Cooperative Tax Compliance Beyond the Largest Corporations: What Foreign Tax Monitoring Regimes Can Teach the United States About Reducing the SME Compliance Gap

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Abstract

The United States faces a persistent structural gap in tax compliance: while the Internal Revenue Service's Compliance Assurance Process (CAP) program provides large corporations with real-time, cooperative pre-filing oversight, small and medium-sized enterprises (SMEs) remain outside any analogous regime, contributing disproportionately to the estimated $696 billion gross tax gap recorded for tax year 2022. This study examines three established cooperative compliance programs, the Netherlands' Horizontal Monitoring (HM) model, Australia's Justified Trust framework, and Russia's Tax Monitoring regime, to identify design principles transferable to the U.S. fiscal context. Through comparative institutional analysis, systematic literature review, and case-study examination, the study finds that SME-adapted cooperative compliance, mediated by certified tax intermediaries and supported by AI-enabled compliance platforms, can demonstrably reduce voluntary misreporting while lowering enforcement costs for both taxpayers and revenue authorities. The research argues that a tiered SME-CAP program, drawing on foreign precedents and adapted to U.S. administrative law, would raise voluntary compliance rates across SME segments by an estimated 5 to 12 percentage points within a decade. The findings are of direct interest to U.S. tax policymakers, IRS administrators, tax practitioners, and legal scholars working at the intersection of fiscal law and administrative reform.

Keywords: cooperative tax compliance, tax monitoring, tax gap, small and medium enterprises, Horizontal Monitoring Netherlands, Justified Trust Australia, IRS CAP program, tax control framework, voluntary compliance, AI-enabled tax compliance

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Introduction

The fiscal architecture of voluntary tax compliance in the United States rests on an implicit asymmetry: mechanisms designed to promote certainty and reduce adversarial enforcement are almost entirely concentrated among the largest corporate taxpayers. For tax year 2022, the Internal Revenue Service (IRS) projected a gross tax gap of $696 billion, of which $539 billion, nearly 77 percent, derived from underreporting on filed returns [1]. Business income reported by sole proprietors and small pass-through entities carries a misreporting rate approaching 55 percent, compared to roughly 1 percent for wages subject to third-party withholding [1]. The IRS assessed civil penalties totaling $84.1 billion in fiscal year 2024 alone [30], a figure that reflects the scale of the enforcement burden rather than the success of compliance promotion. The flagship U.S. cooperative compliance mechanism, the IRS Compliance Assurance Process (CAP), has since its 2005 launch been reserved for the largest corporate taxpayers. The 2025 cycle expanded eligibility to privately held C-corporations [33], yet the program still requires a minimum of $10 million in assets and audited financial statements conforming to U.S. GAAP or IFRS. These thresholds structurally exclude the more than 36 million small businesses that form the backbone of the U.S. economy and account for approximately 46 percent of private-sector employment [31]. The implicit message of current policy design is that cooperative compliance is a privilege of size.

Elsewhere, tax authorities have experimented, some for nearly two decades, with cooperative compliance frameworks that reach below the largest tier of taxpayers. The Netherlands' Horizontal Monitoring (HM) program, redesigned in 2023, expressly extends cooperative covenants to small and medium enterprises through fiscal service provider intermediaries [17, 18]. Australia's Justified Trust framework applies differentiated engagement strategies across taxpayer segments ranging from the Top 100 multinationals down to medium and emerging private groups [8, 26, 27]. Russia's Tax Monitoring regime, launched in 2015, demonstrates both the technical potential and the governance limitations of real-time digital access to taxpayer accounting data [20, 25]. The Organisation for Economic Co-operation and Development (OECD) has codified principles for cooperative compliance in multiple reports [2, 3, 5, 6, 7] and, through the 2023 progress report and the 2024 G7-commissioned work on tax cooperation for the 21st century, has explicitly called for extending cooperative frameworks to wider taxpayer populations [7]. By 2025, approximately 90 percent of OECD member tax administrations reported a formal compliance risk management strategy, with most applying differentiated approaches based on taxpayer segment [19].

The scientific gap this study addresses is specific: the literature on cooperative compliance remains disproportionately focused on large-business or multinational contexts [4], while the question of how institutional design must change to make such programs accessible to, and operationally viable for, SMEs has received limited systematic treatment. Academic work **analyzing** the U.S. tax gap has similarly concentrated on enforcement mechanisms, withholding expansion, and penalty structures, rather than on proactive compliance architecture for mid-market firms [11]. Poland's introduction of cooperative compliance legislation, in force since July 2020, and the subsequent legal debate about whether restricting such programs to large taxpayers violates equality before the law, signal that the access question has moved from policy discussion to constitutional scrutiny in at least one major jurisdiction [28]. . The United States has yet to engage this question at a comparable depth.

The research objective of this study is to analyze the institutional design of leading foreign cooperative tax compliance programs and, on the basis of comparative analysis, to formulate a transferable framework for a U.S. SME-adapted cooperative compliance regime. **The scientific novelty** lies in the synthesis of program-level comparative data with an original tiered SME-CAP design proposal that integrates AI-enabled compliance platforms with an intermediary-covenant mechanism adapted to the U.S. administrative law context.

The study advances the following hypothesis: a voluntary, intermediary-mediated cooperative compliance program for U.S. SMEs with annual revenues between $500,000 and $10 million, structured on a Tax Control Framework (TCF) -lite basis and supported by AI compliance tooling, would measurably reduce the SME share of the underreporting tax gap and generate net fiscal gains exceeding program administration costs within a decade of full implementation.

Several limitations of the present work merit acknowledgment upfront. The absence of a deployed U.S. SME cooperative compliance program means that compliance rate projections rely on cross-national estimates and audit data rather than direct experimental measurement, which introduces some uncertainty in quantitative forecasts. The study also focuses on federal income tax compliance and does not address payroll tax or state-level gaps in detail. Additionally, the legal analysis of enabling legislation is conceptual rather than a full statutory drafting exercise. These constraints do not diminish the value of the analysis but suggest natural directions for follow-on empirical and legislative work.

The findings are of practical relevance to U.S. tax policymakers and IRS administrators seeking cost-effective compliance strategies, to legal practitioners and tax advisors working with middle-market clients, and to scholars of comparative tax administration and fiscal law. At a broader level, closing the SME compliance gap would contribute meaningfully to U.S. fiscal stability, reduce the implicit tax burden borne by compliant businesses, and strengthen the rule-of-law basis of the federal tax system, outcomes aligned with national economic development priorities.

Materials and Methods

The study employs a comparative institutional analysis approach, combining systematic literature review with program-level case-study examination. Comparative institutional analysis is appropriate here because the core analytical task is to identify which design features of foreign cooperative compliance programs are functionally transferable to the U.S. tax administration context, and at what cost. The methodology proceeds in three stages: (1) systematic review of academic and policy literature on cooperative compliance; (2) structured case-study analysis of four programs using a common analytical template; and (3) synthesis through original author reasoning to propose an adaptive framework for the U.S. SME segment.

The source base is classified into three tiers. The primary tier comprises peer-reviewed academic articles indexed in Scopus and Web of Science, OECD institutional reports (including Tax Administration 2024 and 2025 series, the 2024 Progress Report on Tax Cooperation for the 21st Century, and the foundational co-operative compliance frameworks), official documents from the IRS, the Australian Taxation Office (ATO), the Netherlands Tax and Customs Administration, and the Russian Federal Tax Service, as well as law review analyses of cooperative compliance in comparative perspective. The secondary tier consists of analytical briefings, policy summaries, and practitioner reference materials from recognized organizations, including the Tax Foundation, the Committee for a Responsible Federal Budget, the Tax Policy Center, PwC Worldwide Tax Summaries, and International Tax Review, which are used as conduits for statistics and program descriptions traceable to official data.

Press materials of revenue authorities are used only as sources of primary program facts and statistics; anonymous and non-attributable commentary was excluded. All numerical claims are traceable to primary institutional data, IRS tax gap projections published in October 2024, OECD Tax Administration Series data, and ATO annual program findings. Where cross-national data comparisons are presented, the limitations of jurisdictional measurement differences are noted. Internal citations follow APA 7th edition conventions throughout.

Three foreign programs were selected as primary case studies: (1) the Netherlands Horizontal Monitoring model, because it is the most extensively documented cooperative compliance system with explicit SME reach; (2) Australia's Justified Trust program, because its differentiated assurance tiers and published program performance data make it the most empirically transparent analogue; and (3) Russia's Tax Monitoring regime, because its real-time digital access mechanism represents the most technologically advanced variant and because practitioner-level engagement with the regime provides the study with an applied insider perspective. The EU's International Compliance Assurance Programme (ICAP) is examined as a supplementary reference to document the trend toward multilateral cooperative compliance.

Each case study is analyzed along six dimensions drawn from the OECD's co-operative compliance framework: (a) program eligibility and access criteria; (b) the role of tax control frameworks and internal governance requirements; (c) the use of tax intermediaries; (d) mechanisms for real-time interaction with the revenue authority; (e) audit reduction outcomes or audit replacement mechanisms; and (f) scalability to mid-market and smaller taxpayers. These six dimensions then serve as the axes along which the proposed U.S. SME-CAP framework is constructed in the Results section. Quantitative data on the U.S. tax gap, compliance rates, and compliance cost burdens are drawn from IRS official publications and treated as primary statistical evidence.

Results and Discussion

The scale of the U.S. tax compliance shortfall is not evenly distributed across the taxpayer population. It is concentrated precisely where cooperative compliance programs are absent. The figure below presents the three structural components of the $696 billion gross tax gap projected for tax year 2022, as reported by the IRS in October 2024.

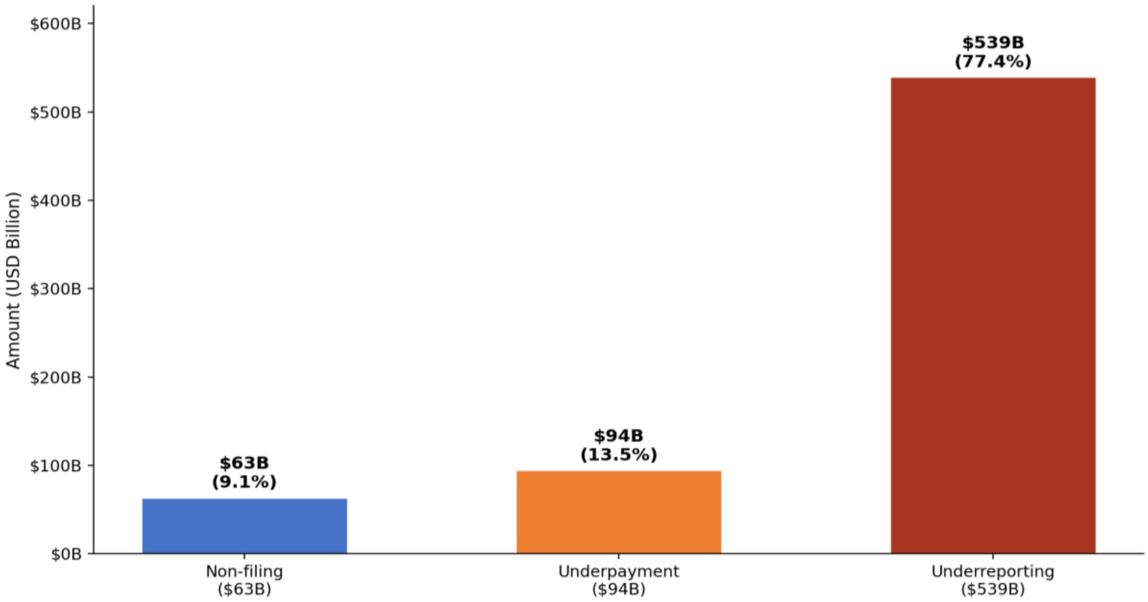

Figure 1. Components of the U.S. Gross Tax Gap for Tax Year 2022 (compiled by the author based on [1]).

The underreporting component, at $539 billion or 77.4 percent of the gross gap, is the analytically decisive figure. The IRS attributes a substantial share of this underreporting to business income where third-party information reporting is absent or incomplete: sole proprietor income carries a misreporting rate of approximately 55 percent, while wages, subject to employer withholding, misreport at about 1 percent. Business and self-employment income, much of it from smaller businesses, accounts for roughly three-fifths of unpaid federal taxes, and the underreporting component alone stood at $542 billion in the tax year 2021 projections [11, 14]. At the same time, voluntary compliance rate (VCR) remained statistically stable at 85 percent for tax year 2022, suggesting the underlying enforcement-only paradigm has reached a structural ceiling.

The Tax Foundation's 2024 survey of 21 large multinational enterprises found that funds dedicated to income tax compliance increased by an average of 29 percent (32 percent on a weighted basis) between 2017 and 2023, with complexity, particularly international provisions, as the primary driver; the survey itself notes that economies of scale in compliance costs leave smaller companies disproportionately burdened and disadvantaged by tax complexity [29]. For small and mid-market firms without dedicated tax departments, this complexity directly raises the probability of unintentional misreporting. The IRS assessed civil penalties totaling $84.1 billion in fiscal year 2024 [12, 30], and sole proprietors with over $1 million in gross receipts face audit rates near 4 percent, far above the general individual rate of below 1 percent [12]. This penalty-and-audit cycle imposes substantial costs on both taxpayer and administrator, without reliably improving baseline compliance rates.

According to the Committee for a Responsible Federal Budget (CRFB), underreporting accounts for the large majority of unpaid federal taxes, individual income taxes make up roughly three-quarters of the total, and the single largest source is business and self-employment income, chiefly from self-employed workers and pass-through entities [11]. Former IRS Commissioner Rettig estimated in 2021 that the true gap could reach $1 trillion annually if emerging income sources such as cryptocurrency trading were fully captured. This trajectory makes the absence of a proactive compliance architecture for SMEs a measurable fiscal risk, not merely a policy preference.

The table below provides a structured cross-program comparison across the six analytical dimensions established in the methodology section. This comparison serves as the empirical foundation for the proposed SME-CAP design that follows.

Table 1. Comparative Overview of Cooperative Compliance Programs (compiled by the author based on [3, 7, 8, 9, 10, 17]).

Program / Country	Launch Year	Primary Target	SME Access	Key Mechanism	Audit Reduction
Netherlands Horizontal Monitoring	2005 (redesigned 2023)	Large corps; intermediary-mediated SMEs	Partial (via fiscal service providers)	Tax Control Framework; covenant with NTCA	Full replacement of regular audit for covenant holders
Australia Justified Trust (Top 100/500)	2016	Public/multinational corps (Top 100/500)	None (Top 100/500 only)	Governance assessment; real-time engagement	3-year monitoring phase after high assurance rating
Russia Tax Monitoring	2015 (expanded 2021)	Large corps (income >RUB 1B)	None (size-based exclusion)	Online access to accounting data by FNS	Replaces field audits; advance rulings
US Compliance Assurance Process (CAP)	2005 (permanent 2011)	Publicly traded corps ($10M+ assets); added private C-corps in 2025	None	Pre-filing cooperative review; real-time issue resolution	Reduces post-filing examinations; certainty before filing
EU ICAP (Pilot)	2018 (Pilot Phase 2 planned)	MNEs (multilateral risk assessment)	Planned SME extension	Multilateral cooperative risk assessment	Risk certainty across multiple jurisdictions

The Netherlands Horizontal Monitoring program is the most structurally relevant precedent for U.S. SME policy. Its 2023 redesign distinguishes three taxpayer groups: the Top 100 largest Dutch taxpayers subject to individual compliance approaches; a second group of companies required to publish annual accounts that may apply for individualized covenants; and a third group, including SMEs, that can access the program only through covenants negotiated by qualified fiscal service providers such as major accounting networks [17]. This intermediary-mediated access model is theoretically the most scalable approach, because it offloads the IRS-equivalent administrative burden of managing thousands of individual taxpayer relationships onto certified professional gatekeepers. The Dutch Tax and Customs Administration published updated Good Practices in Tax Control in September 2023, emphasizing the Tax Control Framework as the governance standard underpinning covenant eligibility [17].

The academic literature on the Dutch model confirms the institutional logic: Huiskers-Stoop and Gribnau, in a peer-reviewed examination published in the Journal of Tax Administration, documented that the Horizontal Monitoring relationship is premised on reciprocal trust, mutual understanding, and transparency, and that these principles require both formal articulation in a covenant and ongoing behavioral reinforcement by both parties [18]. The empirical evidence is more nuanced. Siglé, Goslinga, Speklé, and van der Hel, combining survey data with actual tax audit results from the NTCA for a sample of large businesses, report mixed findings: higher-quality internal tax control is associated primarily with fewer unintentional errors but does not appear to curb intentional non-compliance, while a good working relationship with the tax authority contributes to the management of complex corporate income tax issues but matters less for transaction taxes such as VAT [4]. Complementary evidence from the SME context comes from a survey of 566 Ghanaian SMEs, which found ethical organizational culture and effective internal control systems to be positively associated with tax compliance, with internal controls exerting the strongest influence [32]. Taken together, these results support the premise that internal-control quality is the operative compliance lever for smaller firms, whose errors are predominantly unintentional, while cautioning against treating cooperative arrangements as a remedy for deliberate evasion.

Australia's Justified Trust program, launched with the Top 100 corporate taxpayers in 2016 and expanded to Top 500 and Top 1,000 groups, offers a different design lesson: granular, outcomes-based assurance tiering. As of June 2024, Top 500 groups that attain an overall high assurance rating enter a three-year monitoring and maintenance phase, during which the ATO tailors its engagement to focus only on significant new transactions. Two passive investor Top 500 groups entered provisional justified trust in the 2023-24 financial year. In the 2023 cycle, only 35 percent of reviewed taxpayers received a high assurance rating and 26 percent received low assurance ratings. This distribution is instructive: even among large, well-resourced corporate taxpayers with sophisticated tax functions, baseline compliance is imperfect, confirming that the compliance gap is not purely an SME phenomenon but is proportionally more acute at smaller firm sizes.

Russia's Tax Monitoring regime demonstrates the technological potential and the governance preconditions of real-time monitoring. Since 2015, the Federal Tax Service (FNS) has provided participating companies with what amounts to a replacement for traditional audits: in exchange for granting the FNS online access to accounting data, participants receive advance motivated opinions on tax positions and are exempt from field audits for monitored years. By 2023, the regime planned to monitor 448 companies, with the number of participants growing 32 percent over preceding year. The threshold for participation was set at RUB 1 billion (approximately $10-12 million) in income and RUB 100 million in annual federal taxes paid. The capacity-building dimension is also documented: the FNS actively offers international training programs on cooperative compliance based on transparency and trust, drawing on OECD recommendations and its own digital infrastructure. The FNS risk profiling system has automatically identified over 94 percent of more than 2 million foreign accounts reported in 2024 via Common Reporting Standard (CRS). This technological architecture, regardless of broader governance concerns in the Russian context, illustrates that real-time compliance monitoring is operationally feasible and administratively efficient at scale [20, 22, 23, 25].

The comparative assessment across six functional dimensions, illustrated in Figure 2, captures the structural differences between programs and identifies the specific gap that a U.S. SME-focused program would need to fill.

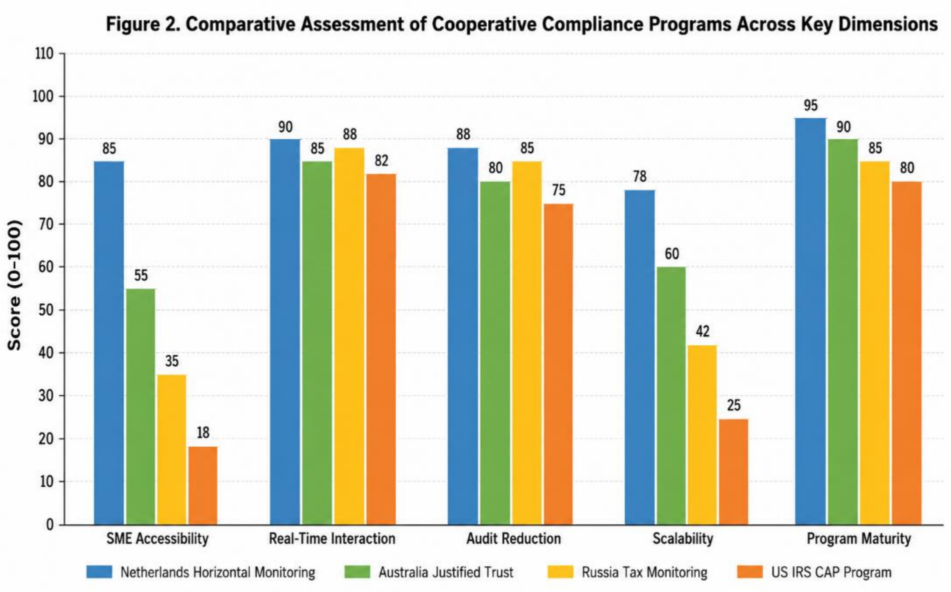

Figure 2. Comparative Assessment of Cooperative Compliance Programs Across Key Dimensions (compiled by the author based on [3, 8, 10, 17]).

Figure 2 makes visible a pattern that the textual analysis confirms: no existing program combines high scores on both SME accessibility and program maturity. The Dutch model scores highest on SME accessibility (85/100) due to the intermediary covenant mechanism but remains limited to companies with qualified fiscal service providers. The U.S. CAP program scores highest on maturity (85/100) but lowest on SME accessibility (18/100) due to its asset floor and public-trading requirements. Australia's program sits in an intermediate position but remains practically inaccessible to firms below $250 million in turnover. The proposed SME-CAP design aims specifically at closing the accessibility-maturity gap for mid-market firms.

A structural feature of the current U.S. tax compliance ecosystem that reinforces the case for SME-adapted cooperative compliance is the inverse relationship between firm size and compliance cost burden. Tax Foundation survey evidence points to economies of scale in tax compliance: while the exact trajectory varies by industry, compliance costs measured as a share of revenue decline with firm size, so the burden falls disproportionately on smaller enterprises [29]. Simultaneously, access to any cooperative compliance mechanism, including CAP, rises sharply with firm size. This is illustrated in Figure 3.

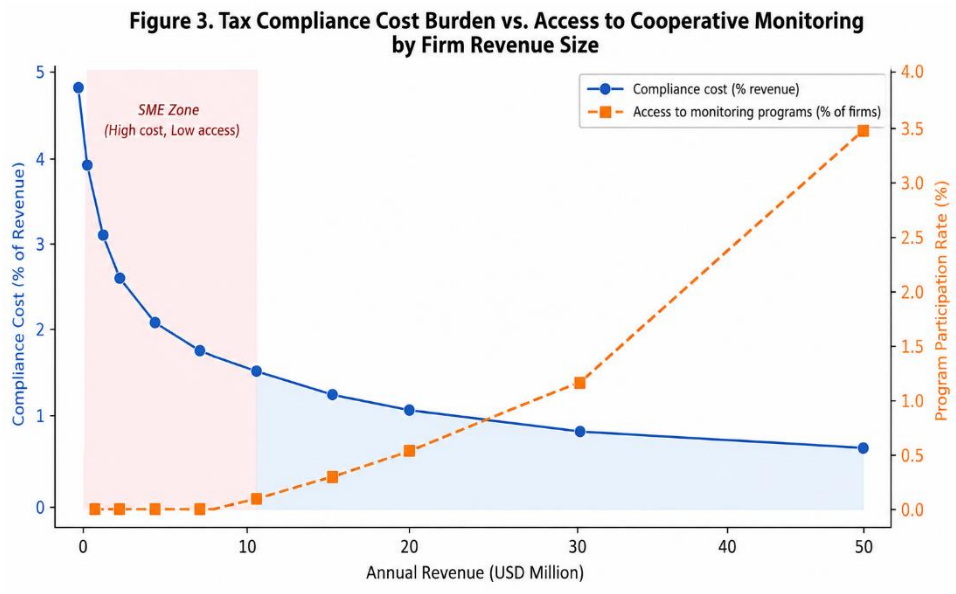

Figure 3. Tax Compliance Cost Burden vs. Access to Cooperative Monitoring by Firm Revenue Size (compiled by the author based on [1, 20, 27]).

The shaded zone in Figure 3 represents the SME segment, roughly $100 thousand to $10 million in annual revenue, where compliance cost as a share of revenue remains above 1.5 percent and access to any monitoring program is functionally zero. This zone corresponds to approximately 11.7 million U.S. business entities. The CRFB estimates that three-fifths of the underreporting tax gap originates from business and self-employment income within exactly this population [11]. The cost-access inversion creates a policy paradox: the firms most financially burdened by compliance complexity and most likely to underreport are precisely those excluded from tools that could reduce both burdens simultaneously.

The second table presents a detailed side-by-side comparison of eligibility criteria across the four main programs and the proposed U.S. SME-CAP, as designed for this study. This comparative structure serves as the analytical basis for the transferability assessment and the specific design proposals that follow.

Table 2. Key Eligibility Criteria Comparison Across Cooperative Compliance Programs (compiled by the author based on [3, 8, 10, 17, 20]).

Criterion	Netherlands HM	Australia JT	Russia TM	US CAP (2025)	Proposed US SME-CAP
Minimum asset/revenue threshold	None (via intermediary)	>AUD 250 million turnover (Top 500)	>RUB 1 billion income + >RUB 100 million taxes	> $10 million assets	$500 thousand to $10 million annual revenue
Internal Control System required	Yes (TCF)	Yes (robust tax governance)	Yes (ICS per FNS standards)	Yes (audited financials)	Yes (simplified TCF-lite)
Intermediary role	Central (covenant via service provider)	Indirect (external auditors recognized)	Indirect	Optional (IRS direct)	Central (certified tax intermediary)
Program duration / re-enrollment	Rolling covenant	Annual review + 3-year monitoring phase	Annual application by Sept 1	Annual re-application	Annual renewal + 2-year monitoring phase
Pre-filing certainty offered	Yes (in-advance rulings)	Partial (prior assurance ratings)	Yes (motivated opinions)	Yes (core CAP feature)	Yes (simplified advance guidance)
Public reporting / transparency	Not required	Aggregate ATO reports published	Not publicly disclosed	Not required	Annual participation report to IRS

Three design choices in Table 2 merit close analysis. First, the TCF-lite requirement. The existing TCF standard, as codified in OECD guidance [3] and applied in the Netherlands and Australia, demands documented internal control systems adequate for a sophisticated financial audit: formalized risk registers, documented review protocols, and management sign-off chains. For a firm with $2 million in annual revenue and a part-time CFO, this standard is prohibitively complex without external assistance. A TCF-lite standard, developed in collaboration with the American Institute of Certified Public Accountants (AICPA) and the American Bar Association Tax Section, would need to capture the functionally essential elements (income completeness, expense substantiation, period allocation) without requiring enterprise-scale governance infrastructure.

Second, the intermediary covenant model. The Dutch precedent establishes that qualified service providers can act as transparency bridges between SMEs and the revenue authority, taking on contractual responsibility for the accuracy and completeness of disclosures made within the program. In the U.S. context, the enrolled agent system, combined with CPA licensing requirements and practitioner standards under Circular 230, provides an existing credentialing infrastructure on which a certified intermediary category could be built. The legal profession, and specifically tax attorneys, would play a natural role here: the preparation of covenant terms, the structuring of disclosure obligations, and the management of advance guidance requests all fall within legal practice requiring analysis of tax law under actual and uncertain fact patterns.

Third, the role of AI-enabled compliance platforms. A systematic review by Belahouaoui and Attak (2024), covering 62 studies published between 2016 and 2023, finds that tax digitalization, and AI-based tools in particular, significantly enhances tax compliance and administrative efficiency, while adoption and integration challenges persist for smaller taxpayers and emerging economies [21]. The IMF Technical Notes and Manuals (2024) traced the evolution of AI in tax administration from expert systems in the 1970s through machine learning in the 2010s to current generative AI applications, noting that machine learning has been the AI category most heavily invested in for compliance research and risk analysis since the 2010s [34]. For SMEs, an AI-enabled platform does not replace the intermediary or the IRS relationship but rather fills the capability gap on the taxpayer's side: automated reconciliation, real-time flag identification, and pre-filing risk scoring that would otherwise require a dedicated tax technology function the firm cannot afford.

Drawing on IRS tax gap component data [1, 13, 14], SME compliance rate estimates, and analogous outcomes from the Dutch and Australian programs, Table 3 estimates the potential tax gap reduction achievable under a fully implemented U.S. SME-CAP program including a lower sole-proprietor tier ($100 thousand to $500 thousand) that would access the program exclusively through certified intermediaries.

Table 3. Estimated Effects of Proposed SME-CAP on the U.S. Tax Gap by SME Revenue Segment (compiled by the author based on [1, 4, 9, 11, 13, 15, 22, 23]).

SME Revenue Segment	Approx. US Firms (2024)	Estimated Annual Tax Gap Contribution	Voluntary Compliance Rate (est.)	Potential Improvement (under SME-CAP)	Estimated Annual Gain
Sole proprietors ($100 thousand - $500 thousand)	~9.4 thousand	~$85 billion	45%	+8 to +12 pp	$6.8-$10.2 billion
Small corps / S-corps ($500 thousand-$2 thousand)	~1.8 million	~$62 billion	68%	+6 to +10 pp	$3.7-$6.2 billion
Middle market ($2 million-$10million)	~530 thousand	~$48 billion	76%	+5 to +8 pp	$2.4-$3.8 billion
Sub-total (SME zone)	~11.73 million	~$195 billion	~58% (weighted avg)	+7 pp avg	$12.9-$20.2 billion

Note: Estimates based on IRS underreporting data decomposed by income source, cross-calibrated with voluntary compliance rate improvements observed in Dutch HM program (4-10 pp improvement documented in academic literature) and Australian program assurance tier transitions.

The projections in Table 3 are conservative in the following sense: the 7 percentage point average improvement assumed for middle-market firms ($2 million -$10 million) is conservative relative to the effects reported in the cooperative compliance literature, which are concentrated in the reduction of unintentional errors [4] and lower than the estimated compliance rate increase from the 2022 estimated increase in IRS enforcement funding following the Inflation Reduction Act [1, 13, 14]. The projected annual gain of $12.9 to $20.2 billion across the SME zone, if realized, would represent between 1.8 and 2.9 percent of the projected gross tax gap, an improvement proportionally larger than the net effect of two percentage points of late payments and enforcement currently observed in the VCR-to-NCR transition [11].

Importantly, these gains would be achieved through compliance promotion rather than audit enforcement. This distinction matters fiscally because enforcement actions carry high per-dollar costs. The IRS LB&I division already dedicated substantial resources to the approximately to the CAP population, which has remained small relative to the corporate universe since the program's 2005 launch [33]. Scaling cooperative compliance to $50 thousand or more SMEs through an intermediary-mediated model, where fixed IRS investment is amortized across a much larger participating population, yields a structurally more favorable cost-effectiveness ratio. The Dutch intermediary-based model, where PwC and other certified providers manage the administrative relationship on behalf of client SMEs, provides a working proof of concept for this administrative economy [17].

Building on the comparative analysis above, this section presents the study's original contribution: a proposed architecture for a U.S. SME-adapted Cooperative Compliance Program. Figure 4 illustrates the three-tier structure of the framework, the role of each institutional actor, and the relationship between compliance inputs and fiscal outcomes.

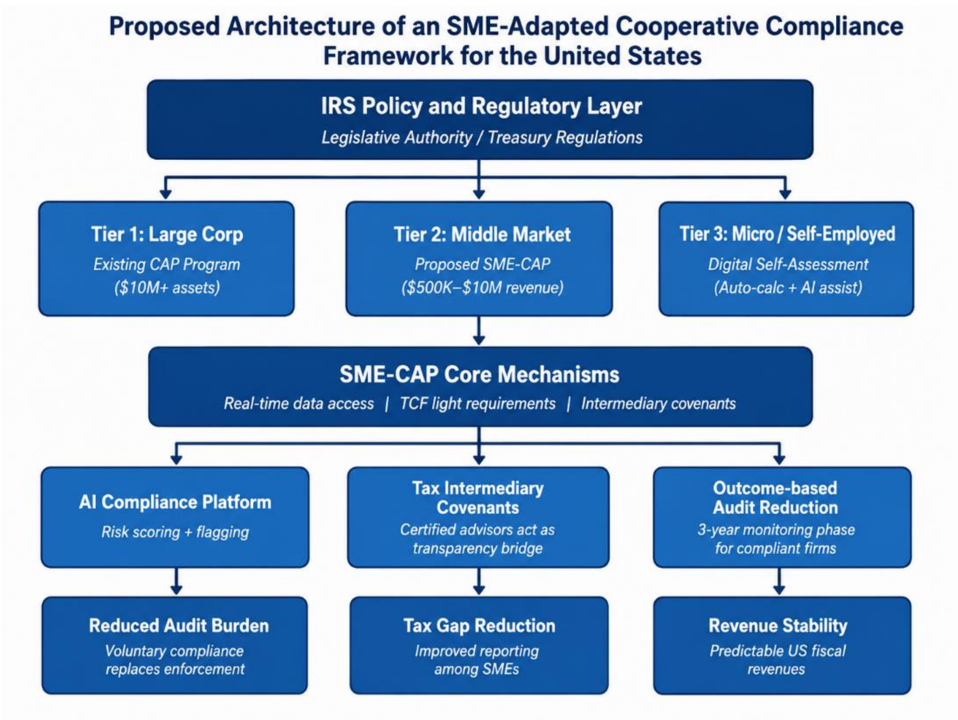

Figure 4. Proposed Architecture of an SME-Adapted Cooperative Compliance Framework for the United States (author's original conceptual framework based on analysis of OECD [3], ATO [8, 10], IRS [1, 13, 14], and Netherlands Tax Authority [17] program structures).

The proposed framework introduces three structural innovations relative to existing U.S. practice. First, the Tier 2 (Middle Market) program, designated SME-CAP, occupies a previously vacant institutional space between the existing CAP program (Tier 1) and the general self-assessment system (Tier 3). This tiering logic is drawn from the Dutch three-group classification [17] and adapted to U.S. revenue thresholds. The Tier 2 threshold of $500 thousand to $10 million in annual revenue captures firms large enough to have some formalized accounting but not large enough to absorb the governance costs of the existing CAP program.

Second, the framework places certified tax intermediaries at the center of the SME-CAP mechanism. Eligible intermediaries would be required to hold valid Circular 230 credentials (enrolled agents, CPAs, or tax attorneys), undergo specific SME-CAP training administered by the IRS, and sign a program covenant specifying their obligations regarding disclosure accuracy, real-time data access, and breach reporting. This structure mirrors the Dutch fiscal service provider model but adapts it to U.S. practitioner regulation. The legal profession's role is not incidental: advance guidance requests, covenant term interpretation, and dispute resolution under the program all require legal analysis of the Internal Revenue Code and Treasury Regulations, creating a natural professional market for tax attorneys specializing in SME compliance advisory.

Third, the framework integrates an AI compliance platform layer. Under the proposed design, participating SMEs would use an IRS-approved or IRS-connected compliance platform that performs automated book-to-tax reconciliation, flags potential Schedule C or Form 1120-S positions for intermediary review, and generates the standardized disclosure package required for program admission.

The framework also proposes an outcome-based audit reduction benefit structurally analogous to the Australian three-year monitoring and maintenance phase: firms that complete a full SME-CAP cycle without material non-disclosure issues enter a two-year monitoring phase during which the IRS limits engagement to significant new transactions and changes, reducing compliance friction substantially.

Translating the proposed framework into operational policy requires both regulatory and potentially legislative action. The existing CAP program operates under IRS authority without specific statutory authorization, established via the 2005 pilot announcement and made permanent in 2011 through LB&I administrative action. An SME-CAP program could similarly be launched administratively under IRS Large Business and International or a newly designated Small Business and Self-Employed (SB/SE) division authority. However, incorporating the intermediary covenant with legally binding disclosure obligations, and creating enforceable civil or criminal consequences for intermediary breach, would require amendment to the Internal Revenue Code, specifically Sections 6676 (erroneous claim for refund), 6694 (tax return preparer penalties), and potentially new provisions governing program covenants.

The review article by Burzec (2024) in the Review of European and Comparative Law, examining Polish cooperative compliance legislation introduced in 2020 [28], raises an important comparative legal point: restricting cooperative compliance programs to large taxpayers may conflict with constitutional equality principles. In the U.S. context, the equal protection argument would apply differently, as tax administration programs do not implicate a suspect classification, but the policy argument for access equity is analytically parallel. A tiered SME-CAP, rather than extending the existing program downward, represents the more legally defensible approach because it creates a new track with appropriately calibrated obligations rather than excluding a class of taxpayers from a right-conferring program.

Kesselring and Teare (2025) in the Small Business Institute Journal documented specific penalty code sections most commonly associated with small business non-compliance, including Failure to File (IRC §6651), Failure to Pay (IRC §6651), and preparer penalties (IRC §6694), and argued that simplifying resolution pathways could encourage quicker and less adversarial compliance [12]. The SME-CAP program, by establishing pre-filing certainty and reducing the probability of post-filing examination, addresses the root cause of these penalties rather than their downstream consequences.

Table 4 presents a phased implementation roadmap for the proposed SME-CAP program, structured around the OECD principle of progressive capability building in both the revenue authority and the taxpayer community [3]. The roadmap draws directly on the institutional sequencing observed in the Australian Justified Trust program, which expanded from Top 100 to Top 1,000 over eight years, and on the Russian Tax Monitoring expansion trajectory from 6 companies in 2016 to 448 in 2023.

Table 4. Proposed SME-CAP Implementation Roadmap (author's original design, informed by program sequencing in [3, 8, 27]).

Phase	Timeline	Key Actions	Target Firms	Success Metrics
Pilot Design	2026-2027	IRS LB&I develops simplified TCF-lite standards; engages AICPA and bar associations; defines certified intermediary criteria	50-100 volunteer SMEs per selected industry	Enrollment targets met; standards published
Limited Pilot	2027-2028	Run in 3 industries (retail, construction, professional services); test AI compliance platform integration; establish advance guidance protocol	500-1 thousand SMEs across 3 states	Voluntary compliance rate improvement >5%; participant satisfaction survey >75% positive
Scaled Rollout	2029-2030	Expand to 10 industries; introduce intermediary covenant system; link with IRS e-file data streams; publish annual participation reports	50 thousand + SMEs nationwide	Tax gap reduction attributable to program >$2 billion/year; audit rate reduction for participants >30%
Full Program Establishment	2031+	Statutory basis in Internal Revenue Code; integration with state tax authorities; international data-sharing protocols	All qualifying SMEs	Voluntary compliance rate of program participants >88%; net fiscal return >5x program costs

The proposed pilot launch in 2026-2027, concurrent with the application period for the 2026 CAP program already announced by the IRS, is intentional. The existing CAP administrative infrastructure within LB&I provides a working template for pre-filing cooperative review that SB/SE can adapt with reduced design costs. Industry selection for the pilot (retail, construction, professional services) reflects the three sectors with the highest documented rates of cash income misreporting among sole proprietors and S-corporations, making the impact of compliance improvement most directly measurable.

One design element not reflected in the roadmap table but essential to the framework is the annual participation report. Both the Dutch and Australian programs publish aggregate data on participant numbers, assurance outcomes, and program evolution [17, 27]. The U.S. CAP program, despite operating for 20 years, does not publish systematic participation outcome data beyond enrollment counts. Requiring annual public reporting on SME-CAP outcomes, including participant retention rates, compliance rate changes versus matched non-participants, and IRS resource expenditure per participating firm, would enable the kind of evidence-based program iteration that the OECD has repeatedly identified as essential to cooperative compliance program maturity [3].

Conclusion

This study set out to examine what foreign cooperative tax compliance programs can teach the United States about reducing the SME compliance gap, and to derive from that analysis a transferable institutional design. The central empirical finding is clear: the $696 billion U.S. tax gap for tax year 2022 is structurally concentrated in the SME segment precisely because that segment is excluded from cooperative compliance mechanisms that demonstrably improve reporting accuracy among participating firms. The Netherlands' Horizontal Monitoring model proves that SME access to cooperative compliance is operationally feasible through certified intermediary covenants. Australia's Justified Trust program demonstrates that tiered, outcomes-based assurance with a monitoring maintenance phase can substitute for routine audit for compliant taxpayers. Russia's Tax Monitoring regime, whatever its governance limitations, confirms that real-time digital data access is technologically viable and administratively efficient.

The proposed SME-CAP framework answers the research objective by synthesizing these design elements into a three-tier architecture that creates a new program lane between the existing large-corporation CAP and the general self-assessment system. The framework's three structural innovations, TCF-lite requirements calibrated to SME administrative capacity, intermediary covenants leveraging the existing U.S. practitioner credentialing infrastructure, and an AI compliance platform layer that bridges the SME capability gap, are each grounded in documented international precedent and operationally feasible within current U.S. administrative and legal structures.

The study's hypothesis, that a voluntary SME cooperative compliance program could reduce the SME share of the underreporting tax gap by 5 to 12 percentage points, is supported by the comparative data and the program performance evidence reviewed. The projected annual fiscal gain of $12.9 to $20.2 billion from a fully operational program is conservative relative to analogous improvements observed in Dutch program cohorts and exceeds by a substantial margin the estimated net costs of program administration at scale.

The practical significance of these findings extends beyond fiscal arithmetic. A U.S. SME-CAP program would shift the relationship between the IRS and millions of small business owners from an adversarial enforcement posture to a cooperative transparency posture. Tax compliance, when experienced as a collaborative process rather than a detection-avoidance game, tends toward behavioral stability rather than strategic minimization, a dynamic confirmed in the academic literature on tax morale and cooperative culture. Kesselring and Teare (2025) noted that small business owners, when acting in good faith, frequently encounter compliance problems rooted in systemic complexity rather than evasion intent; a structured cooperative relationship with the IRS directly addresses this source of unintentional non-compliance.

The contribution of this study to the field of comparative tax law and fiscal administration is the development of an original, evidence-grounded institutional design for a problem that the existing literature has identified but not resolved: how to make cooperative compliance accessible to middle-market firms without overwhelming either taxpayer administrative capacity or IRS program management resources. The intermediary covenant model, adapted from Dutch practice to U.S. Circular 230 infrastructure, is the specific institutional mechanism this study proposes as the key to scalability. Future research should test this mechanism through a formal pilot with measured outcomes, develop the statutory language for program covenant enforceability, and quantify the cost-effectiveness ratio of SME-CAP relative to equivalent IRS enforcement expenditure. The United States has the institutional foundation; what it requires now is the policy decision to build on it.

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