, JCT estimates become critical, especially if the taxwriting committees are required to hit congressionally mandated budget targets. Still later, if Treasury recommends a veto, Treasury estimates will be used to advise the president.

Regarding estimating transparency, there are some important differences between the OTA, the JCT, and the CBO. Of the three, the CBO is the most willing to make information public regarding its revenue estimating methods. The reasons for that are discussed later in this report.

In contrast, the OTA staff at Treasury is very secretive. As one former senior economist in the current Bush administration observed of the Treasury staff, "They are discouragingly nontransparent even to folks within Treasury."

Similar comments abound on Capitol Hill regarding the JCT estimating staff. However, the JCT staff has been consistently more open than Treasury in some significant ways that will be described below.

### B. What Does Transparency Mean?

This report focuses primarily on the technical process of preparing revenue estimates by assembling data and making assumptions and calculations at the staff level. It focuses only secondarily on the process by which staff estimates are reviewed and sometimes changed by senior staff and political officials.

<sup>7</sup>See Chart 1450 in *The Tax Directory*, *supra* note 5.

<sup>8</sup>See Chart 1750 in *The Tax Directory*, *supra* note 5. A description of the CBO's staff and organization is available on the Web at <http://www.cbo.gov/Organization.cfm>; the mission of the CBO is described at <http://www.cbo.gov/Mission.cfm>; and a description of "CBO's Policies for Preparing and Distributing Its Estimates and Analyses" appears at <http://www.cbo.gov/Policies.cfm>.

Transparency in the technical revenue estimating process at the staff level means different things to different people. Depending on how transparency is defined, individuals can easily find themselves on opposite sides of the debate over whether greater transparency is a good idea.

The following are some of the possible components of the transparency concept as applied to the revenue estimates prepared by federal agencies:

### Generalized Transparency

1. Publication of written explanations describing how, in general, an agency prepares revenue estimates. Variations on this theme include publishing focused explanations relating to specific topics such as capital gains estimating methods.

2. Sponsorship of occasional conferences or seminars at which revenue estimators describe their work, provide illustrations, and solicit comments from peers.

3. Publication of source data — such as the IRS *Statistics of Income*<sup>9</sup> or the IRS tax return “public-use file” — that can be used by private organizations to make their own revenue estimates.

4. Publication of retrospective analyses of the accuracy of prior revenue estimates in the limited instances<sup>10</sup> in which that is possible.

### Specific Transparency

5. Preparation and release of written explanations describing how a specific revenue estimate was done.

6. Release of the assumptions that were made by an estimator when doing a specific revenue estimate, including the behavioral assumptions (that is, expected changes in taxpayer behavior resulting from a change in taxation).

7. Listing of the sources of data that were used in making a specific revenue estimate, including any links to publicly available data.

8. Description of the spreadsheets or simulation models used in doing a specific estimate, including any use of specialized software.

<sup>9</sup>Publication of the IRS Statistics of Income is authorized by Internal Revenue Code section 6108(a).

<sup>10</sup>A 1991 article by Emil M. Sunley, a former deputy assistant secretary for tax policy at Treasury, and Randall D. Weiss, a former deputy chief of staff at the JCT, warns that “there are severe limitations on the ability of anyone to make an *ex post* judgment on the accuracy of [revenue] estimates.” However, the article also states that “although most estimates probably cannot be checked easily, some can.” See Emil M. Sunley and Randall D. Weiss, “The Revenue Estimating Process,” *Tax Notes*, June 10, 1991, p. 1298 at 1306. The Sunley-Weiss article also appeared in *American Journal of Tax Policy*, vol. X, no. 2 (Fall 1992).

On May 18, 1995, in letters to the chairs of the House Ways and Means Committee and Senate Finance Committee, JCT Chief of Staff Kenneth J. Kies stated that the JCT would begin to undertake retrospective analyses of revenue estimates in selected cases. See the discussion in the text accompanying note 50 *infra* regarding the Joint Committee’s transparency efforts, and *Doc 95-5074*, 95 TNT 98-25 (Ways and Means Committee letter) and *Doc 95-5075*, 95 TNT 98-26 (Finance Committee letter).

9. Release of the spreadsheet or computer simulation model output files underlying a specific revenue estimate, preferably in electronic form, and any off-model adjustments made to the output files.

10. Release of the nonprivileged elements of the simulation models themselves.

11. Release of the actual data used in making a specific revenue estimate to the extent that this can be done without jeopardizing taxpayer privacy or business confidentiality.

Which of those components we include in our definition of transparency depends on our goals. If the goal is to permit “accuracy checking” through full replication and validation of a specific revenue estimate, our definition of transparency should include all 11 of those general and specific components. If, in contrast, the goal is to acquire a general understanding of how revenue estimates are done, the components listed under “Generalized Transparency” are sufficient.

The goals of most requests for revenue estimating transparency fall between those two extremes. For some individuals, it is sufficient to know how estimates are prepared and to be assured that the estimates are honest and reliable. For them, generalized transparency is usually adequate. But for scholars, researchers, and tax professionals, more than generalized disclosure is needed, and at least some of the components of “Specific Transparency” should be made available to those individuals.

### C. Sources of Transparency Guidance

Revenue estimates are related more or less directly to several other types of government forecasts. While each type of forecast can be distinguished from the others, transparency practices developed for one type are often instructive when determining the degree of transparency that is appropriate for other types. Accordingly, this report considers the transparency practices that apply to all of the following forecasts:

- **Baseline receipts estimates.** Baseline receipts estimates indicate the expected revenues under current law for a specified time period, such as 5 or 10 years.
- **Baseline economic estimates.** Baseline economic estimates forecast major economic variables, including gross domestic product, unemployment, inflation, and interest rates, for a specified time period.
- **Distributional estimates.** Distributional estimates, such as those prepared by the Treasury and JCT revenue estimating staffs, indicate the financial effect, by income class, of changes in the tax laws.<sup>11</sup>
- **Cost estimates.** Cost estimates, such as those prepared by the CBO and Office of Management and Budget, project the fiscal effects of spending bills.

<sup>11</sup>For an overview of distributional analysis at Treasury, the JCT, and the CBO, see David F. Bradford, ed., *The Distributional Analysis of Tax Policy* (Washington, D.C.: American Enterprise Institute Press, 1995). For an update of the Bradford book’s account of Treasury distributional practices, see *OTA Paper 85*, described in the text on p. 333, *infra*.



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- **Revenue estimates.** Revenue estimates (the subject of this report) are forecasts indicating the expected change in tax payments resulting from a change in the tax law.

One must be cautious, however, when applying transparency practices developed in one of these forecasting areas to other types of forecasts or estimates. Baseline estimates, for example, are few in number and attract considerable public interest. In contrast, thousands of cost and revenue estimates are prepared each year, and the public is generally interested in only a few of them. That makes it important to think in cost benefit terms about the amount of detail to be provided when making cost or revenue estimates public. In-depth documentation is appropriate for baseline estimates, but run-of-the-mill revenue estimates ordinarily demand only brief explanations.

Nevertheless, if one keeps that caveat in mind, there are useful lessons to be learned for the revenue estimating process from studying transparency practices in all the areas listed above.

#### D. The Transparency Situation Today

No matter how transparency is defined, reliable, official information about the U.S. Treasury revenue estimating process is insufficient to provide even a rudimentary understanding of that process.

In contrast, since 1990 the JCT has published a series of documents describing its revenue estimating procedures, has held several revenue estimating conferences open to private-sector invitees, and has established an advisory panel of private revenue estimating experts. In almost all cases, however, the technical foundations for specific JCT estimates remain shrouded in secrecy.

Meanwhile, thanks to a congressional disclosure mandate,<sup>12</sup> CBO estimators are relatively open regarding the basis for their baseline and cost estimates, and the staff in

general has an accepting attitude toward public disclosure. But, although it is clearly better than the JCT or Treasury when it comes to transparency, according to professional observers the CBO is definitely not laying out all the details that underlie its forecasts.

**1. The Treasury staff.** Treasury has published almost nothing that officially describes its revenue estimating procedures. However, Treasury economists familiar with revenue estimating issues have created a fairly significant body of unofficial, scholarly revenue estimating research over the years, some of it written after the authors left Treasury for other employment.<sup>13</sup>

About 15 years ago, the Treasury revenue estimating staff compiled an internal document known as the "Revenue Estimating Handbook," a loose-leaf compilation of documents designed to introduce newly hired employees to their work.<sup>14</sup> The handbook was never published or released to the public. Nor has it been updated.

As a result, the estimating staff today uses a 13-year-old article from *Tax Notes* magazine as an introduction to the revenue estimating process for newly hired staff. The article, entitled "The Revenue Estimating Process" was authored by Emil M. Sunley, a former deputy assistant secretary for tax policy at Treasury, and Randall D. Weiss, a former deputy chief of staff of the JCT.<sup>15</sup> By the time their article was written, both had entered the private sector.

Although Treasury has not published an official description of its revenue estimating process, it has released an excerpt from its internal revenue estimating "briefing

<sup>12</sup>The Congressional Budget and Impoundment Control Act, *supra* note 1, directs the CBO to prepare "for each bill or resolution of a public character reported by any committee of the House of Representatives or the Senate . . . an estimate of the costs which would be incurred in carrying out such bill or resolution . . . together with the basis for each such estimate." See 2 U.S.C. section 653 (emphasis added). The CBO interprets the italicized words to require disclosure of both the "critical assumptions" and the "analytic methodologies" used to prepare its estimates. (The quoted phrases appear in the disclosure discussion under "CBO's Statutory Responsibilities" in "CBO's Policies for Preparing and Distributing Its Estimates and Analyses" at <http://www.cbo.gov/Policies.cfm>). A similar disclosure mandate is set forth in the Unfunded Mandates Reform Act of 1995, P.L. 104-4, 109 Stat. 48.

The applicable legislation also mandates broad public disclosure of data obtained by the CBO from other agencies, including executive branch departments and congressional agencies such as the Government Accountability Office (formerly U.S. General Accounting Office) and the Comptroller General. That disclosure directive is codified as 2 U.S.C. section 603, subsection (a) of which provides as follows: "Except as provided in subsections (c), (d), and (e) of this section [relating to data exempted from disclosure on national defense and other grounds], the Director shall make all information, data, estimates, and statistics obtained under section 601(d) and (e) of

(Footnote continued in next column.)

this title [relating to executive branch and congressional agencies] available for public copying during normal business hours, subject to reasonable rules and regulations, and shall to the extent practicable, at the request of any person, furnish a copy of any such information, data, estimates, or statistics upon payment by such person of the cost of making and furnishing such copy." Section 603(b) of the act adds a requirement that the CBO prepare a publicly available data index.

<sup>13</sup>See Sunley and Weiss, *supra* note 10. Two earlier articles by a former estimator also describe the Treasury revenue estimating process. See Howard W. Nester, "Interpreting Revenue Estimates: Macro-Static/Micro-Dynamic," National Tax Association, 1986 Conference Proceedings, p. 208, and "The April Surprise," National Tax Association, 1989 Conference Proceedings, p. 157. Other descriptive articles from Treasury staff are listed in the text accompanying note 18 and in notes 20, 29, 39, and 40 *infra*. See also Bradford, ed., *The Distributional Analysis of Tax Policy*. A recent article from OTA staff members contains detailed revenue estimates but only a limited description of how they were produced. See Donald Kiefer, Robert Carroll, Janet Holtzblatt, Allen Lerman, Janet McCubbin, David Richardson, and Jerry Tempalski, "The Economic Growth and Tax Relief Reconciliation Act of 2001: Overview and Assessment of Effects on Taxpayers," 55 *National Tax Journal* 89-117 (March 2002).

<sup>14</sup>Treasury provides extensive job orientation to new revenue estimators. The "Revenue Estimating Handbook" is a small part of a larger on-the-job training program.

<sup>15</sup>Sunley and Weiss, *supra* note 10.

book"<sup>16</sup> in response to a 1990 Freedom of Information Act request from Tax Analysts, a nonprofit publisher. The Treasury briefing book discusses such topics as the use of revenue estimates, deadlines, general estimating methods, the data and models used in revenue estimates, the conventions employed, and relations with outside estimators including the JCT and "Lobbyists/Accounting Firms."

The briefing book also sets forth<sup>17</sup> Treasury's rationale for limiting the amount of revenue estimating information that is released to the public. The following is quoted from that discussion:

- "Estimates are often made on short notice and a great deal of experience and judgment is required."
- "Estimates frequently involve novel ideas where there is little or no data, no previous experience to draw upon, no studies to refer to, indeed nothing available but the estimator's past experience. Making this public will not result in better estimates and will hamper efforts to take advantage internally of the estimator's input."
- "Public release of detail allows interested parties to criticize those elements of the estimate favorable [sic] to them and conveniently overlook issues on the other side. Only biased criticism results and the estimate is not improved."

Although Treasury has not produced any published, official description of its revenue estimating processes and is reluctant to release information about those processes, two *OTA Papers* have touched on aspects of the subject in recent years.<sup>18</sup> The first, "U.S. Treasury Distributional Analysis Methodology" (*OTA Paper* 85), appeared in September 1999, shortly before Treasury reduced distributional analyses to "insignificant levels."<sup>19</sup> The second, "Defining and Measuring Marriage Penalties and Bonuses" (*OTA Paper* 82-Revised), appeared in November 1999 and provides insights into Treasury's esti-

imating techniques relating to the consequences of filing tax returns as a couple rather than as individuals.

An earlier staff-originated resource is the "Compendium of OTA Papers," edited by OTA members Don Fullerton and Thomas S. Neubig and written after enactment of the Tax Reform Act of 1986.<sup>20</sup> That compendium sought, among other things, to make the Treasury revenue estimating process more transparent. It included numerous articles explaining how Treasury prepared the revenue and distributional analyses required in connection with the 1986 Act.

A potentially significant Treasury revenue estimating paper authored by John McClelland, a financial economist on Treasury's revenue estimating staff, was scheduled for presentation in the fall of 2003 at the annual meeting of the National Tax Association under the working title "Corporate Integration: Description of Revenue Estimating Methodology." However, for reasons that are not clear, it was not presented. If the paper had appeared, it would have described the issues involved in estimating the revenue loss attributable to the president's January 2003 dividend exclusion proposal. According to Treasury, the paper may appear at an unspecified later date as an OTA paper.

As an executive branch agency, the Treasury Department is subject to the disclosure provisions of the Freedom of Information Act. However, with one exception, Treasury has not been required under FOIA to release any information regarding specific revenue estimates.

That exception relates to a case brought by the American Society of Pension Actuaries in 1990. In that case, the society sought release of Treasury's "assumptions and calculations" underlying an estimate that a shift in pension-related enforcement practices would generate \$666 million in new revenue. The U.S. District Court for the District of Columbia ordered release of the relevant documents because:

[T]he estimate they produced became part of the President's Budget. By estimating that the IRS could generate \$666 million in revenue by shifting its enforcement practices, the government adopted as its official policy the calculations and assumptions underlying this estimate. . . . Because [those] documents . . . contain analytic backup for the government estimate, they "embody the agency's effective law and policy" and therefore are not protected [from disclosure].<sup>21</sup>

<sup>20</sup>See *Doc* 88-952, 88 TNT 20-7. Among the 11 articles included in the compendium are "A Guide to Interpreting the Dynamic Elements of Revenue Estimates," by Howard W. Nester; "The Treasury Income Tax Simulation Model," by James M. Cilke and Roy A. Wyscarver; "Family Economic Income and Other Income Concepts Used in Analyzing Tax Reform," by Susan C. Nelson; "Tabulations from the Treasury Tax Reform Data Base," by James R. Nunns; and "The Treasury Depreciation Model," by Geraldine Gerardi, Hudson Milner, Leslie Whitaker, and Roy A. Wyscarver.

<sup>21</sup>*American Society of Pension Actuaries v. IRS*, 746 F. Supp. 188 (D.D.C. 1990) at 191. A somewhat similar suit has recently been

(Footnote continued on next page.)

<sup>16</sup>See "Revenue Estimating — Changes in Tax Law," prepared by the Revenue Estimating Division in the Treasury's Office of Tax Analysis, *Doc* 90-8832, 90 TNT 263-21.

<sup>17</sup>See *id.* at section V(D).

<sup>18</sup>Most *OTA Papers*, including the two mentioned in this paragraph, are available on the Web at <http://www.treas.gov/offices/tax-policy/library/otapapers/index.html>.

<sup>19</sup>Martin A. Sullivan, "The Decline and Fall of Distribution Analysis," *Tax Notes*, June 30, 2003, p. 1869. Sullivan argues (p. 1872) that "conservatives in the executive and legislative branches have been quietly snuffing the life out of analysis that examines tax bills' effects on the tax burdens of the poor relative to the rich." Sullivan's analysis became the basis for an outspoken op-ed article by Paul Krugman that appeared in *The New York Times*, August 5, 2003, p. A15. However, the Sullivan-Krugman charges are hotly disputed by Treasury officials in the current Bush administration, who claim that Treasury continues to make vigorous use of distributional analyses. Both sides may be right. Perhaps Treasury continues to prepare distributional analyses, as officials contend; but, if so, it refrains from making them available to the public, as Sullivan and Krugman point out. For a response to Krugman from Andrew B. Lyon, Treasury's former deputy assistant secretary (tax analysis), see "Taxes and Politics," *The New York Times*, August 9, 2003, p. A10.

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The government did not appeal the *Pension Actuaries* decision, but that hardly constitutes acquiescence in its result. Currently, Treasury is resisting — or at least delaying action on — a FOIA request<sup>22</sup> filed by Tax Analysts for documents underlying Treasury's \$364 billion cost estimate relating to the president's January 2003 dividend exclusion proposal.<sup>23</sup>

Oversight of the Treasury revenue estimating process is the responsibility of the managers who direct the Office of Tax Analysis in the Office of the Deputy Assistant Secretary for Tax Policy (Tax Analysis). They have the professional skills needed to keep tabs on the revenue estimating staff, which is one of five under their direction,<sup>24</sup> and they provide expectable, routine guidance. Individual revenue estimates are reviewed by those managers, as are other papers and memorandums generated by the OTA staff.

In the past 15 years, there have been two external reviews of the Treasury revenue estimating process by other executive branch agencies. Alan Greenspan of the Federal Reserve Board conducted the first around 1990. The second, in 2001, was undertaken by the president's Council of Economic Advisers and apparently resulted from concern by then-council member Laurence Lindsey that Treasury might be underestimating the beneficial effects of tax cuts. Neither of those estimating reviews was ever publicly announced, nor have the results been published.

With those two exceptions, there is no evidence that the estimating staff has been subjected at any point within the past generation to an in-depth, internal examination of its procedures, techniques, and estimating consistency (as contrasted with routine supervision).

Public oversight of Treasury's revenue estimating process is not currently possible as a supplement to any official, internal oversight that may occur. As outlined

earlier, Treasury provides almost no official information about how it does revenue estimates, and none at all about the basis for particular estimates. Given that fact, effective monitoring by outsiders is currently impossible. For this reason, interested members of the public are unable to perform "trust-but-verify" reviews of Treasury's revenue estimating process.

**2. The JCT.** The JCT has been engaged in some form of revenue estimating almost since its inception in 1926. When the 1974 Budget Act became law, a decision was made to enhance the JCT's revenue estimating capability. Treasury's individual income tax estimating model was made available to the JCT soon thereafter. Following the hiring of two former Treasury revenue estimators, the JCT gained access to Treasury's corporate income tax model as well.<sup>25</sup>

The JCT revenue estimating process operated completely out of the public eye until the late 1980s, at which point the JCT began to publish a series of documents describing its revenue estimating processes, thus providing a welcome amount of generalized transparency.

**a. The capital gains confrontation.** The first of those documents appeared in March 1989.<sup>26</sup> In it, JCT Chief of Staff Ronald A. Pearlman briefly discussed why the revenue estimating staffs at Treasury and the JCT had produced widely divergent revenue estimates relating to a proposal by the administration of President George H. W. Bush to reduce capital gains tax rates.

On March 6, 1990, the Senate Finance Committee held a hearing<sup>27</sup> to investigate the reasons for these differences in the Treasury and JCT estimates regarding the administration's gains tax proposals. Treasury had estimated that, by spurring gains realizations, the administration proposal would increase federal tax receipts by \$12.5 billion for fiscal years 1990-1995. Meanwhile, the JCT estimated that the proposal would reduce federal revenues by \$11.4 billion in the same time frame.

The hearing revealed several unresolved disparities in the estimating assumptions made by the two staffs. It also made clear that the principal reason for the \$23.9 billion disparity in the estimates lay in relatively small differences in the underlying behavioral assumptions used by the Treasury and JCT staffs.

In conjunction with the Finance Committee's March 1990 hearing, the JCT published its *Explanation of Methodology Used to Estimate Proposals Affecting the Taxation of*

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filed by the Security Financial Life Insurance Company. See "Treasury Sued for Info Underlying Its Revenue Estimates," *Tax Notes*, April 5, 2004, p. 50.

<sup>22</sup>Tax Analysts' Freedom of Information Act request was made in a letter to Treasury dated March 4, 2003. *Doc 2003-6918, 2003 TNT 52-12*. The letter requested "output files or printouts" from Treasury's individual income and corporate tax computer simulation models, plus "any spreadsheets summarizing the data . . . or making off-model adjustments to the output." In April 2003 Tax Analysts requested and was granted expedited processing of its March 4, 2003, request. As of January 2005, Treasury has not responded to the March 2003 request, citing its FOIA workload as the reason for the delay. (Only one Treasury attorney processes tax-related FOIA requests, and she has other duties in addition to consideration of FOIA issues.)

<sup>23</sup>President George W. Bush announced his dividend exclusion proposal on January 7, 2003, as part of a broader tax package. See *Doc 2003-565, 2003 TNT 5-25*. The accompanying Treasury press release stated that the president's exclusion plan would decrease revenues by \$364 billion during fiscal years 2003-2013. *Doc 2003-833, 2003 TNT 5-20*.

<sup>24</sup>In addition to the revenue estimating staff, Treasury's Deputy Assistant Secretary (Tax Analysis) supervises staffs handling individual taxation, business taxation, international taxation, and economic modeling. See Charts 2122 through 2134 in *The Tax Directory*, *supra* note 5.

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<sup>25</sup>Background information regarding the JCT revenue estimation process is provided in Part IV of the *Joint Committee History & Background*, which is available on the Web at <http://www.house.gov/jct/revhist.htm>.

<sup>26</sup>JCT, *Statement of Ronald A. Pearlman, Chief of Staff, Joint Committee on Taxation, Before the Senate Committee on Finance*, JCX-3-89, March 14, 1989, *Doc 89-2024, 89 TNT 59-10*.

<sup>27</sup>For a report on the hearing, see *Tax Notes*, March 12, 1990, p. 1223. In addition to presenting a statement to the Finance Committee (*Doc 90-1790, 90 TNT 51-38*), Treasury Assistant Secretary Kenneth W. Gideon provided "the Finance Committee with an armload of papers describing Treasury assumptions, Treasury data, and hard-to-decipher Treasury equations" and "challenged the JCT to do the same." (p. 1224).



*Income from Capital Gains*.<sup>28</sup> That report described the revenue estimating process in general terms and provided specific detail regarding the JCT approach to gains estimates. It then analyzed the differences between the JCT and Treasury's approaches to the capital gains issue, including the differing assumptions about the likely behavioral responses to a cut in gains rates.

Treasury was also active in publishing materials relating to capital gains revenue estimating issues. Starting in May 1989, it released a series of OTA papers detailing several different methods and data approaches to estimating the effects of gains tax changes.<sup>29</sup>

No one can read the JCT's 1989 and 1990 documents on the gains tax estimation issue, Treasury's 1989 OTA papers, and the March 6, 1990, Senate Finance testimony on the same subject<sup>30</sup> without acquiring a better understanding of both the revenue estimating process in general and the importance of assumed behavioral responses in that process.

The 1989-1990 gains tax confrontation was "destructive," according to one JCT observer, because it created considerable acrimony between the Treasury and JCT revenue estimating staffs, which theretofore had generally worked cooperatively on estimating chores. At the same time, however, it demonstrated the ability of full disclosure to dispel suspicion and distrust resulting from conflicting revenue estimates.

**b. Descriptions of methods.** Two other JCT revenue estimating reports also appeared in the early 1990s. *Discussion of Revenue Estimating Methodology and Process*, published in 1992, provided a definitive general overview of the procedures used by the JCT when making revenue estimates, including distributional analyses.<sup>31</sup> Part II provided answers to common questions asked by members of Congress, who are the principal consumers of JCT estimates. Those questions and answers cover a wide variety of issues. The Q&A functions, in effect, as an estimating procedures manual for the JCT.

The following year, the JCT produced a document dealing with distributional analysis and methods.<sup>32</sup> It has become known as the "Red Book." Although thought-

fully written, only a single distributional table was prepared using its methods.<sup>33</sup> Thereafter, the proposed methods were not used again because the JCT estimating staff failed to reach an ongoing consensus about how to implement them.<sup>34</sup>

A more recent description of the JCT's overall estimating methods is set forth in May 2002 testimony before the House Ways and Means Oversight Subcommittee by Lindy Paull,<sup>35</sup> who was then chief of staff of the JCT. This testimony provides a brief but useful JCT revenue estimating overview and history, and includes an "attachment" that lists 15 JCT "Revenue Estimating Methodological Publications" that appeared between 1990 and 2001. However, the main focus of the Paull testimony is on the feasibility of incorporating the macroeconomic effects of tax law changes into JCT revenue estimates. That topic is discussed in the next section.

**c. Dynamic scoring.** Since the appearance of the Red Book more than 10 years ago, most of the revenue estimating information released by the JCT has focused on the issue of "dynamic scoring," which is the phrase used to describe the incorporation of macroeconomic effects into the assumptions underlying revenue estimates.

The principal macroeconomic aggregates that relate to dynamic scoring are gross domestic product, aggregate investment, interest rates, the overall price index, and the total level of state and local taxes.<sup>36</sup> In ordinary revenue estimates, those baseline aggregates, which are supplied to the JCT by the CBO, are assumed to remain unchanged by proposed tax law changes. Hence, any "feedback effects" on revenue attributable to changes in those aggregates are excluded from the revenue estimate. For that reason, those estimates are sometimes called "standard" or "static" estimates. In contrast, a dynamic revenue estimate relating to a tax proposal includes both the proposal's initial revenue effects and the feedback effects

<sup>28</sup>JCT, *Explanation of Methodology Used to Estimate Proposals Affecting the Taxation of Income from Capital Gains*, JCS-12-90, March 27, 1990, Doc 90-2432, 90 TNT 67-8.

<sup>29</sup>See Gerald E. Auten, Leonard E. Burman, and William C. Randolph, "Estimation and Interpretation of Capital Gains Realization Behavior: Evidence from Panel Data"; Robert Gillingham, John S. Greenlees, and Kimberly D. Zieschang, "New Estimates of Capital Gains Realization Behavior: Evidence from Pooled Cross-Section Data"; and Jonathan D. Jones, "An Analysis of Aggregate Time Series Capital Gains Equations," all of which are available on the OTA Web site at <http://www.treas.gov/offices/tax-policy/library/otapapers/otapapers80-93.shtm>.

<sup>30</sup>See *supra* note 27.

<sup>31</sup>JCT, *Discussion of Revenue Estimation Methodology and Process*, JCS-14-92, August 13, 1992, Doc 92-7658, 92 TNT 166-8.

<sup>32</sup>JCT, *Methodology and Issues in Measuring Changes in the Distribution Tax Burdens*, JCS-7-93, June 14, 1993, Doc 93-7105, 93 TNT 133-21. For a related scholarly paper by Thomas A. Barthold and William Jack, see "JCT Authors Report on JCT Distributional Methodology," Doc 93-13077, 93 TNT 259-29. For

(Footnote continued in next column.)

a somewhat more recent discussion of JCT distributional analysis techniques, see "Distributional Analysis at the Joint Committee on Taxation" in Bradford, ed., *The Distributional Analysis of Tax Policy*, AEI Press, Washington, 1995.

<sup>33</sup>The table using the JCT's new distributional techniques related to the revenue provisions of the Omnibus Budget Reconciliation Act of 1993. That table appeared as footnote 17 in Joint Committee on Taxation, *Estimated Budget Effects of the Revenue Provisions of H.R. 2264 (the Omnibus Budget Reconciliation Act of 1993) as Agreed to by the Conferees*, JCX-11-93, August 4, 1993, Doc 93-8497, 93 TNT 164-7.

<sup>34</sup>A chart indicating the number of JCT distributional estimates produced each year since 1989 appears in Martin Sullivan, "The Decline and Fall of Distribution Analysis," *Tax Notes*, June 30, 2003, p. 1869.

<sup>35</sup>Testimony of the Staff of the Joint Committee on Taxation at a Hearing of the Subcommittee on Oversight of the House Committee on Ways and Means Concerning Modeling the Economic Effects of Changes in Tax Policy, JCX-36-02, May 6, 2002, Doc 2002-10877, 2002 TNT 89-8.

<sup>36</sup>See "Behavioral Effects and Macroeconomic Aggregates" in *Written Testimony of the Joint Committee on Taxation Regarding the Revenue Estimating Process*, JCX-1-95, January 10, 1995, section II(D)1, Doc 95-441, 95 TNT 7-10.

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on revenue attributable to the likely changes in the baseline economic aggregates due to enactment of the proposal.<sup>37</sup>

Dynamic scoring involves more than merely considering the behavioral effects of tax changes. Revenue estimators at Treasury and the JCT have always taken behavioral effects into account<sup>38</sup> in revenue estimates whenever they had some basis for predicting those effects. As a former JCT chief of staff recently pointed out, the JCT has never prepared truly "static" revenue estimates that disregarded behavioral effects. Instead, he said, the JCT now prepares both "standard" estimates (which consider behavioral effects whenever possible) and "dynamic" scores (which consider both behavioral effects and macroeconomic feedback effects).

Use of dynamic scoring has been urged by supply-side proponents of cuts in tax rates, who wish to take into account the beneficial effects of tax cuts on subsequent economic activity and thus on tax revenues.<sup>39</sup> Static or standard scoring, in their view, overstates the likely revenue losses attributable to tax cut proposals by omitting subsequently generated revenue attributable to the additional economic activity induced by the tax cut. Those who view dynamic scoring less enthusiastically point to the uncertainties associated with properly modeling feedback effects.<sup>40</sup>

<sup>37</sup>The rules of the House of Representatives that define the process of dynamic scoring are summarized in *Overview of Work of the Staff of the Joint Committee on Taxation to Model the Macroeconomic Effects of Proposed Tax Legislation to Comply with House Rule XIII.3.(h)(2)*, JCX-105-03, December 22, 2003, section I(A) and note 3, Doc 2003-26926, 2003 TNT 246-8.

<sup>38</sup>Examples of typical behavioral effects that have traditionally been considered by Treasury and the JCT include the effects of changes in capital gains tax rates on gains realizations and the effects of IRA changes on the account "take-up rate." For other examples, see Gerald Auten and Robert Carroll, "The Effect of Income Taxes on Household Income," 81(4) *The Review of Economics and Statistics*, 681-693 (1999).

<sup>39</sup>An early discussion of how and when to consider macroeconomic feedback effects is contained in the appendix to the August 17, 1978, Senate Finance Committee testimony by Treasury Secretary W. Michael Blumenthal regarding H.R. 13511, the Revenue Act of 1978. That nine-page appendix is available as Doc 78-7133 through the Tax Analysts Document Service at 800-955-3444. Regarding the effect of tax changes on economic capacity and long-run budgetary figures, the appendix concludes that "As research sheds more light on the nature of these effects, it may be possible to incorporate them more formally into longer-run projections." As it turned out, it took 25 years before the first full-blown macroeconomic scoring appeared. See note 47 *infra*.

<sup>40</sup>For example, in 1981 Northwestern University economist Robert Eisner prepared two Treasury OTA papers with Robert S. Chirinko in which the authors compared investment equations for different macroeconomic models. They basically concluded that, by choosing one's model carefully, large macroeconomic effects could be produced for tax changes relating to such matters as depreciation. See Robert S. Chirinko and Robert Eisner, "The Effects of Tax Policies on Investment in Macroeconometric Models: Full Model Simulations," OTA paper 46, January 1981, and "The Effects of Tax Parameters on the Investment Equations in Macroeconomic Econometric Models,"

(Footnote continued in next column.)

The year 1995 was a watershed in the JCT's approach to dynamic scoring. The year began with an unusual joint hearing conducted on January 10 by the House and Senate Budget committees.<sup>41</sup> The purpose of the hearing, in the words of House Budget Committee Chair John R. Kasich, R-Ohio, was "to consider the role that static versus dynamic scoring plays in promoting or hindering accurate assessment of the costs and benefits of policy options before the Congress."<sup>42</sup> The hearing was inspired by Republican demands that dynamic scoring techniques be applied to evaluate the likely economic effects of the "Contract With America" that formed the Republican legislative agenda for the first 100 days of the 104th Congress.

The hearing featured a distinguished panel of witnesses from the private sector<sup>43</sup> in addition to representatives of the JCT and CBO.<sup>44</sup> The witnesses, whose views spanned the political spectrum, generally agreed that, in theory, revenue estimates would be more accurate if they included the feedback effects of tax changes on the basic macroeconomic aggregates. Except for Dr. Martin Feldstein of Harvard, they also agreed that there were serious practical and theoretical hurdles to overcome before macroeconomic feedback effects could be included in revenue estimates.<sup>45</sup>

The Finance Committee held a hearing on January 24, 1995, that produced similar conclusions regarding the feasibility of using dynamic revenue estimating techniques. As a result, Finance Committee Chair Bob Packwood, R-Ore., announced on January 24, 1995, that revenue estimates would remain "static" for the time

OTA paper 47, January 1981. OTA papers are available on the Web at <http://www.treas.gov/offices/tax-policy/library/ota/papers/otapapers80-93.shtml>.

<sup>41</sup>See John Godfrey, "Witnesses Caution Lawmakers on Use of 'Dynamic' Budget Estimates," Doc 95 TNT 7-2.

<sup>42</sup>See paragraph 2 of the opening statement of House Budget Committee Chair John R. Kasich, Doc 95-446, 95 TNT 7-36.

<sup>43</sup>Written testimony was furnished by Henry J. Aaron, director of the Economic Studies Program at the Brookings Institution, Doc 95-449, 95 TNT 7-42; Michael J. Boskin, professor of economics and Hoover Institution senior fellow, Stanford University, Doc 95-450, 95 TNT 7-43; Martin Feldstein, president of the National Bureau of Economic Research and professor of economics at Harvard, Doc 95-451, 95 TNT 7-44; Alan Greenspan, chairman, Board of Governors of the Federal Reserve System, and Rudolph G. Penner, managing director of Barents Group LLC, KPMG Peat Marwick, and former director of the CBO, Doc 95-447, 95 TNT 7-40; Norman B. Ture, president, Institute for Research on the Economics of Taxation, and Paul A. Volcker, former chairman, Board of Governors of the Federal Reserve System, Doc 95-448, 95 TNT 7-41.

<sup>44</sup>For the testimony of Robert D. Reischauer, director of the CBO, see Doc 95-442, 95 TNT 7-16. For the testimony of Kenneth J. Kies, newly installed chief of staff of the JCT, see Doc 95-441, 95 TNT 7-10.

<sup>45</sup>A useful summary of the testimony of the private witnesses appearing at the January 10, 1995, hearing is set forth in Joint Committee on Taxation, *Methodology and Issues in the Revenue Estimating Process*, JCX-2-95, January 23, 1995, section V, Doc 95-1118, 95 TNT 15-15.



being. Packwood said the message he had received from witnesses was “be careful, don’t go wild.”<sup>46</sup>

After those hearings, the JCT continued to work on the dynamic scoring issue. Those efforts came to fruition on May 8, 2003, when a floor statement by House Ways and Means Chair William M. Thomas, R-Calif., made public a detailed description by the JCT of the steps it had taken to provide a dynamic estimate of the revenue costs of H.R. 2, which contained President George W. Bush’s 2003 tax cut proposals.<sup>47</sup> This was the JCT’s first full-blown dynamic analysis. Its release came in response to the January 7, 2003, adoption of House Rule XIII.3(h)(2),<sup>48</sup> which required a “macroeconomic impact” analysis of major tax legislation.

That JCT floor statement discussed the three economic models used in preparing the JCT’s dynamic estimate, described the estimators’ assumptions regarding federal fiscal and monetary policy, outlined the behavioral response assumptions made by the estimators, and set forth the estimators’ simulation results including the probable changes in economic growth, labor supply, and employment. It also described the likely budgetary effects of the proposals under review and listed the data sources used by the estimators.

Subsequently, on December 22, 2003, the JCT published an expanded version of its May 2003 analysis of the macroeconomic effects of H.R. 2.<sup>49</sup> The December report also contained a history and description of the JCT’s macroeconomic modeling work and a description of the dynamic scoring activities of its “Blue Ribbon Advisory Panel.”

**d. Transparency efforts.** The JCT squarely addressed the issue of revenue estimating transparency in a May 18, 1995, press release,<sup>50</sup> in which the committee announced that it was taking steps to “open up the estimating process so that the public has a better understanding of the assumptions and procedures used.” The press release also said that the JCT would establish an advisory board “to improve the estimating process and estimating meth-

odology.” The release added that the JCT would begin to include “information about the behavioral assumptions” in its estimates, provide a “description of significant potential macroeconomic effects” of tax proposals, and make public “aspects of its primary [estimating] models which do not include confidential taxpayer information.”

The JCT’s May 18 press release was accompanied by two substantially identical letters, also dated May 18, from Kenneth J. Kies, chief of staff of the JCT, to Bill Archer, House Ways and Means Committee chair, and Bob Packwood, Senate Finance Committee chair.<sup>51</sup> In addition to the changes outlined in the press release, those letters stated that the JCT would begin to meet with “reputable outside economists” to discuss the feasibility of actually “incorporating macroeconomic effects into our estimates” as contrasted with simply describing them. The letters also pledged to monitor the accuracy of the estimating process “by selecting several estimates to study over a period of years following enactment” and to institute a new inventory system “so that we can more efficiently process and monitor the progress of pending estimate requests.”

At the same time, however, the two May 18 letters cut back on some of the broad language in the JCT press release. For example, the letters indicated that most of the information listed in the JCT release would be prepared only if “requested by the member of Congress submitting the revenue estimate request” and thus would not be available to the public unless the member decided to release it.

Later in 1995, Kies authored a Viewpoint article in *Tax Notes* magazine<sup>52</sup> in which he declared flatly that “the public knows too little about how the JCT prepares revenue estimates.” He went on to outline the initiatives then underway to begin “letting in the light on the estimating process while at the same time deflating the wrong and misleading statements about the estimating process.”

**The 1995 JCT initiatives mark the high-water point for JCT efforts to ‘open up’ the estimating process. It is not clear how much those initiatives accomplished to promote transparency.**

The 1995 JCT initiatives mark the high-water point for JCT efforts to “open up” the estimating process. Nearly 10 years later, it is not clear how much those initiatives accomplished to promote transparency.

<sup>46</sup>See “Packwood: Revenue Estimates to Stay Static,” *Doc 95 TNT 16-4*.

<sup>47</sup>*Macroeconomic Analysis of H.R. 2, the “Jobs Growth Reconciliation Tax Act of 2003” Prepared by the Staff of the Joint Committee on Taxation, Congressional Record*, May 8, 2003, pp. H3829-H3832.

<sup>48</sup>*Rules of the House of Representatives*, 108th Congress, January 7, 2003, p. 25. Rule XIII.3(h)(2)(A) provides that “it shall not be in order to consider a bill or joint resolution reported by the Committee on Ways and Means” unless the report on the bill includes either “an analysis of the macroeconomic impact” of the bill or an explanation “why such an analysis is not calculable.”

<sup>49</sup>*Supra* note 37.

<sup>50</sup>“Chairmen Archer and Packwood Announce Improvements in the Joint Committee Revenue Estimating Process,” Joint Committee Press Release No. PR-1, May 18, 1995, *Doc 95-5070*, 95 *TNT* 98-27. For related news coverage, see “JCT Announces Efforts to Develop ‘Macroeconomic’ Models,” *Doc 95 TNT 98-4*. The press release was based on two essentially identical letters from JCT Chief of Staff Kenneth J. Kies, one to Ways and Means Committee Chair Bill Archer (*Doc 95-5074*, 95 *TNT* 98-25) and the other to Senate Finance Committee Chair Bob Packwood (*Doc 95-5075*, 95 *TNT* 98-26).

<sup>51</sup>See *Doc 95-5074*, 95 *TNT* 98-25 (Archer) and *Doc 95-5075*, 95 *TNT* 98-26 (Packwood).

<sup>52</sup>See “The Revenue Estimating Process — Letting In the Light and Letting Out the Hot Air,” *Tax Notes*, Oct. 16, 1995, p. 373.

For example, it does not appear that the JCT has initiated a project “to monitor the accuracy” of its estimating process by “selecting several estimates” for retrospective analysis subsequent to enactment. If it has done monitoring of that sort, the results have not been made public.

The status of several of the other initiatives is also murky. In particular, it is not clear whether members of Congress regularly request and receive information about modeling techniques or macroeconomic effects. However, in a few instances, according to former JCT officials, members of Congress have asked about — and been briefed on — the behavioral assumptions underlying estimates.

Also, former JCT officials confirm that the Joint Committee has now and then made public the basic elements of its estimating models, mainly in response to requests from major accounting firms.

Unlike Treasury, the JCT is not required to disclose documents under the Freedom of Information Act, but it is subject to a different — and perhaps more effective — disclosure regime because it has “535 Congressional bosses” who can request both revenue estimates and supplementary information about how they were done. In addition, by working through a sympathetic member of Congress, the lobbying community can obtain detailed information about JCT revenue estimates. That type of disclosure is sometimes called “selective transparency.”

However, the existing JCT restrictions on disclosure of information relating to revenue estimates do affect the general public, including students, academic researchers, and the press. Their access to specific revenue estimating information depends to a large degree on how well-connected they are on Capitol Hill. Under existing selective transparency arrangements, if individuals lack political connections, they lack access.<sup>53</sup> Thus, outside review of the JCT revenue estimating process — especially scholarly review — is frequently thwarted.

**e. Advisory boards.** The advisory board announced in the Joint Committee’s May 18, 1995, press release became known as the “Blue Ribbon Advisory Panel.” It was composed of private-sector economists from both political parties and various political persuasions. Its status is murky, and it is not clear what work it has actually done. It appears that the panel has been largely inactive, except for three meetings in 2002 to consider dynamic scoring issues.

The Blue Ribbon Advisory Panel superseded an earlier Revenue Estimating Advisory Board, formed on April 18, 1989, at the request of Ways and Means Chair Dan Rostenkowski, D-Ill., to consult with the JCT revenue

estimating staff on econometric models, estimating methods, and current academic research.<sup>54</sup>

From its inception, the Blue Ribbon Panel’s principal focus has been to assist the JCT in moving toward use of dynamic analysis. However, until 2002, the panel was not regularly called on for advice. In that year, in response to a request from Ways and Means Chair Thomas, the panel met three times to review the JCT’s dynamic scoring capability.

The original announcement of formation of the Blue Ribbon Panel envisioned use of the panel to review all aspects of the Joint Committee’s revenue estimating work, but that review has not occurred. Nor has the panel met since it finished its series of three 2002 meetings on dynamic scoring.

Opinions differ about the panel’s usefulness. A recent JCT description of the panel’s activities paints a favorable picture,<sup>55</sup> but a private-sector observer who is a member of the panel states that its work has been “directed entirely” to the issue of dynamic scoring and that, while it has been “useful and influential” regarding that subject, it has “not taken up” any other topics. Another knowledgeable private-sector revenue estimator describes the panel as a semimoribund body whose chief function is to provide the JCT with a response when the committee is challenged on the need for enhanced public oversight over the revenue estimating process.

In 1996 the JCT also convened a group of macroeconomic modelers who had experience in forecasting the economic effects of major tax initiatives. That “macro group” was separate from the Blue Ribbon Panel discussed above. The modeling group worked with the JCT staff to ascertain why different forecasting or simulation models produced varying results. The results of that effort were made public in a symposium held in January 1997.<sup>56</sup> The JCT then set to work to develop a macroeconomic equilibrium growth model (MEG). The MEG, along with other models, can be used to produce a dynamic analysis of tax proposals and to estimate the effects of specific tax proposals on different groups of taxpayers.

**f. The JCT and Congress.** Relations between members of Congress and the JCT are a problematic element in the revenue estimating transparency picture. Congress, acting through the JCT, is in full charge of the JCT revenue estimators. Congress is the revenue estimators’

<sup>53</sup>This is made clear in the discussion of “Administrative Procedures” in Part II(A)(5) of Joint Committee on Taxation, *Discussion of Revenue Estimation Methodology and Process*, August 13, 1992, which states that “Requests for revenue estimates of legislative proposals are treated as confidential correspondence. Generally, revenue estimates are released only to the Member making the request. Therefore, the estimate remains confidential unless the Member decides to make the estimate public.”

<sup>54</sup>The Ways and Means Committee press release announcing the formation of this panel is available as *Doc 89-3089*, 89 TNT 88-2. Brief biographical sketches of the six advisory board members are available as *Doc 89-3231* through the Tax Analysts Document Service at 800-955-3444.

<sup>55</sup>See *Overview of Work of the Staff of the Joint Committee on Taxation to Model the Macroeconomic Effects of Proposed Tax Legislation to Comply with House Rule XII.3.(h)(2)* (JCX-105-03), December 22, 2003, pp. 15-22.

<sup>56</sup>The models used in the 1996-1997 exercise, together with the proposals and results of the JCT’s effort, are summarized in *Joint Committee on Taxation Tax Modeling Project and 1997 Tax Symposium Papers*, JCS-21-97, November 20, 1997. This report was published in three parts as *Doc 97-31764*, 97 TNT 227-41 (Part 1), 97 TNT 227-42 (Part 2), and 97 TNT 227-43 (Part 3).

employer and the party that has authority to oversee the estimating process, alter the rules, and implement changes.

Therefore, if the JCT is secretive about its revenue estimates, that fact reflects the will of Congress. Congress, acting through the JCT chief of staff, currently requires the revenue estimators to maintain confidentiality about legislative proposals and their related estimates. Even the existence of a request to the JCT for a revenue estimate is confidential,<sup>57</sup> and the resulting estimates are also confidential. Early in the history of JCT revenue estimating, the practice emerged that estimates were released only to members of Congress and that the members could then release the estimates to the general public if they so desired.<sup>58</sup> Greater transparency for the JCT revenue estimating process could threaten this custom; but even if this custom remains unchanged, it should nevertheless be possible to increase the degree of transparency for estimates that are part of a chair's mark or scored legislation.

Members of Congress now and then hide behind delays<sup>59</sup> in the revenue estimating process when they really do not want to support a specific tax proposal but want to appear to do so. "We can't move without a revenue estimate," they tell advocates of the proposal. Also, when members wish to block a proposal, they sometimes attack it by claiming it is based on flawed or biased revenue estimates. The JCT estimators find it difficult to defend themselves when they are used as whipping boys in these ways.

<sup>57</sup>See "Need a Revenue Estimate? JCT Officials Demystify the Estimating Process," *Tax Notes*, May 1, 1989, p. 521.

<sup>58</sup>At present, this practice is merely customary and is not required by any statute or rule. It is described in part II(A)(5) of JCT, *Discussion of Revenue Estimating Methodology and Process*.

<sup>59</sup>Over the years, JCT reports and press releases on the revenue estimating process have cataloged the increasing number of requests for JCT revenue estimates, which have grown steadily from fewer than 1,000 per year in the 1970s and 1980s to nearly 5,000 per year today. (Although no figures are available, the number of requests for Treasury estimates has doubtless grown too.) Delay is a result of that growth, which is caused by an excess of requests (demand) over staff resources (supply). In economic terms, this excess is inevitable (given the current rules for requesting estimates) for three reasons. First, those asking for revenue estimates (executive branch officials and members of Congress) face a zero price (revenue estimates are free), so demand is unlimited. Second, there is a real cost (staff time and resources) to preparing revenue estimates, and that restricts supply. Third, policymakers in the executive branch and Congress realize that honest revenue and cost estimates can "clip their wings" when they propose tax cutting and spending plans and are therefore reluctant to increase the supply of revenue and cost estimates by authorizing the money needed to hire more estimators. As the mayor of London has proven in the case of vehicular access to public streets, the solution to this supply-demand problem is obvious: One must "charge" executive branch officials and members of Congress in some fashion for revenue estimates (institute a quota system, impose an increasing "delay sanction" as the number of requests increases, or the like). Revenue estimators are good economists, and demand-supply problems are their bailiwick; a solution to the overload and delay problem therefore ought to be possible.

**f. Oversight.** The members of Congress who constitute the Joint Committee seldom meet, and at no point have they conducted a meaningful investigation into the quality of the work of the JCT revenue estimating staff. Instead, members' interests in recent years have focused on questions regarding so-called dynamic scoring. Beyond that, there has been no oversight of the JCT estimating process by the members of the JCT.

As a result, the task of internal oversight has been left almost entirely to the JCT chief of staff, who is usually trained as a lawyer or public administrator, not as an economist. This increases the difficulty of supervising economists working in an arcane area. Further, the chief of staff has duties that go far beyond review of revenue estimating practices. Hence, for routine revenue estimates, the chief of staff "can obtain only a rudimentary understanding of the staff's methodology," according to one former JCT revenue estimator. Detailed scrutiny is necessarily left to the revenue estimating staff itself. For more controversial estimates, the chief of staff meets with the estimating staff and asks questions. However, that type of review falls short of consistent, ongoing oversight and quality control.

Moreover, there is no indication that this lack of oversight has been remedied to any degree by critiques from individual members of Congress, lobbyists, advisory groups, or the general public. Lobbyists and the members of Congress with whom they work may ask questions about a revenue estimate with which they disagree; but once an estimate has been completed, it is generally difficult or impossible to change,<sup>60</sup> especially when legislative time constraints are severe.

Almost never do discussions between lobbyists and revenue estimators amount to a thoughtful critique of estimating procedures, methods, and consistency. Lobbyists usually want to produce a specific result, not necessarily the right result. Now and then, a lobbyist will share suggestions and insights privately, but private suggestions hardly amount to a thorough investigation of the quality of the work of the JCT revenue estimating staff. A critique of that sort has yet to be conducted.

**g. Operating guidelines.** The JCT revenue estimating process is not governed by any statutes or published regulations,<sup>61</sup> as is the CBO process,<sup>62</sup> but there are internal guidelines that are prepared by the committee itself.

<sup>60</sup>One private-sector revenue estimator routinely advises his clients that their chances of having an effect on official scoring are greater if a client's analysis is provided *before* an official score is prepared. Lobbyists may sometimes submit a competing revenue estimate after an official score has been released, he says, but that approach generally has little effect on official estimates.

<sup>61</sup>Sections 8001-8023, which authorize establishment of the JCT and set forth its powers and duties, do not mention revenue estimating. The JCT's authority to engage in revenue estimating appears to derive from its generalized duty to "report, from time to time . . . the results of its investigations." See section 8022(3)(A).

<sup>62</sup>See *supra* note 12.



An example is set forth in section II(A) of the JCT's *Discussion of Revenue Estimation Methodologies and Process*,<sup>63</sup> which, under the heading "Administrative Procedures," discusses such questions as how estimates are requested, how the JCT staff decides which requests to answer, how members of Congress can obtain further information, the confidentiality of estimates, the content of estimates, the time periods to which estimates relate, the criteria for doing reestimates, and the participation of "outside parties" in the estimating process.

Because those guidelines are internal rather than statutory, they can be changed by the JCT when change seems appropriate. Thus, for example, the JCT could decide to expand the number of revenue estimates it publishes on the Web to include substantially all of its revenue estimates,<sup>64</sup> just as the CBO now does for substantially all of its legislative cost estimates.

**h. Who is served by the JCT?** The JCT's revenue estimating transparency obligations sometimes become muddled because it is not clear who should be served by the work of the JCT estimating staff. Is the JCT staff working primarily for individual members of Congress who "need a number" to facilitate introduction of tax legislation, or should it be working primarily for the general public and satisfying the public's need to know about government operations?

A facile answer is that the JCT estimating staff should be doing both things simultaneously, but sometimes those dual goals conflict. For example, as outlined earlier, the JCT maintains strict confidentiality about revenue estimates prepared at the request of individual members of Congress. When preparing those estimates, the JCT operates, in effect, as a confidential professional adviser to the individual member of Congress who requested the estimate. On completion, the estimate effectively becomes that member's property, not the public's, so the estimate is released only if the requesting member so authorizes. As a professional adviser, the JCT regards itself as being in much the same position, vis-à-vis a member of Congress, as a private attorney or accountant is in relation to a client.

A variation on that position is the claim that disclosure of revenue estimates would have a chilling effect on the

sound advice that the JCT currently provides to members of Congress and that revenue estimates should therefore be protected from disclosure just as "attorney work product" is protected from disclosure in an attorney-client situation.

One problem with that argument is that revenue estimates relate to proposals that have the potential to become public laws. Once a bill is introduced, a revenue estimate is not simply a private matter between "attorney" and "client." Instead, estimates are an important piece of information that the public needs to evaluate proposed public laws. Hence, even if estimates are kept confidential while legislation is being developed, the JCT Web site should never lack a revenue estimate for an introduced bill. Secrecy for estimates should end when a tax bill is dropped into the legislative hopper.

**Secrecy for estimates should end when a tax bill is dropped into the legislative hopper.**

A second problem with the attorney-client argument is that the existing practice of publishing the JCT's revenue estimates with respect to chair's marks and other scored legislation does not appear to have had any chilling effect on the frankness of the JCT's advice. Surely, if any "chill" were to occur, it would occur in those cases.

A change in the JCT's member-centric orientation is needed if the JCT is to achieve the same degree of revenue estimating transparency as the CBO. Bringing about such a change will not be easy. Members of Congress clearly benefit from having a skilled professional staff to crunch numbers without having to release those numbers to the public if they prove embarrassing. Under those circumstances, a JCT chief of staff will need strength, some courage, and the backing of supportive Ways and Means and Finance committee chairs to assert the public's right to know against built-in congressional pressures favoring secrecy.<sup>65</sup>

In any event, the attorney-client argument has little relationship to other estimating disclosure issues such as publishing the assumptions underlying revenue estimates, making estimating models available to the public, and providing sensitivity analysis for estimates.

**3. The CBO staff.** Unlike either Treasury or the JCT, the CBO operates under statutory rules that require it to provide "the basis for each . . . estimate" and to make "information, data, estimates, and statistics" obtained from other agencies available for "public copying."<sup>66</sup>

Obedient that mandate, the CBO has developed a disclosure policy<sup>67</sup> that requires the agency "to disclose

<sup>63</sup>See *supra* note 31.

<sup>64</sup>The JCT publishes revenue estimates that relate to chairs' marks, reported legislation, House- and Senate-passed bills, conference reports, and tax expenditures. To obtain those estimates, the reader can go to the JCT Web site at <http://www.house.gov/jct/>, click on "continue," access JCT Publications by year, and then search for JCX Documents relating to "estimated revenue effects." However, the JCT does not publish the far more numerous revenue estimates it prepares in response to requests from individual members of Congress, even after legislation based on those estimates is introduced. Nor do its published estimates generally describe either how the estimates were done or the assumptions on which they were based. In addition to the JCT, the CBO publishes selected JCT revenue estimates. See, e.g., the revenue estimate relating to H.R. 3971, the Highway Reauthorization Tax Act of 2004, on the CBO Web site at <http://www.cbo.gov/showdoc.cfm?index=5257&sequence=0>.

<sup>65</sup>Now and then, the JCT has indicated a desire to open up the revenue estimating process. See *supra*, p. 337.

<sup>66</sup>See 2 U.S.C. sections 603 and 653, *supra* note 12.

<sup>67</sup>The CBO's *Policies for Preparing and Distributing Its Estimates and Analyses* are available on the Web at <http://www.cbo.gov/Policies.cfm>. They provide in pertinent part that "Both the Congressional Budget Act and the Unfunded Mandates Reform Act direct CBO to disclose the basis for each

(Footnote continued on next page.)

the basis for each budget and mandate cost estimate.” The policy statement says that includes “disclosure of the critical assumptions and analytic methodologies used to prepare the estimate.” The statement also assures interested persons that the CBO will supply “further details on request.”<sup>68</sup> Plainly, this approach is different from the disclosure regime at Treasury or the JCT.

However, the CBO’s basic estimating job is quite different from that of Treasury and the JCT. The CBO’s main job is to prepare baseline economic forecasts involving the major economic variables: gross domestic product, unemployment, inflation, and interest rates. It also prepares baseline receipts estimates. Those forecasts constitute the guideposts in terms of which congressional committees, including the JCT, can compute the effects of changes in the tax law.

The CBO also develops cost estimates for most legislation, and the underpinnings for those estimates are published on the Web at <http://www.cbo.gov/CESearch.htm>. However, for legislation involving income, estate and gift, excise, and payroll taxes, the applicable law requires the CBO to use the estimates provided by the JCT.<sup>69</sup> CBO revenue-related analyses are limited to proposals involving tariffs, offsets, and user fees. Proposals in those three areas are generally of minor importance to most tax practitioners.

There are some important differences between the CBO and the JCT when it comes to preparing tax-related revenue estimates. First, the JCT estimating staff has the advantage of immediate access to the tax attorneys on the JCT staff, who can help in significant ways to improve the accuracy of an estimate. The CBO staff lacks similarly prompt access to legal advice. “Having revenue estimators and tax attorneys working for the same boss helps to break down barriers” said one Washington think tank economist familiar with both JCT and CBO estimating

practices. “This is particularly true,” he added, “with respect to issues such as international taxation and depreciation.”

Second, the JCT estimating staff is often given much less turnaround time when preparing an estimate than is the CBO. JCT estimators are frequently called on to provide ballpark revenue estimates when members of Congress are drafting legislation. In contrast, the CBO’s tax division is hardly ever called on to provide ballpark estimates. Similarly, in the course of a single drafting session, tax legislation may undergo numerous permutations, thus requiring multiple JCT revenue reestimates. In contrast, the CBO is not usually required to produce on-the-fly estimates and is therefore able to focus on developing more carefully honed figures.

The JCT routinely provides the CBO with very little information about the bases for its revenue estimates relating to tax bills. As a result, the CBO remains largely in the dark, just like the general public, about the underpinnings for the Joint Committee’s revenue estimates.

***The CBO remains largely in the dark, just like the general public, about the underpinnings for the Joint Committee’s revenue estimates.***

Because the CBO’s basic job is to forecast the major economic variables, it finds transparency to be in its interest. Transparency is a way of achieving credibility for its estimates. “We have to convince the world that we have a sensible way of doing business,” a senior CBO official recently said.

However, the CBO is not completely transparent when making its baseline estimates. According to persons familiar with the baseline estimating process, the CBO’s internal baseline forecast contains a great deal of detail that is of significant use to both CBO and JCT revenue estimators but is never released, even to the House and Senate Budget Committees. It should be released, however, as a means of further enhancing the credibility of the CBO’s estimates.

There is little downside for the CBO in making its baseline estimating process relatively transparent, because its baseline estimates are unlikely to come under political pressures from lobbyists and special-interest representatives. “No one lobbies on the baseline,” a Washington think tank economist has observed.

In contrast, when the CBO makes its estimates of the costs of nontax legislation:

Lobbyists watch the process carefully, hoping to find analytic errors if a score goes against them — or to persuade analysts to adopt assumptions favorable to their cause before the analysis begins.<sup>70</sup>

<sup>70</sup>Rudolph G. Penner, “The Dynamics of Scoring: A Congressional Tale,” *The Milken Institute Review*, Third Quarter 2003, p. 28.

budget and mandate cost estimate. CBO interprets that directive to include the disclosure of the critical assumptions and analytic methodologies used to prepare the estimate. All written cost estimates include explanations of the basis of the estimate, and CBO supplies further details on request.”

<sup>68</sup>However, the CBO does not supply “further details” for the selected JCT revenue estimates that it publishes on the Web. For a discussion of this limitation, see note 153 *infra*.

<sup>69</sup>See 2 U.S.C. section 601(f). This provision originated in 1985 when Ways and Means Committee Chair Dan Rostenkowski and JCT Chief of Staff David Brockway became nervous about possible encroachment by the CBO on the traditional prerogatives of the JCT and the taxwriting committees of Congress. According to a participant in the development of the legislation, there had been “little turf battles” over estimates dealing with tax-related topics such as depreciation. To prevent such “scrambles,” Brockway wanted to solidify the JCT’s authority over the revenue estimating process. According to observers, enactment of legislation confirming the JCT’s role in the revenue estimating area was readily acquiesced in by Rudolph G. Penner, who then headed the CBO, because Penner regarded the legislation as merely ratifying the status quo. However, Penner’s staff was dismayed, and Brockway reportedly regarded the legislation’s enactment as a significant victory.

Rudolph G. Penner, a former CBO director and the author of the article just quoted, continues:

More than once I had to hold the phone away from my ear when listening to a member of Congress who claimed that our scoring methods had destroyed some pet initiative that, but for our stupidity, would save the nation.

The CBO achieves transparency through its Web site and its publications. Those publications include annual analyses of the president's budget proposals and biennial projections of revenues by source. Also, the CBO produces occasional special analyses, explaining how it arrives at its estimates.

An example of the latter is the CBO's July 2003 paper entitled *How CBO Analyzed the Macroeconomic Effects of the President's Budget*.<sup>71</sup> That paper focused on the president's proposals to reduce the double taxation of dividends, expand tax-free savings accounts, and extend repeal of the estate tax. It described and compared the four models used by CBO in its estimating effort, listed the assumptions made when applying the models, and described some of the difficulties encountered.

## II. The Arguments Pro and Con

### A. The Arguments for Greater Transparency

As a theoretical matter, the case for greater transparency in the revenue estimating process is nearly overwhelming. This section reviews the arguments in favor of transparency. There are also some serious practical problems that have to be considered and dealt with if greater transparency is to become a reality. Those are discussed in the next section of this report.

Theory and practice aside, it is clear that the same degree of transparency achieved by the CBO estimating staff when scoring nontax legislation should also be achievable by the Treasury and JCT estimating staffs when dealing with tax bills. The transparency issues presented by estimates for the two types of legislation are similar. Furthermore, the CBO's nontax, cost-estimating workload is roughly comparable to the tax-estimating workloads of Treasury or the JCT.<sup>72</sup> Hence, the CBO's transparency practices should probably constitute an irreducible minimum for Treasury and the JCT to emulate.

It is important to decide *how much* transparency is desirable and why. If the goal is merely to keep the public generally informed about revenue estimating practices, the four elements listed earlier<sup>73</sup> under "Generalized

Transparency" may suffice. But if the goal is to make possible near-replication by private parties of government estimates, substantially all components of the transparency concept must be implemented.

The basic arguments favoring greater transparency in the revenue estimating process are as follows:

#### *Argument 1: Self-Government*

In a democracy, citizen access to information is fundamental. Without adequate information, self-government is impossible.

Tax policy judgments in the executive branch and Congress are influenced, often decisively, by revenue estimates and distributional analyses. A democratic approach to the tax policy process requires that the decisive elements in the process, including revenue estimates, be open to public understanding and scrutiny.

Congress mandates transparency for the budget and cost information estimated by the CBO. Tax estimates are no less interesting and important in the public debate, and they should be equally open to the public.

#### *Argument 2: Credibility*

The usefulness of a revenue estimate is severely limited if the estimate is regarded as questionable by those who must make policy on the basis of the estimate. Revenue estimates have been challenged by critics for many decades. However, 25 or more years ago, they were more likely to be accepted without much question in the course of political debate simply because they came from an official source that was generally deemed to be reliable. Revenue estimates require more supporting information to be credible today, at a time when the survival of proposed legislation often depends on the assumptions and conclusions of Treasury or JCT estimators.

Revenue estimates will be more credible to decision-makers, the press, and the public if they describe not only the general methods used to create estimates but also the specific assumptions, procedures, and data used to produce a given estimate. Disclosure of those underpinnings of a revenue estimate will significantly increase the credibility of the estimate itself, and that in turn will facilitate the legislative process by lessening or eliminating distrust of the estimating process.

If revenue estimates are not based on publicly available facts, it becomes all too easy to claim that they are a result of political considerations rather than careful analysis. In that environment, revenue estimators can easily become pawns in a political struggle, and there is danger that the revenue estimating process will be improperly denigrated.

"The credibility of a revenue estimate," a former Joint Committee chief of staff recently stated, "is built by transparency. Transparency helps dispel the idea that revenue estimates are the product of some sort of 'black box' or that they are produced by throwing darts at a dartboard."

Also, when estimates are not credible, political debate is likely to focus on the numbers — on the relative merits of conflicting estimates — rather than on policy. Formulating tax policy is difficult enough without the further complication of dueling revenue estimates. Debates about revenue estimates can sometimes be smoke screens

<sup>71</sup>The CBO paper is available on the Web at <http://www.cbo.gov/ftpdoc.cfm?index=4454&type=1>.

<sup>72</sup>In addition to reports, analyses, and baseline economic forecasting work, the CBO is required to develop a cost estimate for virtually every bill reported by a congressional committee (other than bills involving income, excise, payroll, and estate and gift taxes, which are estimated by the JCT). It also prepares estimates for bills in the early stages of drafting. Also, it prepares cost and revenue estimates for tariff proposals, offsets, and user-fee proposals.

<sup>73</sup>See *supra*, p. 331.



for policy differences. However, by minimizing the mystery surrounding revenue estimates, transparency can make it easier to move beyond doubts about the numbers and focus instead on the underlying tax policy issues.

Of course, like weather forecasts, revenue estimates will never be fully credible. The process of forecasting is premised on the realization that actual events are likely to turn out differently than originally forecast. The real issues in forecasting are how far off the mark estimates turn out to be, whether the degree of error can be reduced, and what steps can be taken to buttress the credibility of future forecasts.

Some Treasury observers argue that the availability of information about the underpinnings of a particular estimate will facilitate the creation of competing estimates on the same subject, thus weakening the credibility of the first estimate. That is certainly true if the underpinnings of the first estimate turn out to be weak, but openness, competition, and honest debate are not likely to weaken a sound estimate. In fact, competition can strengthen an estimate, especially if its authors revise and improve it in response to competing estimates.

**By minimizing the mystery surrounding revenue estimates, transparency can make it easier to move beyond doubts about the numbers and focus instead on the underlying tax policy issues.**

Hence, although promoting transparency in the revenue estimating process may not strike tax policymakers as a priority issue, greater transparency is in their interest. Transparency will make more credible the figures they use to formulate policy, and that will improve the quality of the policy debate by focusing it on the actual tax changes being proposed rather than on the methods used to estimate costs and revenues.

#### **Argument 3: Improving Consistency and Quality**

Current and former revenue estimators state that the revenue estimating staffs at Treasury and the JCT prepare relatively little internal documentation of their estimates, other than their own notes, even in the case of major tax legislation.<sup>74</sup> They also state that documentation practices vary from one estimator to another.<sup>75</sup> Those facts mean that internal review is difficult or impossible and that

<sup>74</sup>Documentation of estimates relating to major legislation is obviously important for a variety of reasons, including internal review, but the time pressures encountered when preparing major legislation commonly make it difficult to prepare adequate documentation. That is another instance in which adequate staffing would improve the estimating process.

<sup>75</sup>According to current and former estimators interviewed for this report, some estimators routinely prepare fairly detailed documentation, while others are less thorough. Workloads also affect the amount of documentation that can be prepared. As mentioned in note 74, when workloads are heavy, documentation suffers.

consistency from one estimate to another is hard to achieve. It also means that quality control is generally lacking.

Greater transparency would make that situation clear (which is one of the reasons why greater transparency is likely to be resisted). By making the situation clear, greater transparency would produce pressure for greater consistency in estimating. It would also facilitate development of meaningful quality controls.

To improve accuracy and consistency, government revenue estimators should routinely prepare technical estimating memorandums regarding their estimates, or at least each significant estimate, and those memorandums should be made publicly available. Former government estimators now in the private sector routinely prepare memorandums of that sort for submission to clients and government agencies. They view that as a necessary part of their service, because they know their estimates will be more credible if they are carefully documented.

Indeed, the documentation process may improve estimates by uncovering overlooked errors in estimating methods. Technical memorandums have quality-control value in their own right because preparing documentation, by itself, helps to correct errors, even if the documentation is used only for internal review. Also, documentation can provide a basis for supervision to enhance consistency and quality.

#### **Argument 4: Facilitating Public Comment**

Greater transparency will facilitate critiques by outside parties of the techniques used to prepare revenue estimates. Many of those critiques will come, of course, from self-interested private parties and their lobbyists, who will point out the faults, but not the strengths, of estimates that affect them. But even one-sided critiques are likely to contain elements of truth, and not all the critiques will come from interested parties; some will come from disinterested parties including think tanks, universities, and independent scholars.

The situation is similar to the case of proposed tax regulations, which are published in the *Federal Register* in response to the mandate of the Administrative Procedure Act (APA).<sup>76</sup> Under APA procedures, most comments come from interested parties and are appropriately discounted for bias by the individuals in charge of the regulations project. Regulators nevertheless glean from them the wisdom they contain, which is sometimes considerable. Valuable comments also come from disinterested agencies and individuals seeking to serve the public by improving the proposals.

Public critiques of regulations — including self-interested critiques — seldom make regulations worse, and they often make them better. There is no reason to think the situation would be different for revenue estimates.

#### **Argument 5: Accountability**

<sup>76</sup>Publication of regulatory rules in the *Federal Register* is required by 5 U.S.C. section 552(a)(1).

Oversight and accountability are important to any institution. Without accountability, standards slip and there is little pressure for improvement.

As outlined earlier, there is not much internal oversight, and almost no external oversight, over the revenue estimating processes at Treasury and the JCT. Also, there is anecdotal evidence that at Treasury and the JCT, careful documentation of estimates is infrequent, consistency is difficult to maintain, and quality-control measures are nonexistent. Greater transparency would help to put those fears to rest, assuming they are ill-founded; and if those fears were correct, enhanced transparency would create pressure for improvement.

Are there agencies that could peer review the Treasury and Joint Committee's estimating work, assuming it were more open to the public? Thirty years ago, the answer to that question was probably "no";<sup>77</sup> today, however, there are several answers. Two of the major accounting firms now have significant revenue estimating capabilities<sup>78</sup> and the others have expertise in the area. However, not much of that capability would be diverted to a critique of Treasury and JCT estimating efforts unless those efforts happened to run counter to a client's interests.

More important, several nonprofit groups have both a strong interest in the estimating process and a fair amount of estimating capability. Those groups include the Heritage Foundation, the Urban-Brookings Tax Policy Center, the National Bureau of Economic Research, the American Enterprise Institute, Citizens for Tax Justice, and the Center for Budget and Policy Priorities. They span the political spectrum and are therefore likely to enrich the estimating debate with opposing viewpoints. Additional groups will get involved in the revenue estimating debate if increased availability of information makes that involvement possible.

Both the Government Accountability Office (GAO, formerly known as the General Accounting Office) and the National Science Foundation also have the capability to provide oversight and peer review of the revenue estimating process at Treasury and the JCT.

Further, if there were greater transparency in the estimating process, both Treasury and the JCT could more readily critique one another's estimates. With a few rare exceptions, that is something that has not occurred with much frequency in recent years. According to government sources, relations between the JCT and Treasury in the relatively recent past have at times been icy, but an ongoing dialogue between the two revenue estimating staffs nevertheless continues. Greater estimating trans-

parency might facilitate growth of that cooperative dialogue between the two agencies to the benefit of both.

Also, greater transparency will enable the private sector to improve the revenue estimates that are made for specific pieces of legislation by contributing private iterations of the original government estimates. That might initially increase government estimators' workload by making it necessary to justify or revise their original estimates, but it would also help to spur debate and thus contribute to the improvement of estimating techniques.

#### *Argument 6: Improving the Science*

There is now almost no way to suggest improvements in the Treasury and JCT revenue estimating processes because almost no one has enough information about those processes to comment on them usefully.<sup>79</sup> Academics and others cannot critique the models used; the press and the public cannot comment on the validity of estimating assumptions; and limitations and deficiencies in the data cannot be pointed out and perhaps corrected.

Greater transparency would foster discussion of what needs to be done to improve the revenue estimating process and make its results more accurate. That discussion would benefit both the public and the estimating agencies themselves.

#### *Argument 7: Promoting Research*

In the words of a senior Treasury economist, university economics departments "don't teach revenue estimating." Furthermore, he said, only a few prominent academics have an interest in the subject.

It is difficult to teach, or to have an interest in, a subject about which very little is known. Greater transparency for the revenue estimating process could change that situation. For the first time, there would be a body of information that could be analyzed and discussed in class or become the basis for scholarly articles. Revenue estimating issues could take their place as part of the public-finance curriculum. The resulting discussion and debate could improve the revenue estimating process.

### **B. The Arguments Against Increased Transparency**

There are four main arguments, and a few minor arguments, against increased transparency for the revenue estimating process. They are listed below in descending order of importance.

#### *Argument 1: Destroying What One Seeks to Reveal*

Proponents of greater transparency frequently assume that disclosure efforts will cause more information to reach the public, but that is not always the case. Thirty years of tax-related experience under the FOIA makes it clear that court-ordered disclosure of a particular type of document often leads tax agencies to stop producing that

<sup>77</sup>Contrary to the suggestion in the text, a Treasury source has stated that more than 60 years ago, one of PricewaterhouseCoopers' predecessor firms provided a critique of Treasury revenue estimates with respect to a then-current proposal to integrate the corporate and personal income taxes. That proposal evolved during congressional consideration of what became the personal holding company tax and the accumulated earnings tax. For further information, see the Tax History Project Web site at <http://www.taxhistory.org>.

<sup>78</sup>KPMG and Deloitte no longer have formal revenue estimating staffs, but both PricewaterhouseCoopers and Ernst & Young do.

<sup>79</sup>A group such as the JCT's Blue Ribbon Advisory Panel could perform this function, but — as explained on p. 338, *supra* — that group has not been very active. Moreover, when the panel has met, it has focused entirely on questions relating to dynamic revenue estimating rather than on improvement of the normal revenue estimating process. Also, to be effective in an oversight role, the panel would need considerably more access to information than it currently has.

type of document.<sup>80</sup> That is especially the case when agencies lack the staff or the mandate to promote disclosure. In those cases, disclosure efforts can effectively destroy what they seek to reveal.

Revenue estimating documents could be a case in point. For example, it is now common practice for an estimator at Treasury or the JCT to note the assumptions used when making an estimate. The estimator's notes may also include a list of data sources. If lists of assumptions and data sources are put into the public domain, estimators may simply stop preparing them. Or they may list only the most reliable assumptions and sources, omitting the rest. If that happens, disclosure efforts will have curtailed or destroyed what they sought to reveal.

That perverse result could be mitigated in various ways. If the agency is committed to full disclosure and realizes the benefits of disclosure both to the estimating process and the agency, transparency efforts may succeed. So too, if the agency operates under a statutory or other disclosure mandate (as does the CBO), disclosure is likely to be regarded as part of the agency's job, and disclosure initiatives will have a greater chance of being adequately funded and staffed.

However, in the absence of careful planning to avoid or mitigate the tendency of disclosure to destroy what it reveals, greater transparency for the revenue estimating process could produce a disaster rather than a victory for public participation and the democratic process.

### *Argument 2: Politicization*

Revenue estimators are currently the vestal virgins of the tax legislative process. Traditionally, policymakers have sought to shield estimators from the pressures of politics so that the revenue figures they produce will have unassailable scientific authority.<sup>81</sup> In that scenario, politicians are seen as unwanted interlopers in sacred precincts, eager to "cook the books" by manipulating

assumptions and data sources. Secrecy is believed to protect the estimating process from these pressures.<sup>82</sup>

And perhaps it has. There is no recorded instance in which a Treasury or JCT revenue estimator has accused his superiors of forcing him to accept estimating assumptions or methods with which he did not agree.

Nevertheless, the political pressures are persistent and real. One former Treasury official described how he seemed to "spend half my time" shielding the revenue estimators on his staff from pressures brought to bear by Congress and his own administration. So it is hard to believe that the secrecy dike designed to protect estimators from political pressures never springs a leak.<sup>83</sup>

Fear of politicization has led to the physical and social isolation of the revenue estimating staffs from other tax policy staffs at the JCT and Treasury. As a former Treasury estimator put it, "A trade-off has been made at both JCT and Treasury to 'protect the revenue estimator,' which has had the partially intended effect of making the estimation process more secretive, and the staffs isolated and less accountable to their peers (but not less accountable to politicians and political appointees)." "The current separation of revenue estimating from public tax policy analysis," he continued, "has prevented a lot of good economic analysis from being included in the public policy debate." He concluded that the "separation of the revenue estimating staff from the policy economists at both JCT and Treasury, and their general isolation from the rest of the economic and public policy community, has been detrimental to the policy debate, the tax staffs, and the individual revenue estimators themselves."

Disclosure advocates should recognize the genuineness of agency concerns that greater transparency for the revenue estimating process will politicize it. At a minimum, those advocates need to consider how to protect the integrity of the process even though it becomes more open to scrutiny by those who seek to influence it. Also, protection for the estimators themselves, both from unwelcome publicity and from undue political pressure, is very important.

<sup>80</sup>The IRS has become particularly adept at discontinuing or renaming documents that it has been ordered to reveal, thus avoiding court mandates under the FOIA. Examples of discontinued or renamed documents include general counsel memorandums (replaced by secret legal memorandums) and technical advice memorandums (replaced by secret field service advice memorandums (FSAs), which, in turn, were discontinued in favor of other forms of secret guidance when the courts ruled that FSAs must be made public). For a discussion of the discontinuance-renaming issue, see *Tax Analysts v. Internal Revenue Service*, 326 U.S. App. D.C. 53, 117 F3d 607, at 616 (D.C. Cir. 1997).

<sup>81</sup>For example, according to Bernard A. Schmitt, the JTC's Deputy Chief of Staff and long-time director of the committee's revenue estimating activities, the physical location of the JCT's revenue estimators in a building isolated from Congress and the rest of the JCT staff was chosen to insulate the estimators from partisan pressures. See "New JCT Advisory Board Formed to Improve Revenue-Estimating Process," *Tax Notes*, May 1, 1989, p. 523. (Space pressures in the Longworth House Office Building are another obvious reason for locating the JCT estimators elsewhere, as is the desire to facilitate coordination with the CBO, whose staff is currently located near the JCT estimators.)

<sup>82</sup>However, secrecy can have adverse consequences for the tax policy process. As one former Treasury revenue estimator put it, "The desire to isolate the revenue estimating staff from the political process has resulted . . . in non-participation by the estimating staffs in meaningful tax policy discussions, including discussions that might lead to improvement of estimating data, methodology, and modeling. More frequent public discussion of the revenue estimating process would be likely to result in improvements in the estimators' methodologies and modeling, since by its nature economics is a 'social,' not a private science."

<sup>83</sup>According to anecdotal evidence from a small number of former estimators, Treasury and JCT estimators have, in rare instances, been required by political pressures to accept assumptions or estimates with which they did not agree. As a former estimator put it, "Due to the secrecy, we don't know the extent to which the [revenue estimating] process has already been politicized. We trust that the current revenue estimating staffs are acting as true professionals, which I believe they are, but when was the last time a revenue estimator publicly resigned to protect his or her independence from political interference?"



The example of the CBO is instructive. It has had a succession of strong, capable directors willing to protect their estimating staffs from pressures brought to bear by outsiders.<sup>84</sup> The same is true at both Treasury and the Joint Committee, so that essential bulwark against politicization is in place. Written rules and practices, modeled on those in place at the CBO,<sup>85</sup> would help to reinforce and solidify the protections provided by strong tax administrators.

#### *Argument 3: Lack of Staff Resources*

Enhancing the transparency of the revenue estimating process is a labor-intensive exercise. At bottom, it is no different from any other kind of publishing. Publishing typically involves writing, editing, revising, and classifying information and creating formats and indexing tools to facilitate access to that information by interested users. Enhancing transparency is not a job that can be done by estimating staffs that are already beleaguered and overworked. Transparency requires more staff time, more writing, more review, and a set of skills not commonly taught in economics classes. Also, staff time will have to be spent evaluating and responding to comments from outside groups.

Just how overworked are the Treasury and JCT revenue estimating staffs? And how much labor would be required to bring their work into the public domain? The short answer to both those questions is that no one really knows, not even the agencies themselves.

Accurate statistics are unavailable partly because there is no agreement about what constitutes a “revenue estimate.” For example:

- Is guidance by an estimator in the course of a telephone call to be counted as a “revenue estimate”?
- Is an in-depth estimate requiring hundreds of hours of staff time to be given the same weight as an “easy” estimate that can be dashed off in the course of an afternoon?
- If an estimate regarding a specific tax proposal is rerun six successive times on the basis of six variations in a crucial assumption, does that count as one estimate or six estimates?
- If an estimate is redone multiple times to take into account successive changes in the language of a legislative proposal, does that constitute one estimate or many estimates?
- If a prior revenue estimate is rerun against an updated macroeconomic baseline<sup>86</sup> without other changes, does that count as one estimate or two?

Because answers to those questions are essentially arbitrary, it is difficult to produce meaningful workload statistics regarding the revenue estimating process.

<sup>84</sup>Note, for example, the comments by former CBO Director Rudolph G. Penner on p. 341, *supra*.

<sup>85</sup>The CBO’s policies are available on the Web at <http://www.cbo.gov/Policies.cfm>.

<sup>86</sup>Treasury’s estimating baseline is updated every two months to take into account recent economic developments. Crucial estimates regarding pending legislative proposals may therefore be updated again and again throughout the year as the baseline changes.

However, no matter how the term “revenue estimate” is defined, it is clear that the number of estimates prepared by the Treasury and JCT staffs has increased steadily over the years.<sup>87</sup> It is also clear that both staffs are subjected to unmanageable time pressures during the closing days of a congressional session and (in the case of Treasury) during the preparation of the annual federal budget. But periods when time pressures are unmanageable are juxtaposed with periods of calm after a legislative session concludes (or, in Treasury’s case, after the president submits his budget to Congress). So again, workload anecdotes do not reveal the whole story.

When asked, Treasury states that full transparency for revenue estimates would require it to approximately double the size of its existing revenue estimating staff. That would involve increasing that staff from 13 to 26 professionals, plus support staff. That estimate sounds unrealistically high, particularly in light of the CBO’s experience in implementing transparency initiatives. Nor is it clear how much of that additional staff would be needed to do work — such as quality control and documentation of estimates — that ought to be done already (but often is not).

However, suppose Treasury is right and that full transparency for its revenue estimating process would require it to double the size of its estimating staff. That would cost \$2 million to \$4 million per year. That seems a relatively small price to pay, given the crucial role that revenue estimates play in the tax legislative process.

In summary, advocates of transparency need to recognize that enhancing the transparency of the Treasury and JCT revenue estimating processes is going to require additional staff resources. The benefits of greater transparency, though intangible, are likely to be well worth those additional costs.

#### *Argument 4: Confidentiality of Returns*

A major objection to disclosure of the data used to make revenue estimates (as contrasted with merely listing data sources) is that the Internal Revenue Code strictly prohibits revealing tax return data and imposes both civil and criminal penalties for violations of that rule.<sup>88</sup> Because Treasury and JCT revenue estimates rely heavily on tax return data, the prohibition on disclosure of return information makes it impossible to release the precise data used to make Treasury and JCT estimates.

<sup>87</sup>JCT representatives have stated in recent speeches that the committee receives nearly 5,000 requests a year for estimates. If all of those were answered, the committee would find itself processing an average of 20 responses each work day, which would constitute a truly extraordinary workload. The actual number of estimates prepared by the JCT in response to requests must therefore be significantly less than 5,000. Treasury does not tabulate estimating requests or responses, but an official familiar with Treasury’s estimating activities states that the number of estimates prepared each year has “gotta be in the thousands.”

<sup>88</sup>Section 7213(a)(1)-(3) imposes a fine of up to \$5,000, imprisonment for up to five years, or both for unauthorized disclosure of tax return information. In addition, sections 7431 and 7435 provide civil damages for unauthorized tax information disclosures.

For example, there is probably no way in which the data underlying so-called rifle-shot tax legislation — that is, legislation designed to benefit only one (or at most a few) individuals or firms — could ever be released. Release of the data underlying those estimates would almost certainly jeopardize taxpayer confidentiality. However, most revenue estimates relate to broad-based legislation, not to rifle shots.

Fortunately, the Statistics of Income Division within the IRS Office of Research, Analysis, and Statistics prepares a special compilation of tax data known as the public-use file, which contains return data that have been appropriately homogenized to protect taxpayer privacy. Those are *not* precisely the same data used by Treasury and the JCT when making estimates, but they are as similar as possible given the need to preserve tax return privacy and confidentiality.

The availability of the public-use file has been an essential element in development of private accounting firm and think-tank revenue estimating capabilities over the past 30 years.<sup>89</sup> Also, the public-use file provides an example of how government efforts to enhance transparency can support and spur helpful private-sector initiatives in the revenue estimating area.

### **There are serious problems with the public-use file.**

However, there are serious problems with the public-use file.

First and most important, the public-use file contains only individual tax return data. A public-use file containing at least a limited amount of small and midsize business return data (both corporate and noncorporate) should also be made available. That suggestion is discussed later in this report.

Funding for production of the IRS public-use file is currently very limited. More resources are essential, especially if a business return public-use file is to be produced. It is up to Treasury to request those resources.

Lack of timeliness is another serious problem. In recent years, there have been two- to three-year delays in production of the public-use file.<sup>90</sup> Some of those delays

were apparently attributable to lack of publication funds. Publication has also been delayed by IRS concerns that the growth of private-sector computational power, the increasing availability of cross-matching financial data, and developments in record-linking mathematical models might make it possible to obtain individual tax return information from the public-use file, especially in the case of high-income individuals.

The problems associated with delays in production of the public-use file are compounded when government revenue estimators base their estimates on updated or corrected public economic data that have not yet been published by the compiling agency. Use of not-yet-published data is entirely appropriate when those data are available to government estimators, because the goal is to produce the most accurate possible revenue estimates. However, to avoid public confusion, use of not-yet-published data should be mentioned in any estimating memorandums that accompany revenue estimates.

IRS concerns about possible disclosure of individual tax return information in the public-use file have been made even more acute by the growing use of “longitudinal” data — data covering more than a single year — in the revenue estimating process. Using longitudinal data helps to make revenue estimates more accurate than those produced using only annual, cross-sectional data.

However, the availability of longitudinal panel data produces a concentration of information for one individual, and thus makes it easier to identify individual taxpayers. That fact will make it increasingly difficult to disclosure-proof the public-use file if longitudinal data are included, as they should be.

Those concerns have led the IRS Statistics of Income Division to hire outside contractors to improve the “disclosure-proofing” of the public-use file. Release of the file was significantly delayed while the contractors finished their work. The IRS needs to prevent those delays from recurring.

The public-use file also omits data that could be included without jeopardizing taxpayer privacy, such as age distribution data. Private estimators are unhappy about those omissions, which seem unjustified on privacy or other grounds.

### **Argument 5: A Reduced Role for Judgment**

Good professional judgment is a crucial, appropriate, and required component of revenue estimating. It is what makes revenue estimating an art rather than a science.<sup>91</sup> Opponents of disclosure fear that enhanced transparency would make estimators less free to exercise independent

<sup>89</sup>Release of statistical material such as the public-use file is authorized by section 6103(b)(2), which states that the term “return information” does not include “data in a form which cannot be associated with, or otherwise identify, directly or indirectly, a particular taxpayer.”

<sup>90</sup>Since 1995, according to the IRS, release of the public-use file has occurred, on average, about 32 months after the close of the filing period for a given tax year. For example, public-use file data for 1999 did not become available until February 2003 — 26 months after the close of the filing period. The public file release dates and delays for earlier tax years are as follows: 1998, September 2002 — 33 months delay; 1997, February 2002 — 38 months delay; 1996, February 2001 — 38 months delay; and 1995, April 1999 — 27 months delay. In contrast, statistics of income data for a given tax year become available about six months after the close of the filing period for that year. For example, according to the IRS, statistics of income data for tax

(Footnote continued in next column.)

year 1999 became available in June 2001 — about six months after the close of the filing period.

<sup>91</sup>Perhaps the science now outweighs the art. According to former JCT Chief of Staff Ronald A. Pearlman, “It has been said that revenue estimating is as much an art as it is a science. Certainly all would agree that it is not an exact science. But economic theory and econometric methods are much more sophisticated than most of us realize. Revenue estimating assuredly is much more than an art.” See the “Conclusion” in section VI of JCT, *Statement of Ronald A. Pearlman, Chief of Staff, Joint Committee on Taxation, Before the Senate Committee on Finance* (JCX-3-89), March 14, 1989, Doc 89-2024, 89 TNT 59-10.

professional judgment, especially in cases in which they cannot readily document the basis for their beliefs and assumptions. Instead, they fear, estimators will tend to base their estimates on more easily justified mechanical standards.

Typically, the judgmental part of a revenue estimate relates to the behavioral component (the “what will the consequences be” part) rather than the static component (the “what does one deduce from the current data” part). Professional judgment is necessarily involved when estimating the likely behavioral response to a tax change. Sometimes judgment is required because little or no empirical evidence is available. In other instances, ample evidence is available,<sup>92</sup> but judgment is required to interpret it.

In those cases, adopting a mechanical alternative to the use of judgment is simply not feasible. There is nothing wrong with the use of judgment in those instances, provided the judgment is disclosed and explained. Government regulators use judgment all the time. Making behavioral judgments public will assure greater consistency across revenue estimates with respect to behavioral responses, and that is all to the good. If the judgment is sound, it will be able to withstand public scrutiny.

#### **Argument 6: Delay**

Greater transparency will inevitably slow the production of revenue estimates, both because each step in a transparent estimating process is likely to be documented with care (rather than with informal notes or not at all) and because additional review is likely to be given to publicly released revenue estimates and documentation. Providing additional staff will ameliorate but not necessarily resolve that problem.

Some delay may have to be regarded as the price of additional transparency. Policymakers will have to plan accordingly. Offsetting that cost, however, is a clear benefit: Revenue estimates, once they are released, will be more accurate because they will have been reviewed with care so they can withstand the light of day.

#### **Argument 7: Confusing the Debate**

Opponents of transparency for the revenue estimating process argue that revealing the underpinnings for a revenue estimate might distract attention from the proposal itself and transform the debate on the proposal into an argument over revenue estimating methods.

If there are grounds for suspecting that a revenue estimate is unsound, that might occur. However, if a

revenue estimate is questioned, is the ensuing debate a good thing or a bad thing? For many years, legislators, the press, and the public have been accustomed to accepting revenue estimates as not-to-be-questioned “givens.” As a consequence, some serious errors and bad judgments have doubtless been obscured from view. Why is it inappropriate, at last, to provide a basis for questioning the process?

There will certainly be cases in which the tax debate is distracted by a dispute over estimating procedures. In some cases, we may be confronted with several differing revenue estimates, each from a different source. But that is healthy, not bad.

As a result of honest public debate, adjustments will be made in the estimating process, procedures will become accepted and far better understood, and consensus will emerge. What will disappear is pervasive suspicion about the validity of the numbers, the possible biases of the estimators, and the rationality of the estimating process. Bloodying one’s nose in an occasional dispute over numbers is a small price to pay for long-term certainty about the integrity of the revenue estimating process. As public confidence in the quality of revenue estimates grows, the debate can again focus on the merits of the tax policy issues at hand.

#### **Argument 8: Loss of Mystique**

Thirty or more years ago, revenue estimates had very nearly the authority of utterances from the ancient oracle at Delphi, at least to outsiders.<sup>93</sup> Like the utterances of the oracle, estimates resulted from a mysterious and secretive process known only to a few. Estimates could seldom be challenged, and few dared to try.

Today, much of this mystique has been lost, partly as a result of the spread of revenue estimating capability in the private sector and slowly growing public knowledge about the nuts and bolts of the estimating process. Opponents of transparency fear a further loss of authority if even more information is revealed about the Treasury and JCT estimating processes. For example, at an Airlie House conference in 1988, David Brockway, who was then chief of staff of the Joint Committee, told the conferees:

[W]e generally attempt to avoid laying out what our estimating model is, and how we’ve reached our conclusions, so that people can’t come back and challenge those aspects of the estimate that lead to results they don’t like.<sup>94</sup>

The short answer to those concerns is that, in a democracy, authority should be earned rather than based on one’s position or on privileged access to information. In the case of revenue estimating, this means that the authority of a revenue estimate should derive from the

<sup>92</sup>Empirical evidence about behavioral responses can grow over time. For example, assumptions about the likely behavioral changes induced by a change in capital gains tax rates have differed quite widely in the past. See the discussion *supra* on pp. 334-335, regarding the 1989-1990 dispute between Treasury and JCT estimators over the likely behavioral effects of the gains tax changes proposed in that year. Since that time, however, Congress has varied gains tax rates with such frequency that there is now a firmer empirical basis for estimating the behavioral effects of those changes. For a further discussion of the capital gains issue, see section III(B)(1) of JCT, *Methodology and Issues in the Revenue Estimating Process*, JCX-2-95, January 23, 1995, section V, Doc 95-1118, 95 TNT 15-15.

<sup>93</sup>However, there was vigorous internal debate among the revenue estimators themselves, according to government observers active in the estimating process at the time, and vigorous internal debate continues to characterize the process.

<sup>94</sup>The full text of the conference summary is set forth in *Tax Notes*, June 27, 1988, starting at p. 1581. Brockway’s comments appear at p. 1582. For similar sentiments expressed by Treasury, see the third bullet in the quoted text on p. 333, *supra*.



reasonableness of the assumptions on which an estimate is based, the comprehensiveness and recentness of the data used, and the clarity of the reasoning applied to produce the estimate.

Regrettably, however, lack of transparency in the Treasury and JCT estimating processes makes it impossible at present for those agencies to rely on these legitimate sources of authority. Meanwhile, the deference traditionally accorded to their pronouncements continues to erode.

### III. Lessons From Others

#### A. Lessons From the States

At the state level, revenue and cost estimates play a central, crucial role in the legislative process. That role is even more important than at the federal level because substantially all states have a balanced budget requirement of some sort. Without accurate estimates of likely revenues and expenditures, it is not possible to know whether balance has been achieved. In effect, revenue forecasts establish the allowable parameters of annual state budgets.

Given those facts, "The federal government has a lot to learn [about revenue estimating] from the states," according to James Francis, director of tax research for the Florida Department of Revenue and a member of the JCT's 1989 advisory board.<sup>95</sup> "We have the ultimate fiscal constraint — a balanced budget with no fudging," Francis said. "Thus we have been facing the problem of revenue-driven tax legislation for a long time."

Because almost all states require balanced budgets, it is natural for disputes to arise over the accuracy of state-level revenue estimates and the reliability of the process that produces them. Some states have found themselves embroiled in budget disputes that are rooted in numerical duels over estimating assumptions and methods. Those disputes have sometimes slowed and disrupted the legislative process. In contrast, when state legislators and executive branch officials adopt similar estimating methods and "use the same numbers," that fact "greatly aids the legislative process."<sup>96</sup>

**1. Consensus revenue estimating.** To deal with disputes over revenue estimates, about half the states<sup>97</sup> have adopted what is known as "consensus revenue estimating." The consensus estimating process involves a concerted effort, before a legislative session, to resolve disputes over the likely revenue and expenditure figures

that will be included in an upcoming state budget.<sup>98</sup> The Council of State Governments describes the process in the following words:

By far the most interesting trend in recent years is the movement by states away from forecasting dominated by the executive or legislative branch to a method known as "consensus estimating." . . . Consensus revenue estimating involves participants from the legislative and executive branch, as well as representatives of business and academia. Through discussion and analysis, these members must come to unanimous agreement on the estimates for the coming fiscal year. While no forecasting method is ever 100 percent accurate, studies show that on average a consensus forecast will be more accurate than any of the individual forecasts that compose the consensus.<sup>99</sup>

The consensus estimating process almost always includes representatives of the state treasury or finance commissioner as well as legislators with budget and tax responsibilities. It may also include state university representatives,<sup>100</sup> especially if the university assists state agencies in the revenue estimating process. It may also include representatives of private industry and the press.

In some cases, the consensus process is quite informal. Legislative and executive branch officials simply get together for a detailed discussion a few weeks before the opening of a legislative session.<sup>101</sup> That gives them a chance to compare their approaches to current estimating

<sup>98</sup>The origins of the consensus revenue estimating process are obscure. Florida appears to have been the first state to make use of a full-blown consensus estimating approach. Before 1969 all revenue forecasting was done in the Florida Governor's Office. Consensus estimating developed after the Florida Legislature began in the 1960s to create a nonpartisan professional staff to assist with fiscal and other estimating issues. Starting in 1979-1980, the governor's staff and the legislature's professional staff began to meet at designated times of the year to reconcile their estimates. Consensus revenue estimating evolved as "a custom and practice" out of those meetings. Later, the consensus estimating procedure was codified. Correspondence with James Zingale, executive director, Florida Department of Revenue, August 29 and September 8, 2003. Other states, particularly Michigan, were not far behind Florida in developing consensus estimating. Interviews with Mark Haas, chief operating officer, Michigan State Pension Agency, August 2003, and Patricia Woodworth, now chief financial officer, Art Institute of Chicago, September 5, 2003.

<sup>99</sup>Council of State Governments, State Policy Innovations Group, "Revenue Forecasting and Estimating in the States," reprinted in *State Tax Notes*, September 28, 1992, p. 449.

<sup>100</sup>See Figure 2, "State Offices Participating in Revenue Forecasting," *id.*

<sup>101</sup>Something similar occurs at the federal level when representatives of the Office of Management and Budget, Council of Economic Advisers, and Treasury Department meet to agree on a baseline macroeconomic forecast for the executive branch. But, unlike state-level consensus estimating, representatives of the legislative branch do not participate in those meetings. Nor is there any opportunity for public participation in those meetings.

<sup>95</sup>The Francis quotations are from "New JCT Advisory Board Formed to Improve Revenue-Estimating Process," *Tax Notes*, May 1, 1989, p. 524.

<sup>96</sup>Interview with Jeff Guilfoyle, Michigan Department of Revenue, Office of Revenue and Tax Analysis, August 7, 2003.

<sup>97</sup>The National Association of State Budget Officers counts 24 states as using some form of "consensus forecasting." See Table G in National Association of State Budget Officers, *Budget Processes in the States*, January 2002, pp. 19-21. See also Table 7.35, "Revenue Estimating Practices," in Council of State Governments, *The Book of the States*, 2003, p. 394.

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issues, discuss their assumptions and data sources, and resolve differences in their numbers.<sup>102</sup>

Consensus estimating can also take the form of a large one- or two-day conference, with hundreds in attendance, formal papers, and press and television coverage.<sup>103</sup> It may also include a smaller conference a week or two after the main session to report the results of additional research suggested at the main conference a few days before.

Consensus estimating is an essentially public process. Its goals are to produce agreement on the basic numbers that constitutes a state's annual budget and to increase the credibility of the claim that a state's budget is actually balanced. Those goals would be much harder to achieve if budget estimates were prepared in secret. "Through openness in estimating you get credibility," according to a Florida tax official.<sup>104</sup> A senior Michigan official adds that "Doing an estimating conference publicly allows legislators to see how the forecast is done; this gives increased credibility to the numbers."<sup>105</sup>

States also estimate the costs of particular pieces of legislation, just as Treasury and the JCT do. But they do not generally do that in public, at least not for routine legislation.

However, if a major tax or spending proposal is put forward, the estimated budget effects of the proposed change will sometimes become the basis for a supplementary consensus estimating conference. Also, some states schedule extra consensus estimating conferences when a legislative session moves past a major milestone, such as adoption of the annual budget or the close of a legislative session.<sup>106</sup> Those supplementary conferences necessarily include the budget adjustments required by specific pieces of legislation. In this way, "micro-estimates" for specific legislation are subjected to indirect review by consensus estimating conferences.

<sup>102</sup>Utah provides an example of this approach to consensus revenue estimating. Interview with Mr. Tom Williams, Utah Tax Commission, August 2003.

<sup>103</sup>Florida and Michigan provide examples of this approach. For a description of the Florida consensus estimating process, see Florida Department of Revenue, Office of Research and Analysis, *Florida Tax Handbook*, 2003, pp. 21-22, available on the Web under "Reports" at <http://www.myflorida.com/edr>. For Michigan's approach, see Rebecca Ross, "Consensus Revenue Estimating: The Process," *Fiscal Forum*, House Fiscal Agency, Lansing, Michigan, April 2001.

<sup>104</sup>Interview with Christian Weiss, Chief Economist, Florida Department of Revenue, Office of Research and Analysis, August 5, 2003.

<sup>105</sup>Interview with Jeff Guilfoyle, Michigan Department of Revenue, Office of Revenue and Tax Analysis, August 7, 2003.

<sup>106</sup>In Florida regularly scheduled estimating conferences are held "at least three times a year, once in the fall to provide forecasts for the Governor's budget recommendations, once in the winter to provide final estimates for the Legislature's appropriation process, and once in the spring to adjust the winter forecast to reflect legislative changes." Also, "impact conferences" are held on an as-needed basis. Florida Department of Revenue, Office of Research and Analysis, *Florida Tax Handbook*, p. 21.

Consensus revenue estimating is not merely a process of forging a compromise between a state's executive and legislative branches. Consensus estimating is also a *public* process that enables the press, the business community, and the public to understand and get involved in making and refining revenue estimates.

The spread of consensus revenue estimating shows the usefulness of having a focused public discussion of budget numbers and estimating processes as a means of making budget estimates more accurate and building public confidence in the numbers themselves. The federal revenue estimating process would benefit from similar discussions of important estimates.

**2. Fiscal notes.** In many states, so-called fiscal notes accompany the revenue estimates provided to state legislators for specific legislative proposals. Fiscal notes vary in scope and quality from one state to another, and they are not always made available to the public. However, some states prepare excellent notes and routinely publish them.<sup>107</sup>

Fiscal notes generally provide revenue gain or loss figures, explain current law, discuss a proposed legislative change from a revenue point of view, and outline the assumptions and data sources used in estimating the gain or loss attributable to the legislation. In many respects, they resemble the cost estimates prepared and published on the Web by the CBO.<sup>108</sup>

Similar notes should be published by Treasury and the Joint Committee. State legislative sessions are usually short and intense, and state revenue estimators are often more pressed for time than their counterparts in Treasury and on the JCT. Hence, if state estimators can produce useful fiscal notes in the heat of a brief legislative session, Treasury and the JCT should be able to do so too.

## B. International Experience

During the past 20 years, many countries have moved to enhance the transparency of their forecasting systems. In most cases, however, their newly developed transparency principles have yet to be applied to revenue estimates relating to individual tax bills. This section briefly reviews the trends in international estimating transparency.

**1. Australia.** Australia's 1998 Charter of Budget Honesty Act sought to make the public "better informed about public finances" and to assure "transparency in fiscal policy."<sup>109</sup> The act requires publication before each election of a "Pre-Election Economic and Fiscal Outlook" that

<sup>107</sup>See, e.g., the fiscal notes prepared by the Minnesota Department of Revenue, available at [http://www.taxes.state.mn.us/legal\\_policy/revenue\\_analysis/revenue\\_analyses.shtml](http://www.taxes.state.mn.us/legal_policy/revenue_analysis/revenue_analyses.shtml).

<sup>108</sup>CBO estimates are available on the Web at <http://www.cbo.gov/CESearch.htm>. For a discussion of CBO cost estimates, see *supra* p. 341.

<sup>109</sup>The text of the act can be found at <http://scaleplus.law.gov.au/html/pasteact/2/3115/top.htm>. A brief explanation of the act appears at <http://www.finance.gov.au/budgetgroup/other%5Fguidance%5Fnotes/charter%5Fof%5Fbudget%5Fhonesty.html>.

includes information about the methods and assumptions used in making the forecast. It also requires a costing of national political candidates' major campaign promises. The Charter also requires "Budget Outcome" reports annually and "Intergenerational Reports" every four years.

**2. Canada.** The Canadian government undertook a review of its economic forecasting methods in 1993. Based on that study, the government opened up its budget and forecasting processes. The primary aims were to restore credibility to the budget process, gain acceptance by financial commentators, and shift the debate from the forecasting methods to the policy issues.<sup>110</sup>

**3. Denmark.** Statistics Denmark, the national statistics bureau, makes its economic forecast model available to anyone. The annual budget includes spreadsheets with information about the assumptions used in making the relevant baseline estimates.<sup>111</sup>

**4. Germany.** Revenue forecasts in Germany are reviewed by the Working Party on Tax Revenue Forecasting, which advises the Federal Ministry of Finance. Six private-sector economic research institutes are included in the Working Party. The Working Party's procedures somewhat resemble the consensus revenue estimating procedures used by many U.S. states, including use of a press conference to present the Working Party's results to the public.<sup>112</sup>

**5. Sweden.** In addition to publishing revenue estimates and forecasts, the Swedish National Financial Management Authority provides private-sector users with "the information to make their own assessments and analyses," including the assumptions used by the Authority in its forecasts.<sup>113</sup>

**6. United Kingdom.** In 1997 the British government embarked on a "radical overhaul" of its monetary and fiscal policy. "The principle of credibility through maximum transparency" was the third of four basic principles behind the changes. As explained in a U.K. Treasury publication issued in 2002:

The greater the degree of transparency about the government's objectives and the reasons why decisions are taken, the more information about outcomes that is published as a matter of routine, and the more checks on the ability of government to manipulate the flow of information, the less likely is it that investors will be suspicious of the government's intentions, the greater the flexibility of

policy to react to real crises and the easier it is to build a consensus for difficult decisions.<sup>114</sup>

Regarding tax issues, the U.K. Treasury text states that "The Government believes that transparency should be the rule rather than the exception," adding that:

Transparent government is a fundamental part of a democracy. It ensures that Parliament and the wider public can scrutinize the Government's economic and fiscal plans. It is likely to encourage governments to give more weight to the longer-term consequences of their decisions, leading to more sustainable fiscal policy. It also encourages people and business to plan for the longer term, so that resources are allocated efficiently.<sup>115</sup>

Another aspect of the British initiative is publication of a new type of fiscal policy document known as a pre-budget report, which appears three months before the budget itself. That report results from a belief that "the budgetary process has for too long been shrouded in secrecy." By outlining "the significant policy proposals under consideration for discussion in the budget," the U.K. Treasury hopes "to stimulate a national debate about the major economic issues" presented in each year's budget.<sup>116</sup>

Although it is a written document, the British pre-budget report has the same objectives as the consensus revenue estimating conferences held by many of the U.S. states before the introduction of their budgets, as described earlier.<sup>117</sup> Both consensus estimating and the prebudget report seek to stimulate debate, solicit public comment on fiscal issues, and resolve differences in advance of actual introduction of a budget.

**7. International Monetary Fund.** The International Monetary Fund has been at the forefront in promoting transparency in fiscal affairs on a worldwide basis. Its principal tool for doing that is its *Code of Good Practices on Fiscal Transparency*.<sup>118</sup> The code promotes the timely and comprehensive reporting of fiscal information, open preparation of budgets, and enhancement of fiscal credibility through external audit and independent scrutiny.

The IMF's transparency code has been supplemented by a *Manual on Fiscal Transparency*,<sup>119</sup> which provides guidance on the transparency code's practical implementation and contains illustrations of good transparency practices. For baseline estimates, the manual advocates publication of the economic assumptions underlying

<sup>110</sup>Further information about Canadian developments is available on the Finance Canada Web site at <http://www.fin.gc.ca> and from the Revenue Analysis and Forecasting Branch in the Fiscal Policy Division of the Economic and Fiscal Policy Branch of Finance Canada.

<sup>111</sup>The Web site for the Danish Finance Ministry is at <http://www.fm.dk/>. English translations of selected documents are available.

<sup>112</sup>Correspondence with Dr. Ulrich van Essen, German Federal Ministry of Finance, August 29, 2003.

<sup>113</sup>*Annual Report of the Swedish National Financial Management Authority*, 2002, p. 32. The report is available in English by clicking on the Union Jack on the Authority's Web site at <http://www.esv.se>.

<sup>114</sup>HM Treasury, *Reforming Britain's Economic and Financial Policy*, ed. Ed Balls and Gus O'Donnell (Basingstoke and New York: Palgrave/St. Martins, 2002), p. 40.

<sup>115</sup>*Id.* at 139.

<sup>116</sup>*Id.* at 141.

<sup>117</sup>See the text accompanying *supra* note 97.

<sup>118</sup>The *Code of Good Practices on Fiscal Transparency — Declaration of Principles* was adopted by the IMF Board on April 16, 1998, and was revised and updated on March 23, 2001. It is available on the Web at <http://www.imf.org/external/np/fad/trans/code.htm>.

<sup>119</sup>The *Manual on Fiscal Transparency* is available on the Web at <http://www.imf.org/external/np/fad/trans/manual/ind ex.htm>.



revenue forecasts, plus any adjustments to the forecast to reflect exogenous variables, and "information on the [forecasting] models used."<sup>120</sup>

**8. Organization for Economic Cooperation and Development.** In February 2003 the OECD launched a broad survey on worldwide budget practices and procedures. About 60 countries will eventually be included in the initial survey sample. Among other issues, the survey seeks to compile country-by-country information on the "transparency of budget practices of government agencies."<sup>121</sup>

#### IV. Proposed Improvements

The need for greater transparency in the revenue estimating process at the federal level in the United States seems clear. The arguments in favor of transparency, both theoretical and practical, overwhelm the drawbacks. The need for change is especially apparent at Treasury. Change is also needed at the JCT.

In contrast, within its areas of responsibility, the CBO seems to be doing its best to promote a transparent forecasting regime. Perhaps more could be done, but the agency has made a good start along the road to full transparency.

Calls for greater transparency on the part of Treasury and Joint Committee revenue estimators have been made for a long time, but without much result.<sup>122</sup> Clearly, something must be done to convince those two agencies that it is time to address the transparency problem and to devise responses that will work.

#### A. Some Guiding Principles

It is important to keep costs and benefits in mind when devising solutions to transparency problems. For example, it is clear that publishing in-depth supporting analyses for thousands of revenue estimates would not be worth the cost. Few people would use most of them. But publishing detailed analyses for proposals that are important for revenue or other reasons makes a great deal of sense. A careful weighing of costs and benefits is therefore needed when deciding which revenue estimates require in-depth supporting analysis.

<sup>120</sup>See *Manual on Fiscal Transparency*, Part IV, Box 22 ("Revenue Forecasting"), following paragraph 4.1.2.

<sup>121</sup>Transparency practices are tabulated in tables 7.2.h.1 through 7.2.h.5, which appear in Part 7 of the preliminary survey results. Those results are available on the Web at <http://ocde.dyndns.org/acceuil.aspx?>

<sup>122</sup>For example, 18 years ago, Dr. Gerard M. Brannon, a former director of Treasury's Office of Tax Analysis, advocated "a more open exchange of the assumptions that underlie revenue estimates and of the models that are used to generate these numbers." See "Revenue Estimators Play a New Role as Numbers Dictate Policy," *Tax Notes*, November 24, 1986, p. 698. Sixteen years ago, on January 14-15, 1988, the Taxation Section of the Federal Bar Association held a conference at Airlie, Va., on "The Condition of the Tax Legislative Process." The conference summary indicates that "There was an extensive discussion of injecting more 'sunshine' into the revenue estimating process by making the underlying economic assumptions more publicly available." The full text of the conference summary is set forth in *Tax Notes*, June 27, 1988, p. 1581.

In the end, however, asking about the costs and benefits of transparency is a little like asking about the costs and benefits of democracy in contrast to other forms of government. In both cases, the evaluation involves weighing intangible values against tangible costs. Cost-benefit analysis can help us come up with sensible solutions that work, but in the end, we cannot quantify the intangible values at stake.

When devising solutions to revenue estimating transparency problems, it is also important to avoid proposals that create an "us versus them" reaction on the part of Treasury and the JCT or that reinforce the existing siege mentality that too often affects the revenue estimating staffs.<sup>123</sup> Both agencies need to recognize that greater transparency for the revenue estimating process has benefits for them and for the public, not just drawbacks, and need to know that their concerns and staffing requirements will be taken into account when resolving transparency problems.

It is also important to make it clear that calls for greater transparency do not constitute an attack on Treasury and JCT revenue estimators. Those individuals are professionals who do their best under sometimes difficult circumstances. The work they produce can make a significant contribution to the tax policy debate if it is made more broadly available to the public and if the estimators themselves are encouraged to play a larger, more visible role in the tax policy community. Enhanced transparency can help to show that, far from being second-class citizens, revenue estimators are among the best of public-finance economists.

**Enhanced transparency can help to show that, far from being second-class citizens, revenue estimators are among the best of public-finance economists.**

In general, the details of effective, lasting solutions to transparency questions can best be devised by the affected agencies themselves. They know their procedures better than any outsider possibly can. They are also better positioned to conduct experiments to find out what solutions work or do not work. And it is they who must request the additional staff necessary to implement any effective solution. The impetus for change probably has to come from outside in the form of a policy directive mandating greater transparency, but the detailed nuts-and-bolts implementation can be handled best by the agencies themselves.

Proposed solutions also need to address the distrust of one another's motives that currently characterizes relations between government estimating staffs and private

<sup>123</sup>According to a former government revenue estimator who is now in private practice, "A major issue is the siege mentality of all the participants in the revenue estimating process. Incremental improvements in these attitudes will occur if greater transparency allows the public to learn about the professionalism of the JCT and Treasury estimators."

estimators in accounting firms, think tanks, and academia. According to one government estimator, "No one in the private sector seriously thinks that Joint Committee or Treasury estimates are 'cooked.' What these guys really want is the ability to estimate their own proposals — not to improve JCT or Treasury estimates." Conversely, many private estimators are concerned about the secrecy surrounding official estimates, which they suspect masks inadequate analysis or questionable assumptions.

Dealing with this distrust will require more than mere changes in agency procedures. An ongoing, meaningful, public-private dialog is needed. That in turn will require a lessening of the isolation that separates revenue estimators from the rest of the tax policy community. It will also require real informational reciprocity in public-private discussions of revenue estimates. Both sides need to share information and calculations if trust is to be established; transparency is not a one-way street.

Finally, we need to be willing to accept incremental solutions to transparency problems. Referring to the 11 transparency components listed earlier in this report,<sup>124</sup> a leading revenue estimator in private practice cautioned, "Perfection is the enemy of the good. If we moved Treasury and the JCT to take the first five of these [component] steps, and included descriptions of the assumptions and data in steps 6 and 7, we would achieve 98 percent of the goal."

## B. Is Outside Intervention Needed?

Most of the proposals set forth below could be implemented promptly by the officials in charge of the Treasury and Joint Tax Committee revenue estimating staffs. Aside from the restrictions on disclosure of tax return data, there are no statutes or regulations that bar Treasury and the JCT from becoming more open about their revenue estimating assumptions and procedures.

Despite those facts, however, finding a solution to the transparency problem cannot simply be left to Treasury and the JCT. Those two agencies have had decades to come up with solutions since calls for greater transparency first arose. They have very largely failed to do so. Clearly, outside policy direction is now needed.

***Finding a solution to the transparency problem cannot simply be left to Treasury and the JCT. Outside policy direction is needed.***

Why have Treasury and the JCT failed to resolve the transparency issues discussed in this report? The basic answer is that transparency does not serve their short-term interests. All the internal pressures and institutional barriers at both agencies are against openness. As a Treasury official recently put it, "transparency doesn't give any return to the Assistant Secretary [for Tax

Policy]." So, he concluded, "nothing is going to happen on transparency without a mandate."

For example, greater transparency would inevitably delay the production of estimates because extra time would be needed to ensure that the estimates and the underlying documentation could withstand public scrutiny. That would aggravate complaints about delays in producing estimates. Further, transparency would make it easier for outside parties to criticize revenue estimates, and staff time would be required to respond to those criticisms. The managers of the Treasury and JCT estimating staffs have no desire to pile those new burdens on the shoulders of already overworked staffers. It is therefore unlikely that either Treasury or the JCT will enhance the transparency of their revenue estimating practices on their own.

This section proposes a few modest steps that should help to move Treasury and the JCT along the road toward greater openness for their revenue estimating activities. If these proposals fail to produce results, more vigorous intervention may be needed, but it is too early to assume failure. To the contrary, the appropriate current starting point is to assume goodwill and an intelligent response from both Treasury and the JCT.

## C. A Few Modest Proposals

The transparency suggestions set forth below fall into two categories: "process" proposals and "substance" proposals. Process proposals relate to the rules and customs that govern the preparation of revenue estimates. Substance proposals relate to the actual content of estimates and the underlying data. Both types deserve careful consideration.

### Process Proposals

**1. Enact statutory disclosure mandates.** The disclosure mandates in the Congressional Budget Act<sup>125</sup> and the Unfunded Mandates Reform Act<sup>126</sup> have played a crucial role in encouraging disclosure of the underpinnings of the cost estimates prepared by the CBO. A similar statutory mandate<sup>127</sup> addressed to Treasury and modeled on the CBO disclosure mandates should be added to the Internal Revenue Code.<sup>128</sup> A separate but substantially

<sup>125</sup>The Congressional Budget and Impoundment Control Act of 1974, P.L. 93-344, 88 Stat. 297.

<sup>126</sup>The Unfunded Mandates Reform Act of 1995, P.L. 104-4, 109 Stat. 48.

<sup>127</sup>The mandate should speak in general terms but should also lay the groundwork for disclosure of all 11 of the elements of generalized and specific transparency listed *supra* on p. 331.

<sup>128</sup>The proposal made in the text might take the form of an amendment to section 7805, which relates to publication of rules and regulations. The proposed amendment is not appropriately part of chapter 61 of the code, which relates to "Information and Returns." The disclosure provisions of section 6104 (relating to exempt organizations), section 6108 (relating to statistical publications), and section 6110 (relating to written determinations) appear to be located in chapter 61 because they function as *exceptions* to section 6103's *general prohibition* on disclosure of tax returns and return information. The proposal made in the text is *different from*, rather than an exception to, section 6103.

<sup>124</sup>See *supra*, p. 331.

identical mandate should be added to the provisions of the code that relate to the JCT.<sup>129</sup>

Those mandates would make clear to both Treasury and the Joint Committee that “disclosure is part of the job” of preparing revenue estimates and that publication of a mere revenue number without any explanation or rational underpinning represents incomplete work. Those mandates would also provide a basis for requests from both Treasury and the JCT for the additional staff and funding needed to make transparency a reality.

At the same time, because those mandates would speak in general terms, Treasury and the JCT would remain free within rather broad limits — as the CBO has been — to experiment with possible solutions to transparency issues.

Statutory mandates are important because they help to change the mindset of those subject to the mandate. JCT estimators now can regard their job as “done” when they send an estimate to the congressman requesting it, and their counterparts at Treasury can feel the same way when they have provided Treasury or White House officials with revenue gain or loss figures. Understandable though those attitudes may be, those mindsets ignore the information needs of the public.

Mere exhortation is unlikely to change those mindsets; the habits of thinking that block disclosure are simply too ingrained.<sup>130</sup> That is why a congressional command is needed to make it clear that the job of preparing a revenue estimate is not completed until the public is adequately informed.

The idea of using a statutory mandate to encourage revenue estimating transparency is not new. Starting in 1988, Sen. Robert W. Kasten Jr., R-Wis., began to champion his Tax Policy Freedom of Information and Sunshine Act.<sup>131</sup> Among other things, that legislation would have required the JCT to report on “the economic assumptions and methodology that underlie” its revenue estimates. It would also have required preparation by the JCT of “technical explanations setting forth the economic data, assumptions, and methodology [underlying a revenue

estimate] in sufficient detail to permit replications of the results by nongovernmental analysts. . . .”<sup>132</sup>

A similar, more-recent call for greater revenue estimating transparency came on May 22, 2003, from Sens. Max Baucus, D-Mont., and Kent Conrad, D-N.D., who outlined “five areas of concern” regarding the revenue estimating process in an open letter to the JCT.<sup>133</sup> “We are concerned with the lack of transparency in the revenue estimating process,” the senators said. They also called for enhanced quality controls over the estimating process, greater timeliness in the production of estimates, and better information about the relationship between revenue yields and IRS enforcement efforts.

**2. Publish assumptions.** The assumptions on which a revenue estimate is based — especially the behavioral assumptions — can have an enormous effect on the resulting estimate. Recall, for example, the furor that arose when, in 1990, Treasury and the JCT made somewhat different assumptions about the likely taxpayer response to a change in capital gains tax rates.<sup>134</sup> As one government revenue estimator put it, “The real differences in revenue estimates arise from the behavioral assumptions, which have a large effect on some estimates and little or no effect on many others.”

The assumptions that underlie revenue estimates should be released precisely because they are so important in understanding and evaluating the estimate. Indeed, publishing the assumptions on which estimates are based is probably the single most important step that should be taken to enhance the transparency of the federal revenue estimating process. Publication of assumptions will not, in itself, resolve disputes about the validity of the assumptions, but it is a necessary first step to talking about and eventually resolving those disputes.

Releasing estimators’ assumptions along with their estimates is a step that could be taken voluntarily, and almost immediately, by Treasury and the JCT. A change in internal directions and procedures is all that is needed. Indeed, the JCT made just such a pledge in 1995.<sup>135</sup> The existence of that pledge shows that release of the JCT’s

<sup>129</sup>See sections 8001-8023.

<sup>130</sup>A related “mindset” problem involves the isolation of the Treasury and JCT revenue estimators from the rest of the tax policy and economics community. That is not a problem that can be addressed by legislation, but it is a problem nevertheless. The economists who do revenue estimating seldom participate in the work of the National Tax Association or the Washington-based associations for professional tax economists. Their isolation from the rest of their professional community weakens the connections that would otherwise exist between the Treasury and JCT staffs, and between revenue estimators and the policy-oriented economists and lawyers working on the Treasury and JCT staffs. Too often, that isolation translates into unhealthy “us versus them” attitudes that do not advance the public interest.

<sup>131</sup>The 1990 version of Sen. Kasten’s proposed legislation was introduced as S. 3243, 101st Cong., 2d Sess., and is available on the Web at <http://thomas.loc.gov/>.

<sup>132</sup>An article by Sen. Kasten explaining his sunshine proposal appears in the February 1990 issue of the Tax Foundation’s newsletter, *Tax Features*, and is reprinted as *Doc 90-1551*, 90 *TNT* 46-30.

<sup>133</sup>See “Baucus Calls on Joint Committee on Taxation for Accountability,” *Doc 2003-12849*, 2003 *TNT* 100-33.

<sup>134</sup>See *supra* pp. 334-335.

<sup>135</sup>Letters dated May 18, 1995, from Kenneth J. Kies, chief of staff of the JCT, to Bill Archer, chair of the Ways and Means Committee, and Bob Packwood, chair of the Finance Committee, stated that “in response to concerns,” the JCT was making eight enumerated “changes in the estimating process.” The first change was that “information regarding any significant behavioral assumptions underlying estimates of major tax proposals will now be included with our estimates if requested by the member of Congress submitting the estimate request.” *Doc 95-5074*, 95 *TNT* 98-25 (Archer); *Doc 95-5075*, 95 *TNT* 98-26 (Packwood).



estimating assumptions is feasible and is not barred by statute or rule. The situation at Treasury appears to be similar.<sup>136</sup>

Releasing assumptions would not involve questions relating to the confidentiality of tax returns and return information, except possibly in a few very rare cases. In those rare instances, redaction could be used to safeguard taxpayer data.

Requiring publication of assumptions would impose an additional workload on the estimators at both Treasury and the JCT because neither agency currently requires their estimators to document all the estimates they produce. Today, in many cases, the assumptions that underpin a revenue estimate either are not written down at all or take the form of brief jottings for the file.

Further, even when assumptions are formally documented internally, the documentation is often less detailed than would be required if the assumptions were open to public scrutiny. Thus, even when internal documentation is available, estimators' workloads would probably increase modestly if their assumptions were released to the public.

Another problem involves the source and nature of the assumptions currently employed in making revenue estimates. Sometimes estimators rely on private-sector data sources such as trade associations that would not want their assistance to be revealed when a revenue estimate is released. Therefore, release of estimating assumptions might constrict Treasury and JCT access to data, at least to some degree.

Further, all estimates involve some degree of personal judgment by the estimator. If publication of estimators' assumptions were required, many estimators would probably be reluctant to list "my best guess" as the assumption underpinning an estimate.

That reluctance would probably push estimators to base their assumptions on more than guesses to the extent that it is possible. However, especially when estimates must be produced under severe time pressure, it will often be necessary to base estimates on assumptions that are little more than educated guesses. Even in those cases, however, the assumptions should be published. In most cases, it is more important to know that an estimating assumption is based on a guess than to know that it is based on rock-hard data.

Educated guessing is required in all professional work, whether the work involves law, medicine, engineering, or revenue estimating. However, even educated guessing should have some basis, such as discussions with industry experts or consideration of analogous behavioral effects. When good professionals are required to guess, they normally make that fact clear, together with the basis for their guess, so that judges, patients, clients, and others can evaluate the information provided. The same standard applies to revenue estimators.

**3. Explore user certifications.** When government agencies wish to spur private research that involves confidential data, they often make use of data protection plans

and "user certifications" to preserve confidentiality while allowing research to go forward. Subject to similar safeguards, both the Treasury Department and the JCT should consider providing access to IRS statistics of income files to researchers in the private sector, including the major accounting firms, universities and nonprofit institutions, and others. That would provide a substantial spur to in-depth research on the revenue estimating process.

The typical user certification procedure involves the signing of data release agreements by the researcher and the relevant government agency.<sup>137</sup> Those agreements require researchers to prepare data protection plans for agency approval. Bonding, encryption procedures, and firewall certifications can also be required. Surprise inspections can be used to enforce the restrictions. Regarding tax data, researchers should be made subject to the same civil and criminal penalties<sup>138</sup> that apply to IRS personnel who have access to tax data.

Development of release procedures such as these would enable Treasury and the JCT to commission private research on the revenue estimating process. Private contractors could also assist in the task of model building and testing to facilitate and support the work of Treasury and JCT estimators. Private contractors have sometimes assisted in that way in the past,<sup>139</sup> and adoption of user certification procedures could facilitate expanded use of their services in the future.

There is a precedent for the use of contract-based estimating data release procedures such as those suggested above. When the JCT established its first private-sector, revenue estimating advisory board in 1989, it required all board members to sign "contracts strictly binding them to observe the confidentiality of JCT taxpayer data."<sup>140</sup> The procedures suggested here are simply a modern elaboration of that earlier approach.

**4. Establish an IRS research data center.** Many federal agencies find themselves under the dual obligation of

<sup>137</sup>The University of Michigan is currently engaged in a "Health and Retirement Study" for the U.S. Department of Health and Human Services. The study requires the use of confidential data that are released to researchers under the provisions of a "Contract for Use of Restricted Data." The contract requires preparation of a "Restricted Data Protection Plan" as part of an "effort to ensure that our promises of anonymity to our respondents are kept and that no persons other than those authorized by the Contract — the Restricted Data Investigator, Co-Investigators, and Research Staff — have access to the contents of the Restricted Data." For further information, see [http://hrsonline.isr.umich.edu/rda/rdapkg\\_prot.htm](http://hrsonline.isr.umich.edu/rda/rdapkg_prot.htm).

<sup>138</sup>Section 7213(a)(1)-(3) imposes a fine of up to \$5,000 and imprisonment for up to five years, or both, for unauthorized disclosure of tax return information. In addition, sections 7431 and 7435 provide civil damages for unauthorized tax information disclosures.

<sup>139</sup>For example, in 1984-1985, a private contractor, Thomas Vasquez, built a comprehensive Treasury income tax model data base that was later used in modeling some of the provisions of the 1986 tax act.

<sup>140</sup>See "New JCT Advisory Board Formed to Improve Revenue-Estimating Process," *Tax Notes*, May 1, 1989, p. 523.

<sup>136</sup>See the comments by Dr. Gerard M. Brannon, former director of Treasury's Office of Tax Analysis, *supra* note 122.

## COMMENTARY / REVENUE ESTIMATING PROCESS

protecting personal identities and information when releasing information and statistics to the public. Treasury, the IRS, and the JCT are not alone in facing those conflicting demands. However, other agencies, notably the Bureau of the Census,<sup>141</sup> Department of Health and Human Services,<sup>142</sup> Department of Education,<sup>143</sup> and Bureau of Labor Statistics,<sup>144</sup> have done better than tax-related agencies in devising creative solutions to their information dilemmas.

Chief among those responses has been the research data center approach. A research data center (RDC) is a way to grant private researchers access to confidential statistical data while carefully limiting the risk of any disclosure of confidential information.<sup>145</sup> RDCs allow licensed researchers to make use of confidential files (either on site or over secure electronic lines) within a closely restricted area of study using specialized equipment and extreme security. By using an RDC, an agency can encourage research without breaching legal and ethical restrictions on data disclosure.

The RDC approach offers a way to resolve the problems caused by the increasing difficulty of disclosure-proofing the IRS public-use file. It also provides a means of allowing sophisticated private researchers to gain access to needed data, such as data relating to larger corporations and multiyear longitudinal data, without jeopardizing taxpayer privacy or confidentiality.

The RDC concept was pioneered by the Census Bureau starting in 1994 through its Center for Economic

Studies. The success of the Bureau's pilot projects led to the establishment of regional RDCs at several major universities. That success also led other agencies, including the National Center for Health Statistics and the Agency for Health Care Research and Quality, to establish RDCs.

Access to an RDC by a researcher is premised on compliance with several highly restrictive conditions. Those include submission of a research proposal for approval; execution of a written agreement covering the work to be done, the data to be used, and the types of output allowed; limitations on the type of analysis allowed, including use of any outside linkable data brought in by the researcher; use of dedicated computers; review of output; inspection of material removed from the site; and in-person oversight by agency staff.

Adoption of the RDC approach by the IRS would allow tax-related private research to go forward in ways that are not now possible. The approach also offers a partial solution to the increasing challenge of disclosure-proofing the IRS public-use file and would permit controlled release of large-firm corporate tax data to researchers even if inclusion of large-firm data in the IRS public-use file is deemed impossible.

The RDC approach would also permit Treasury, the IRS, and the JCT to subcontract to private agencies some of the tax-related research projects that at present can be performed only by agency staff because of existing restrictions on access to tax data. As indicated in footnote 141, pilot programs of this sort are already underway.

**5. Imitate and enhance CBO publication practices.** From a theoretical point of view, it might make sense to assign the tax estimators who are now part of the JCT staff to the CBO,<sup>146</sup> but from an historical and political point of view, a merger of that sort seems highly unlikely. The JCT has opposed the idea.<sup>147</sup> Moreover, such a move

<sup>141</sup>A description of the Census Bureau's research data center program is available on the Web at <http://148.129.75.160/ces.php/rdc>. According to private researchers with close ties to the IRS, at least three academic economists have used Census Bureau Research Data Centers to do approved tax research using IRS tax return data, so there is precedent for the proposal made in this section.

<sup>142</sup>See, e.g., the discussion of "Restricted-Use Contractual Data" on the Web site maintained by the National Longitudinal Study of Adolescent Health, at <http://www.cpc.unc.edu/projects/addhealth/data/restricteduse>. Examples of security plans for the use of study data are provided at <http://www.cpc.unc.edu/projects/addhealth/data/restricteduse/security2>.

<sup>143</sup>See the Department of Education's "Restricted-Use Data Procedures Manual," which is available on the Web at <http://nces.ed.gov/statprog/rudman/index.asp>.

<sup>144</sup>Information about the Bureau of Labor Statistics program is available on the Web at <http://www.bls.gov/bls/blsresda.htm>.

<sup>145</sup>An excellent description of the research data center approach has been prepared by the Confidentiality and Data Access Committee of the Federal Committee on Statistical Methodology (FCSM) in the Office of Management and Budget. See "Restricted Access Procedures," available (following the fourth boldface bullet) on the FCSM Web site at <http://www.fcsm.gov/committees/cdac/resources.html>. For information on similar centers at the University of Michigan, the U.S. Department of Justice, the U.S. Department of Agriculture, the U.S. Immigration and Naturalization Service, and Statistics Canada, see "Enhancing Researchers' Access to Confidentiality Data: Five Case Studies," presented at the 2001 Joint Statistical Meeting, which is available on the Web at [http://www.amstat.org/meetings/jsm/2001/index.cfm?fuseaction=activity\\_details&activityid=237&sessionid=200619](http://www.amstat.org/meetings/jsm/2001/index.cfm?fuseaction=activity_details&activityid=237&sessionid=200619).

<sup>146</sup>The basic skills needed to do cost estimates for nontax bills are quite similar to those needed to do tax estimates. A merger of the JCT and CBO staffs would therefore make it easier to cope with estimating workloads, because the CBO staff would be available to help the tax estimators on an as-needed basis, and vice versa. Furthermore, the transparency standards and procedures developed by the CBO over the past 30 years would begin to apply to tax estimates as well, and the personnel and other supporting services now provided by the CBO to its operating divisions would become fully available to the JCT tax estimators. However, a merger of the two estimating staffs might impede ready access by the former JCT estimators to the important legal expertise on the JCT staff. According to one former JCT and Treasury estimator, "Estimators are not trained in tax law, do not keep up with rulings and other IRS guidance, and often know little about other areas of controversy." He concludes that "It would be very harmful to the accuracy of the estimates if the estimating staff were to be separated from the attorneys."

<sup>147</sup>See Part 4 of Appendix 1 to JCT, *Written Testimony of the Staff of the Joint Committee on Taxation Regarding the Revenue Estimating Process*, JCX-1-95, Doc 95-441, 95 TNT 7-10. That report indicates that "Some proposals to reorganize the operations of the Congress have proposed merging the Joint Committee on Taxation revenue estimating staff with the Congressional Budget Office." The Appendix then rejects those

(Footnote continued on next page.)

would require agreement by the chairs of the Ways and Means, Finance, and Budget Committees, and that is highly unlikely, because that move would alter the power relationships between those individuals.

Nevertheless, it would be possible to gain the transparency benefits of such a merger if the JCT were to imitate *in toto* the CBO's publication practices. That expansion of JCT disclosure should apply to all revenue estimates prepared by the JCT staff, not just the estimates for the chairs' marks, reported legislation, House- and Senate-passed bills, conference reports, and tax expenditures, all of which are now made available on the Web by the JCT.<sup>148</sup>

Expanded JCT disclosure of estimates would, of course, require a change in the JCT's custom of permitting most revenue estimate disclosure decisions to be made by the individual members of Congress who requested the estimate.<sup>149</sup>

On the basis of similar reasoning, the revenue estimating staff at Treasury should publish all of its revenue estimates within a reasonable time after the estimates have been completed. Treasury's tax expenditure forecasts are already made public in the administration's annual budget.<sup>150</sup> Expanded publication of revenue estimates would, of course, require enlargement of the existing Treasury OTA Web site.<sup>151</sup>

Those suggestions are not as far-fetched as they may seem, because the CBO already publishes on the CBO Web site selected tax estimates supplied by the JCT.<sup>152</sup> However, what is currently published provides little additional information aside from the JCT estimate itself, with only a few accompanying details. The scope of CBO publication of JCT tax estimates needs to be enhanced.<sup>153</sup>

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proposals because "Such a move would seriously impair the unique relationships that permit the Joint Committee's lawyers and economists to work together."

<sup>148</sup>For instructions on accessing those estimates, see *supra* note 64.

<sup>149</sup>See the discussion of this issue in "The JCT and Congress," *supra* pp. 338-339.

<sup>150</sup>See Office of Management and Budget, *Analytical Perspectives (Fiscal 2005)*, pp. 285-328, available at <http://www.whitehouse.gov/omb/budget/fy2005> as the third of the listed "Budget Documents."

<sup>151</sup>The Treasury Office of Tax Analysis Web site is <http://www.treas.gov/offices/tax-policy/offices/ota.shtml>.

<sup>152</sup>See, e.g., the March 22, 2004, revenue and spending estimates for H.R. 3971, the Highway Reauthorization Tax Act of 2004, which are available on the CBO Web site at <http://www.cbo.gov/showdoc.cfm?index=5257&sequence=0>. The CBO discussion entitled "Basis of Estimate" states that the "JCT provided all the revenue estimates."

<sup>153</sup>In addition to lack of detail, there is an unfortunate limitation on the CBO's ability to provide additional information regarding those estimates. The CBO's Web posting of JCT estimates includes the names of the CBO analysts who prepared the estimate for publication; readers are invited to consult them if questions arise. However, if members of the public have questions about the details of the publicly posted JCT estimate, the listed CBO employees cannot answer them. Instead, according to the CBO, those questions must be addressed to the JCT estimating staff, which does not normally respond to questions

(Footnote continued in next column.)

A possible objection is that release of the thousands of revenue estimates done each year by the JCT and Treasury is unlikely to be useful to the public. As a general matter, this is obviously true, just as (in a different context) the current practice of releasing thousands of IRS letter rulings each year is not useful to the general public.

The alternative to general release is to require publication of only "important" revenue estimates, but who is to judge importance? Leaving this judgment to agency administrators is not the right answer. Every revenue estimate, just like every letter ruling, is of interest to someone. Otherwise, the estimate would not exist. For that reason, every revenue estimate should be made available to the public, even though the number of interested individuals may not be large, just as the CBO makes every one of its cost estimates publicly available.

**6. Consider peer review for selected estimates.** Independent, objective peer review is a very effective way to improve the quality of a study's methods, results, and findings. Peer review is commonly used to assure the quality of articles submitted for publication in scholarly journals.<sup>154</sup> Increasingly, it is also being applied in other areas, such as the federal regulatory process.<sup>155</sup>

Selected revenue estimates published by Treasury, the JCT, and the CBO should be subjected to independent peer review. Given the estimating workloads of those three agencies, it would be impractical to subject every one of their estimates, or even the bulk of their estimates, to review; but it would be highly useful to peer review at least *some* of their estimates. The suggestions made during those reviews would benefit the entire estimating process, not just the estimates that are actually subjected to review.

Thought needs to be given to the criteria that might be used to select estimates for peer review. One criterion might be the uniqueness or novelty of the estimating challenge, because peer review is especially needed in cases in which estimating procedures are still in a somewhat experimental stage. Another criterion might be the frequency with which estimates in a particular area are challenged by third parties, because in those cases, peer review might help to resolve or at least clarify the sources of dispute. Perhaps priority ought to go to estimates for

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from the public. The end result of this Catch 22 is that JCT estimates are in some instances publicly available through the CBO, but further information about them is not. That situation seems contrary to the CBO's stated publication policy, which includes providing the press and the public with "further details on request." See *supra*, note 67.

<sup>154</sup>A useful discussion of the purpose and function of independent peer review is set forth in "Proposed Bulletin on Peer Review and Information Quality," published on September 15, 2003, by the OMB. See 68 Fed. Reg. 54,023 (Sept. 15, 2003) at 54,024-54,026.

<sup>155</sup>The Office of Information and Regulatory Affairs (OIRA), which is part of the OMB, encourages federal agencies to conduct peer reviews of proposed regulatory rules. The purpose, according to OIRA, "is to provide an expert review of the use of science that is free from the biases of the regulators and the interested parties." See OMB, "Proposed Bulletin on Peer Review and Information Quality."



newly enacted tax provisions, with the goal of standardizing the applicable estimating techniques. In any event, some minimum number of peer reviews should be done each year, for example, not less than five per agency per year.

Peer reviewers would necessarily require access to tax return data, and perhaps other confidential information, to evaluate the quality of a revenue estimate. That issue could be dealt with by requiring peer reviewers to sign confidentiality agreements, as is commonly done in other instances when the government requires outside advice on confidential subjects.<sup>156</sup>

Peer review cannot be allowed to delay submission of revenue estimates to the agencies requesting them. Legislative time schedules will not permit delay. Consequently, except in rare instances, peer review of revenue estimates will have to be done after estimates have been prepared and submitted to requesters rather than before publication, as in the case of scholarly articles. The focus of the review will therefore be on the improvement of future estimates rather than on correction of the estimate at hand.

It is important to ensure the independence of the individuals who participate in a peer review of agency revenue estimates. The three agencies that prepare revenue estimates already conduct their own internal reviews before releasing their estimates. An important function of independent peer review is to overcome the suspicions to which self-review inevitably gives rise, including fears that self-reviewers might feel pressured to support their agency's position and to refrain from frank comment. Independent reviewers can also provide a fresh look at old problems and can thus supply insights that might not arise during self-review.

Independent peer reviewers should include individuals from the private sector (subject to safeguards similar to those outlined above in connection with user certifications and research data centers). The GAO, the Congressional Budget Office, the Congressional Research Service, and the National Academy of Sciences could also provide peer reviewers for revenue estimates.

When independent peer review of selected revenue estimates occurs, there should be an opportunity for public discussion and participation. At a minimum, the reviewers should present a public report regarding their findings, and the private sector should be given an opportunity to ask questions about that report.

### Substance Proposals

**7. Publish estimating memorandums.** Publishing revenue estimating assumptions would be a good first step toward greater transparency. However, a more comprehensive and satisfactory solution would involve publication of more extensive revenue estimating technical memorandums, including assumptions. At a minimum, technical memorandums should be prepared and published for every significant estimate.

<sup>156</sup>See *supra* notes 137 (Health and Human Services) and 140 (Joint Committee).

Those technical estimating memorandums should be modeled, in the case of routine estimates, on the fiscal notes prepared by the revenue departments of states such as Minnesota<sup>157</sup> or the cost estimates published by the CBO.<sup>158</sup> For more important estimates, the technical memorandums should be modeled on those prepared by private-sector estimators for clients and on the JCT's rare but valuable technical explanations, such as its recent technical explanation regarding dynamic scoring of the president's 2003 tax proposals.<sup>159</sup>

The information in technical memorandums should include a description of the rules of thumb used by estimators to adjust the current-law baselines provided by the CBO or the OMB. For example, the memorandums should describe how the JCT and Treasury divide estimated current-law receipts by income class and how the estimators move from adjusted gross income to imputed income figures, such as the value of owner-occupied housing. Knowing the rules of thumb used to resolve those nitty-gritty issues can help the interested public understand why a given estimate turned out as it did.

Estimating memorandums would also be an appropriate place to describe the techniques used by Treasury and JCT estimators to extrapolate current estimating data into periods 5 or 10 years in the future. Those extrapolations are needed when revenue estimates cover decade-long future periods, as required by current budget rules, but the extrapolation techniques used by Treasury and the JCT are largely unknown.

Estimating memorandums would also be an appropriate vehicle for providing basic sensitivity analysis regarding the point figures normally provided in revenue estimates. A leading private-sector estimator stated:

I would argue that some simple sensitivity analysis around [revenue estimating] results would be much more helpful than detailed information about the data sources, assumptions, and modeling procedures that underlie an estimate. Let's figure out a way to provide some meaningful information about the potential range of results around a point estimate. In addition, I'd like to know about the estimator's relative comfort level with an estimate, on a one to five scale.<sup>160</sup>

Why are technical memorandums outlining this information not routinely prepared and released by Treasury and the JCT, at least for significant revenue estimates? Personnel constraints provide one answer: More staff

<sup>157</sup>See the discussion of state fiscal notes *supra*, p. 350.

<sup>158</sup>See *supra*, p. 341.

<sup>159</sup>See *Overview of Work of the Staff of the Joint Committee on Taxation to Model the Macroeconomic Effects of Proposed Tax Legislation to Comply with House Rule XII.3.(h)(2)*, JCX-105-03, December 22, 2003, Doc 2003-26926, 2003 TNT 246-8.

<sup>160</sup>In March 2003, in its *Analysis of the President's Budgetary Proposals for Fiscal Year 2004*, the CBO published a sensitivity analysis of alternative macroeconomic scenarios relating to the president's budget proposal. The CBO budget report is available on the Web at <http://www.cbo.gov/showdoc.cfm?index=4129&sequence=0>. The sensitivity analysis of alternative scenarios is set forth in the last section of the report.

would be required to write the required memorandums. Another answer doubtless involves political considerations: Making more information public about a tax proposal might provide the proposal's opponents with ammunition to mount a critique.<sup>161</sup>

Neither of those considerations constitutes a valid objection to the proposal to accompany Treasury and JCT estimates with technical memorandums. A desire to suppress information to gain political advantage, while perhaps understandable, is inappropriate in a democracy. Responsible civil servants and their superiors have a duty to request the staffing necessary to serve the public properly.

Preparation and release of revenue estimating technical memorandums might actually be a boon to morale on both the Treasury and JCT estimating staffs. Staff members now have no vehicle that enables them to explain or justify their conclusions. That means they can easily be criticized without having a chance to defend their work. Release of technical memorandums would provide staff members with a means of defending themselves and their conclusions.

As a first step, both Treasury and the JCT should begin to accompany all significant revenue estimates with a technical explanation that is released to the public. At least at the outset, it should be left to them to decide what constitutes "significance." In some cases, revenue effect alone might determine an estimate's significance. In other cases (such as the JCT's release of its first dynamic scoring), the novelty of the estimating approach might lend significance to an estimate.

Once the Treasury and JCT staffs grow accustomed to preparing and releasing technical memorandums in significant cases, they can consider whether abbreviated memorandums or fiscal notes would be useful to them and to the public in additional cases, or perhaps in all cases.

A gradualist approach along those lines would enable revenue estimators to find out what style of reporting would best serve the public. That would minimize the dangers that one former Treasury estimator sees in required estimating memorandums. "Publication of memorandums" he warned, "raises the prospect that disclosure will result in non-meaningful reports that have real costs but produce minimum benefit. Compliance-oriented memos might appear to be addressing the problem, while serving only as window-dressing."

In addition to preparing memorandums on specific estimates, both Treasury and the JCT should publish every three to five years a general description and overview outlining the status of their revenue estimating efforts. That overview should include a discussion of any innovations that have been introduced, changes in data

sources, alterations in estimating techniques, challenges faced, workloads, and problems yet to be resolved. The discussions in the overview should relate to each of the major estimating areas: individual, corporate, payroll, excise, and estate and gift. The goal should be to provide the interested public with a periodic official update regarding the status of Treasury and JCT revenue estimating efforts.

**8. Enhance the public-use file.** Private-sector revenue estimating depends on the availability of tax data. For that reason, it is important both to correct the deficiencies in the public-use tax file prepared by the IRS Statistics of Income Division and to enhance that file in several ways. Unless those improvements are made, private-sector revenue estimating will not flourish and university research on revenue estimating topics cannot be undertaken.

*i. Timeliness.* First, and most important, the IRS public-use file needs to be produced in a timely way and released on a regular basis. In recent years, that has not been the case. Two- to three-year release delays have been common.<sup>162</sup> This has seriously hampered the work of private revenue estimators.

As of early 2004, the most recently released IRS public-use file related to tax year 1999. Even longer delays have occurred for earlier years.<sup>163</sup> As a result, the information in the public-use file is often outdated by the time it becomes available to private estimators.

Much of the delay in releasing public-use files has resulted from IRS concern about the possibility that private-sector operatives could glean individual taxpayer data from the public-use file. Those are serious and legitimate concerns. However, as outlined earlier,<sup>164</sup> the IRS, with the help of private contractors, has developed improved techniques to disclosure-proof the public-use file. As a result, speedier release of the public-use file should now be possible.<sup>165</sup>

Timeliness problems could be somewhat ameliorated if Treasury and the JCT made available their extrapolated files, which show their current and future data extrapolated from prior year figures. As one private-sector estimator has put it, "I can easily get the public-use file, but without a careful extrapolation it is not that helpful, since the [tax] law and the underlying demographics change over time." He said flatly that "Treasury and the JCT should make available their extrapolated files."

If the public-use file is to be published in a timely way, the release effort needs to be adequately staffed. The goal

<sup>162</sup>See the listing of delays in *supra* note 90.

<sup>163</sup>See *supra* note 90.

<sup>164</sup>See the discussion of disclosure-proofing the public-use file *supra* p. 347.

<sup>165</sup>However, Treasury sources indicate that there are "still issues that need to be resolved" to disclosure-proof the public-use file and that delays in release of the file "aren't just foot dragging." If so, the IRS should state what the issues are and address them. Merely delaying publication of data until they are no longer useful is not an acceptable solution.

<sup>161</sup>This may account for Treasury's failure to publish a proposed National Tax Association paper regarding the revenue estimates for the president's 2003 dividend exclusion proposal. See *supra*, p. 333. It may also account for Treasury's long delay in responding to Tax Analysts' FOIA request for access to the assumptions and spreadsheets underlying that proposal. See *supra* note 22.

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should be to release the public-use file contemporaneously with the statistics of income file for the same year.<sup>166</sup>

ii. *Scope.* The individual public-use file should include basic classifiers, such as information relating to age distribution. Also, it should be expanded to include multiyear, longitudinal information in light of the increasing importance of longitudinal files in the revenue estimating process.

For business returns, a public-use file relating to small and midsize corporate and noncorporate business returns should also be made available, despite the obstacles outlined earlier,<sup>167</sup> with confidentiality-preserving aggregation of the data. Small and midsize firms frequently play a disproportionately large role in the formulation of tax policy, and a public-use business file regarding those firms is therefore needed. Obviously, preparation and release of this file would require additional staffing in the IRS Statistics of Income Division.

Disclosure-proofing business return data for larger firms is probably impossible. To be useful, a large-firm business return file would have to identify firms by industry, because many important corporate tax rules vary from one industry to another. But if industry identifiers were provided, it would be easy in many cases to pick out individual firms. Hence, at least for larger corporations, the research data center approach described earlier<sup>168</sup> is probably the only appropriate way to permit private research on large corporate data to go forward.

#### D. Competition as a Driving Force for Change

The ideas suggested in the preceding section may sound innocuous. They are intentionally designed both to intrude as little as possible into the current estimating work of Treasury and the JCT and to leave those agencies largely free to devise their own ways of responding to the need for greater transparency.

Nevertheless, some government experts who have reviewed those suggestions in draft form conclude, in the words of one of them, that the preceding discussion "grossly underestimates the difficulty of doing what is suggested" and "grossly overestimates the utility of doing so." As to the utility of revenue estimating transparency, another government critic adds that transparency concerns are not a priority. "Revenue estimating transparency is not in the top 100 issues that concern tax policymakers," he said.

Comments such as those, which are honestly advanced and deeply felt, show how unlikely it is that Treasury or the JCT will voluntarily enhance their existing disclosure practices. Outside pressure will almost certainly be needed to produce change.

Congress is a possible source of outside pressure supporting greater transparency. Congress is responsible for mandating the CBO's existing transparency prac-

tices<sup>169</sup> and for changing the rules of the House of Representatives to require the JCT to produce dynamic scores.<sup>170</sup> Now and again, individual members of Congress have argued for greater revenue estimating transparency,<sup>171</sup> but there is no sign that Congress is currently interested in transparency issues.

Private competition is a more likely source of pressure for greater transparency. If properly encouraged,<sup>172</sup> competition could become a driving force for improvement and change in the revenue estimating process.<sup>173</sup>

Recall, for example, the 1989-1990 competition between Treasury and the JCT over the assumptions and techniques to be used to estimate the revenue effects of changes in capital gains taxes. That competition forced both agencies to provide Congress and the public with detailed explanations of the methods they used to arrive at their numbers.<sup>174</sup> Recall, too, the competition between advocates of static and dynamic scoring, which spurred the JCT estimators in 1995 to begin a serious investigation of ways to produce a reliable dynamic score. More recently, there has been dynamic scoring competition between the CBO and the JCT.<sup>175</sup> Those various efforts culminated in the 2003 publication of the JCT's first full-scale dynamic score for a tax proposal.<sup>176</sup> Competition was an effective spur to action.

From whom might a competitive critique of revenue estimates come? Certainly, in the first instance, it might come from some of the major accounting firms and their clients.<sup>177</sup> Would that critique be one-sided and self-interested? In a few instances it might be, at least if clients were allowed to insist on assertion of a predetermined viewpoint; but that is not likely, and even self-interested comments contain gems of wisdom. In general, however, the professionals in accounting and law firms are fully

<sup>169</sup>See *supra* note 12.

<sup>170</sup>See *supra* note 48.

<sup>171</sup>See *supra*, p. 354.

<sup>172</sup>Greater transparency, in itself, would encourage competition by making information available to individuals and firms that are in a position to compete. Enhanced transparency would also enable both public and private revenue estimators to compete more intelligently because they would know more about why their estimates differ. For example, they would know whether their differences arose from disparate assumptions (in which case the assumptions could be scrutinized) or from methodological differences (in which case the relative merits of competing models could be debated). The net result would be intelligently focused pressure for improvements in the revenue estimating process, leading to sounder assumptions and better models.

<sup>173</sup>This is not a new suggestion. The same idea was advanced 18 years ago in Jack Teuber, "The Suspicion That Results From the Revenue Estimators' Evolving Role Is Not Easily Overcome," *Tax Notes*, Dec. 8, 1986, p. 882.

<sup>174</sup>See *supra*, p. 334-335.

<sup>175</sup>A 2002 Urban Institute report by Deborah Korbes and Jeff Rohaly comparing the CBO and JCT dynamic scoring efforts appears on the Web at <http://www.urban.org/url.cfm?ID=310316>.

<sup>176</sup>See *supra*, p. 336-337.

<sup>177</sup>See *supra* note 78.

<sup>166</sup>As indicated in *supra* note 90, statistics of income data become available about six months after the close of the filing period for a given tax year.

<sup>167</sup>See *supra*, p. 347.

<sup>168</sup>See *supra*, p. 355-356.



capable of providing high-quality, public-spirited commentary and are willing to do so if given the opportunity.

Government agencies other than the JCT and Treasury are another possible source of comment regarding revenue estimates. Interested agencies might include the Congressional Research Service, the GAO, and executive branch departments outside Treasury. All have the resources needed to provide thoughtful critiques of the estimating process.

Further, at least six think tanks and research groups have developed an ability to estimate broad-based individual income tax provisions that can be simulated with a tax model using the IRS public-use file. As outlined earlier,<sup>178</sup> those groups span the political spectrum from left to right. If the information available to those groups were enhanced in the ways outlined earlier, they would be poised to make a significant contribution<sup>179</sup> to the debate over the revenue estimating process. Several universities would also be able to contribute to the debate.

However, those private charitable and educational groups currently operate on a shoestring in most cases. To compete effectively with Treasury and the JCT, they would have to find the money to make modest enlargements in their revenue estimating staffs. The situation seems made to order for demonstration projects lasting three to five years, funded by private philanthropy.

After the three to five year period, those groups could either convert their revenue estimating prowess into a self-supporting enterprise<sup>180</sup> or, if the ongoing need for their work had been demonstrated, ask for continued foundation support. In either event, their public-spirited competition, along with similar competition from else-

where in the private sector, would push Treasury and the JCT to improve their own procedures and would provide examples of how to do that.

## V. Conclusion: How to Catalyze Change

Public-private competition can lay the groundwork for changes in revenue estimating transparency practices, but competition by itself is unlikely to be the catalyst that is needed to get changes underway. In the interim, in the words of one distinguished economist with both Treasury and private-sector tax experience, "Treasury and JCT will stonewall, with perhaps a dose of arrogance or hubris to boot."

One hopes that prediction will not come true, but it might. If it does, an outside catalyst will be needed to produce action on the transparency issues discussed in this report.

Congress is the most likely catalyst. It can set the rules, not only for the JCT revenue estimators but also for those at Treasury. Further, as mentioned earlier,<sup>181</sup> individual members of Congress, including members of the taxwriting committees, have sometimes expressed their unhappiness with the current lack of revenue estimating transparency. If a senior member of a taxwriting committee became consistently interested in transparency issues, change would occur sooner rather than later.

Alternatively, a blue ribbon commission sponsored by a government agency, nonprofit group, or accounting or law firm might get the ball rolling, especially if it included some of the individuals who lived through the revenue estimating wars of the 1980s and 1990s. Many of them now occupy senior positions in both government and the private sector, and if the commission included at least some of those individuals, it might have the influence required to produce change.

One thing is sure: Change is needed in the revenue estimating transparency practices at both Treasury and the JCT. The current secrecy aids no one. The agencies themselves, the professions, and the public would all benefit from greater openness. Given those facts, change is desirable and perhaps inevitable, even though it is not now possible to outline the circumstances that will produce it.

<sup>178</sup>See *supra*, p. 344.

<sup>179</sup>The revenue and distributional analyses provided by the Urban-Brookings Tax Policy Center in 2003-2004 with respect to tax proposals illustrate how private analyses can inform and enrich the public debate. Those estimates are available at <http://taxpolicycenter.org/TaxModel/tmdb/tmtemplate.cfm>.

<sup>180</sup>Private firms have made a substantial amount of money doing revenue estimating for private clients. Nonprofit organizations could do the same. As nonprofits, they must of course create and enforce strict rules to assure the integrity and independence of their estimating activities. A requirement that all their estimates be published in full after peer review might be among those rules. To keep the playing field level with that of other private firms, earnings from nonprofit revenue estimating should be subject to unrelated business income tax.

<sup>181</sup>See the discussion of congressional calls for greater revenue estimating transparency *supra*, p. 354.