TAX SHELTERS

Services Provided by External Auditors

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Highlights

Highlights of GAO-05-171, a report to the Ranking Minority Member, Permanent Subcommittee on Investigations, Committee on Homeland Security and Governmental Affairs, U.S. Senate

Why GAO Did This Study

Recent legislative and regulatory changes have addressed the relationship between auditor-provided tax services and auditor independence. At this time, the federal regulatory community is exploring further changes.

To contribute to the discussion surrounding these changes, GAO's objectives were to determine (1) according to Internal Revenue Service (IRS) data, how many Fortune 500 companies obtained tax shelter services from their auditor; (2) according to IRS data, in how many Fortune 500 companies did the auditor provide the services to individual company officers or directors; and (3) whether selected Fortune 500 case study companies changed how they obtain tax services from their auditor in recent years.

For the first two objectives, GAO used IRS and Standard and Poor's data after finding they were sufficiently reliable for our work. GAO counted a company, officer, or director as obtaining a tax shelter service from the company's external auditor when an auditor that IRS identified as promoting a tax shelter also audited the company in at least one year that the shelter was in effect. For the third objective, independent of any IRS information, GAO selected case studies on the basis of geographic location and previous GAO contact. The companies are illustrative in nature and not intended to be representative of other companies.

www.gao.gov/cgi-bin/getrpt?GAO-05-171.

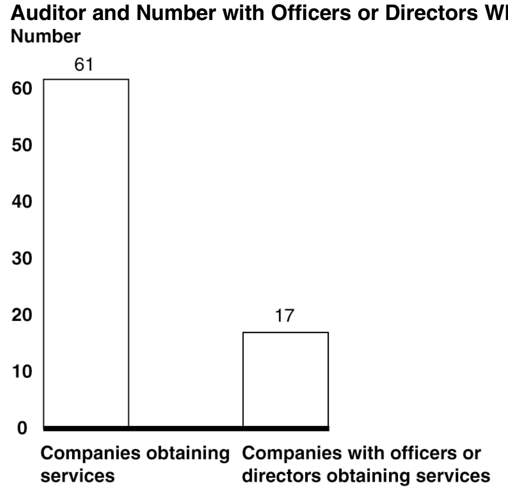
To view the full product, including the scope and methodology, click on the link above. For more information, contact Michael Brostek at (202) 512-9110 or brostekm@gao.gov.

What GAO Found

IRS data available on tax shelter services sometimes predate legislative and regulatory changes reflecting a heightened focus on auditor independence. However, both during this earlier period covered by some of the data and also following the recent changes, auditors were allowed to provide tax services, including tax shelter services, to firms they audited. According to IRS data, 61 Fortune 500 companies obtained tax shelter services from their external auditor during 1998 through 2003 for transactions generally reportable on tax returns sent to IRS. IRS considered some reportable transactions abusive, with tax benefits subject to disallowance under existing law, and other transactions to possibly have some traits of abuse. Estimated multi-year potential tax revenue lost to the federal government from the 61 companies' auditor-related transactions was about $3.4 billion (about $1.8 billion in categories IRS considered abusive). In 17 companies, at least one officer or director used the company's auditor to obtain individual tax shelter services. These numbers are imprecise because they have important limitations. These limitations, such as some transactions in IRS's database without tax shelter providers listed, are fully discussed in this report. Commenting on a draft of this report, IRS said that ongoing changes and recent legislation will enable it to address the data limitations noted.

According to their representatives, all eight case study companies adopted or refined policies or practices in 2002 or 2003 for pre-approving tax services or governing the tax services provided, such as who would provide them. All eight reported using their auditor for tax services during 2000 through 2003. Two told us of obtaining tax shelter services from their auditor, but one of them obtained the services before this period. Six of the eight reported officers or directors obtaining individual tax services from the auditor at some time since 2000, with four disallowing the practice later. None reported officers or directors using the auditor for individual tax shelter services.

Number of Fortune 500 Companies That Obtained Tax Shelter Services from Their External Auditor and Number with Officers or Directors Who Did So, 1998 through 2003



Source: GAO analysis of IRS and Standard and Poor's data.