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GAO Accountability·Integrity·Reliability

Highlights

Highlights of GAO-09-555, a report to the Committee on Finance, U.S. Senate

TAX GAP

Requiring Information Reporting for Charitable Cash Contributions May Not Be an Effective Way to Improve Compliance

Why GAO Did This Study

Individual taxpayers who misreport charitable cash contributions they deduct on their tax returns contribute to the tax gap, the difference between tax amounts taxpayers report and pay voluntarily and on time and the amounts they should pay under the law. The Internal Revenue Service (IRS) most recently estimated a gross tax gap of $345 billion for tax year 2001. One approach that tends to result in high levels of taxpayer compliance is information reporting to IRS by third parties on taxpayer transactions.

GAO was asked to (1) provide information on characteristics of individual taxpayer misreporting of charitable cash contributions, (2) provide information on actions that IRS takes to address misreporting, and (3) evaluate potential benefits and challenges associated with requiring information reporting for charitable cash contributions.

To meet its objectives, GAO used data from IRS's tax year 2001 National Research Program (NRP) compliance study of individual taxpayers, reviewed IRS guidance and enforcement data, and interviewed IRS officials and representatives from charities or organizations that represent charities.

GAO made no recommendations in this report. In email comments on a draft of this report, IRS agreed with GAO's overall conclusion that requiring information reporting for charitable cash contributions may not be an effective way to improve compliance.

View GAO-09-555 or key components.
For more information, contact Michael Brostek at (202) 512-9110 or brostekm@gao.gov.

What GAO Found

For tax year 2001, an estimated 46 percent of taxpayers who deducted cash contributions misreported, resulting in an estimated $13.8 billion in underreported net income. Since this amount is in income, and not tax dollars, the tax gap from the misreported cash contributions was much less than $13.8 billion. About 79 percent of misreporting taxpayers overstated a total of $16 billion in contributions while about 21 percent of misreporting taxpayers understated a total of $2.2 billion in contributions.

Distribution of Estimated Net Misreported Cash Contribution Amounts by Individual Taxpayers, Tax Year 2001

Net misreported amount per taxpayer	Number of misreporting taxpayers (in millions)	Percentage of misreporting taxpayers	Total net misreported contributions (dollars in billions)
Overstated contributions			
Less than $1,000	9.1	53	$3.2
$1,000 to $4,999	3.9	23	8.1
$5,000 or greater	0.5	3	4.7
Understated contributions			
Less than $1,000	3.2	19	-0.6
$1,000 or greater	0.4	2	-1.6
Total	**17.1**	**100**	**$13.8**

Source: GAO analysis of IRS data.

IRS attempts to ensure charitable cash contribution reporting compliance through enforcement and taxpayer service efforts. Cash contributions are one of the areas IRS examines most frequently for individual taxpayers. For fiscal year 2008, IRS examined about 175,000 taxpayers who potentially misreported cash contributions, out of about 1.4 million individual taxpayers it examined that fiscal year, and adjusted cash contribution amounts by $593 million in net terms. Through its taxpayer service programs, IRS provides publications and instructions to tax forms to help taxpayers comply with cash contribution reporting and recordkeeping requirements.

Requiring information reporting for charitable cash contributions may not be an effective way to improve compliance. Charities could incur substantial costs and burdens if they were required to file information returns with IRS and taxpayers on the cash contributions they receive. Exempting some cash contributions, such as those below a certain dollar amount or those made to small or religious charities, from information reporting could reduce the burden on some charities. However, exempting some cash contributions from information reporting would reduce the effect that the reporting would have on improving compliance, in part because IRS may not be able to match information returns against tax returns without complete information reporting. Also, the extent to which information reporting would improve voluntary compliance is unclear. Since the 2001 NRP study, more stringent requirements for the documentation taxpayers must keep to substantiate their cash contributions have gone into effect. It is not yet known whether the requirements have improved taxpayer reporting compliance, although an ongoing NRP study of individual taxpayers could show this.