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TAX COMPLIANCE

Challenges to Corporate Tax Enforcement and Options to Improve Securities Basis Reporting

GAO Accountability · Integrity · Reliability

Highlights

Highlights of GAO-06-851T, a Testimony to Committee on Finance, U.S. Senate

Why GAO Did This Study

Corporate income taxes are expected to bring in about $277 billion in 2006 to help fund the activities of the federal government. Besides raising revenue, the tax alters investment decisions and raises concerns about competitiveness in an environment of increasing global interdependency. The complexity of the tax breeds tax avoidance, including an estimated $32 billion of noncompliance detected by the Internal Revenue Service (IRS).

This testimony provides information on trends in corporate taxes and opportunities to improve corporate tax compliance.

The committee also asked that GAO discuss recent work on the misreporting of capital gains income from securities sales and options to improve compliance.

This statement is based largely on previously published GAO work.

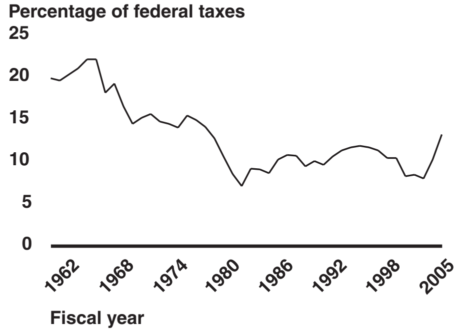
www.gao.gov/cgi-bin/getrpt?GAO-06-851T.

To view the full product, including the scope and methodology, click on the link above. For more information, contact Michael Brostek at (202) 512-9110 or brostekm@gao.gov.

What GAO Found

The corporate income tax is an important source of federal revenue and must be considered in dealing with the nation's long-term fiscal imbalance. Reexamining both federal spending and revenues, including corporate tax policy, corporate tax expenditures and corporate tax enforcement must be part of a multi-pronged approach to address the imbalance.

Corporate Income Tax Revenues as a Share of Federal Taxes, 1962-2005



Source: GAO Analysis of OMB Data.

The total amount of corporate tax avoidance, which includes the $32 billion in noncompliance estimated by IRS, is unknown. A complex tax code, complex business transactions, and often multinational corporate structures make determining corporate tax liabilities and the extent of corporate tax avoidance a challenge. Opportunities exist to improve corporate tax compliance and include simplifying the tax code, obtaining better data on noncompliance, continuing to oversee the effectiveness of IRS enforcement, leveraging technology, and sending sound compliance signals through increased collections of taxes owed.

In a companion report issued today, GAO found that many taxpayers misreport capital gains or losses, sometimes inappropriately underpaying their taxes and sometimes overpaying them. IRS has efforts in place to help ensure proper reporting of capital gains and losses, but these efforts face several obstacles. GAO found that expanding third-party information reporting on the cost basis of capital assets could help mitigate this problem if related problems are addressed. GAO suggested that Congress consider requiring brokers to report adjusted basis to taxpayers and IRS and requiring IRS to work with the securities industry to develop cost-effective ways to mitigate reporting challenges. GAO also recommended that IRS clarify its guidance on reporting capital gains and losses.