United States Government Accountability Office

GAO

Report to Congressional Requesters

July 2008

TAX ADMINISTRATION

Comparison of the Reported Tax Liabilities of Foreign- and U.S.-Controlled Corporations, 1998-2005

GAO

Accountability * Integrity * Reliability

GAO-08-957

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Highlights

Highlights of GAO-08-957, a report to congressional requesters

Why GAO Did This Study

Concerns about transfer pricing abuse have led researchers to compare the tax liabilities of foreign- and U.S.-controlled corporations. (Transfer prices are the prices related companies charge on intercompany transactions.) However, such comparisons are complicated because other factors may explain the differences in reported tax liabilities. In three prior reports, GAO found differences in the percentages of foreign-controlled and U.S.-controlled corporations reporting no tax liability.

GAO was asked to update the previous reports by comparing: (1) the tax liabilities of foreign-controlled domestic corporations (FCDC) and U.S.-controlled corporations (USCC)–including those reporting zero tax liabilities for 1998 through 2005 (the latest available data) and (2) characteristics of FCDCs and USCCs such as age, size, and industry. GAO analyzed data from the Internal Revenue Service's Statistics of Income samples of corporate tax returns.

GAO does not make any recommendations in this report. In commenting on a draft of this report, IRS provided comments on technical issues, which we incorporated into this report where appropriate.

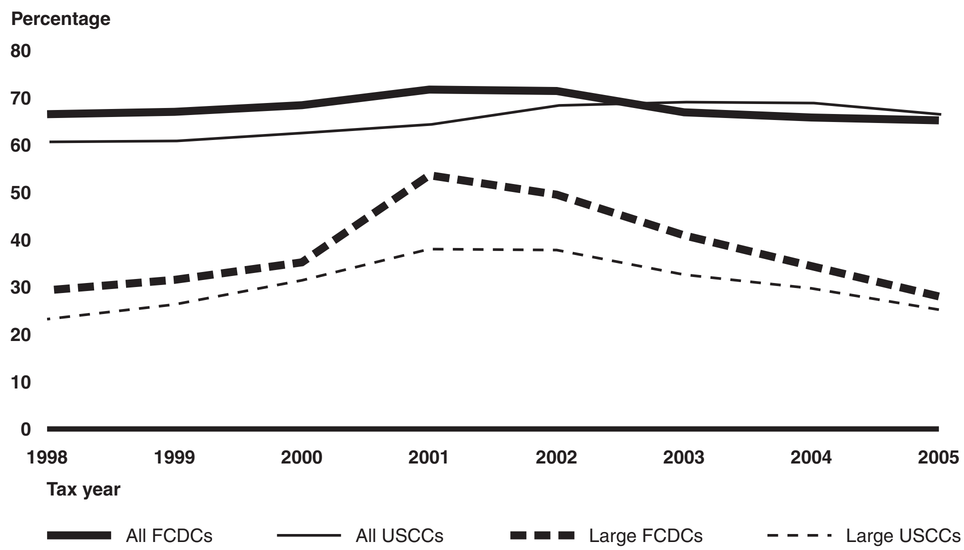
To view the full product, including the scope and methodology, click on GAO-08-957. For more information, contact Jim White at (202) 512-9110 or whitej@gao.gov.

What GAO Found

FCDCs reported lower tax liabilities than USCCs by most measures shown in this report. A greater percentage of large FCDCs reported no tax liability in a given year from 1998 through 2005. For all corporations, a higher percentage of FCDCs reported no tax liabilities than USCCs through 2001 but differences after 2001 were not statistically significant. Most large FCDCs and USCCs that reported no tax liability in 2005 also reported that they had no current-year income. A smaller proportion of these corporations had losses from prior years and tax credits that eliminated any tax liability. By another measure, large FCDCs were more likely to report no tax liability over multiple years than large USCCs. In 2005, comparisons of FCDCs and USCCs based on ratios of reported tax liabilities to gross receipts or total assets showed that FCDCs reported less tax than USCCs.

FCDCs and USCCs differed in age, size, and industry. FCDCs were younger than USCCs in that a greater percentage had been incorporated for 3 years or less from 1998 through 2005. In 2005, FCDCs were larger on average than USCCs in that they reported higher average gross receipts and assets than USCCs. A comparison by industry in 2005 showed that large FCDCs were relatively more concentrated in manufacturing and wholesale trade, while large USCCs were more evenly distributed across industries. GAO did not attempt to determine the extent to which these factors and others, such as transfer pricing abuse, explain differences in tax liabilities.

Percentages of FCDCs and USCCs That Reported No Tax Liability, Tax Years 1998 through 2005



Source: GAO analysis of IRS data.

Notes: "Large" FCDCs or USCCs are those with assets of at least $250 million dollars or gross receipts of at least $50 million dollars. Differences between all FCDCs and all USCCs were not statistically significant in 2002, 2003, 2004, and 2005.

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United States Government Accountability Office
Washington, DC 20548

July 24, 2008

The Honorable Carl Levin
Chairman
Permanent Subcommittee on Investigations
Committee on Homeland Security and Governmental Affairs
United States Senate

The Honorable Byron Dorgan
United States Senate

In response to your long-standing concerns about whether foreign-controlled U.S. corporations are abusing transfer prices and avoiding U.S. income tax, we compared the tax liabilities of foreign- and U.S.-controlled companies incorporated in the U.S. in three prior reports.[1] We reported that from 1989 through 2000 foreign-controlled corporations were more likely to report zero U.S. income tax liability than U.S.-controlled corporations with a majority of both types of corporations reporting no liability. We said that corporations may not report U.S income taxes for a variety of reasons including current-year operating losses, tax credits, and transfer pricing abuses.

Transfer prices are the prices related companies, such as a parent and subsidiary, charge on intercompany transactions. By manipulating transfer prices, multinational companies can shift income from higher to lower tax jurisdictions, reducing the companies' overall tax liability. As we noted in our previous reports, researchers acknowledge that transfer pricing abuses may explain some of the differences in tax liabilities of foreign-controlled corporations compared to U.S.-controlled corporations. However, researchers have had difficulty determining the exact extent to which transfer pricing abuses explain the differences due to data limitations.

[1] Transfer pricing is the pricing of intercompany transactions that affects the distribution of profits, and therefore, taxable income among related companies and sometimes across tax jurisdictions. Our previous reports are: GAO, *International Taxation: Taxes of Foreign- and U.S.-Controlled Corporations*, GAO/GGD-93-112FS (Washington, D.C.: June 11, 1993); *Tax Administration: Foreign- and U.S.-Controlled Corporations That Did Not Pay U.S. Income Taxes, 1989-95*, GAO/GGD-99-39 (Washington, D.C.: Mar. 23, 1999); and *Tax Administration: Comparison of the Reported Tax Liabilities of Foreign- and U.S.-Controlled Corporations, 1996-2000*, GAO-04-358 (Washington, D.C.: Feb. 27, 2004).

Based on your request, we updated our 2004 report. Specifically, we agreed to study (1) how the tax liability of foreign-controlled domestic corporations (FCDC) compares to that of U.S.-controlled corporations (USCC)—including the percentage of corporations reporting zero tax liabilities for tax years 1998 through 2005 and (2) how corporate characteristics such as age, size, and industry compare between FCDCs and USCCs.[2]

To meet these objectives, we analyzed data from the Internal Revenue Service's (IRS) Statistics of Income (SOI) samples of corporate tax returns for tax years 1998 through 2005. These SOI samples were based on returns as filed, and did not reflect IRS audit results or any net operating loss carrybacks from future years. The data that we report are estimates based on the SOI sample. Sampling errors are reported in appendix II. Caution should be used when comparing estimates because not all differences between estimates are statistically significant. Various types of corporations report their taxes on different forms and may differ in their tax liabilities. Unlike our previous reports, here we report separately for each form type. The estimates in the body of the report are for corporations filing Forms 1120 or 1120-A. (In app. II we provide separate estimates for corporations filing Forms 1120-L, 1120-PC, 1120-REIT, 1120-RIC, and 1120S.) We also report separately for large corporations—those with at least $250 million in assets or $50 million in gross receipts—because, while they account for less than 1 percent of all corporations, they make up over 90 percent of all assets reported on corporate returns.

As agreed, we did not attempt to determine whether corporations were abusing transfer prices. Nor did we attempt to determine the extent to which this abuse explains any differences in the reported tax liabilities of FCDCs and USCCs. Detailed information on our scope and methodology appears in appendix I.

We conducted our work from November 2007 through July 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence

[2] For purposes of this report, an FCDC is a U.S. corporation in which foreign individuals or entities own at least 50 percent of the corporation's voting stock.

obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Results in Brief

FCDCs reported lower tax liabilities than USCCs by most measures shown in this report. A greater percentage of large FCDCs reported no tax liability in a given year from 1998 through 2005, and large FCDCs were more likely to report no tax liability over multiple years than large USCCs. Corporations can establish the basis for no tax liability at different places on their tax returns. For example, some corporations could have zero income before deducting expenses and others could have zero net income after deducting expenses—both of which could result in no tax liability. In 2005, large FCDCs and USCCs differed little in where on their tax returns they first established no tax liability. Most large FCDCs and USCCs first established no tax liability where they reported their net current income after deducting expenses. A smaller proportion—about 10 percent—reported losses from prior years that eliminated any tax liability. In 2005, alternative comparisons of FCDCs and USCCs based on ratios of reported tax liabilities to gross receipts or total assets showed that FCDCs reported less tax than USCCs.

FCDCs and USCCs differed in age, size, and industry. FCDCs were younger than USCCs in that a greater percentage had been incorporated for 3 years or less from 1998 through 2005. In 2005, FCDCs were larger on average than USCCs in that they reported higher average gross receipts and assets than USCCs. A comparison by industry showed that FCDCs were concentrated in different industries compared with USCCs in 2005. We did not attempt to determine the extent to which these factors explained differences in tax liabilities.

In commenting on a draft of this report, IRS provided comments on technical issues, which we incorporated into this report where appropriate.

Background

Researchers have studied the factors explaining why FCDCs report lower tax liabilities than USCCs.[3] Generally, the research has recognized that nontax characteristics such as age and industry may explain some of the differences in reported tax liabilities. The researchers have also found that transfer pricing abuses may play a role in explaining the differences. However, measuring the separate effects of these factors on tax liabilities has been difficult due to data limitations.

Factors like the age and industry of corporations may affect tax liabilities by affecting net income. For example, younger corporations may be less likely than older corporations to have net income and, therefore, more likely to report no tax liability than older corporations. If FCDCs tend to be younger than USCCs, age differences may explain some of the difference in reported tax liabilities. We noted in our 1999 report that a study by Grubert (1997) suggested that the lower relative age of foreign-controlled corporations partially explained their lower reported profitability. However, data are not available on all the nontax characteristics that may affect tax liabilities.

Tax liabilities may also be reduced through transfer pricing abuse. Any company that has a related company, such as a subsidiary with which it transacts business, needs to establish transfer prices for those intercompany transactions. The transfer price should be the "arm's length price," i.e., the price that would be charged if the transaction occurred between unrelated companies. Section 482 of the Internal Revenue Code provides IRS authority to allocate income among related companies if IRS determines that the transfer prices used by the taxpayer were inappropriate. How transfer prices are set affects the distribution of profits and ultimately the taxable income of the companies. The following is an example of abusive cross-border transfer pricing. A foreign parent corporation with a subsidiary operating in the United States charges the subsidiary excessive prices for goods and services rendered (for example, $1,000 instead of the going rate of $600). This raises the subsidiary's expenses (by $400), lowers its profits (by $400), and effectively shifts that income ($400) outside of the United States. At a 35-percent U.S. corporate

[3] Harry Grubert, "Another Look at the Low Taxable Income of Foreign-Controlled Companies in the United States," *Tax Notes International* (Dec. 8, 1997), pp. 1,873-97; and David S. Laster and Robert N. McCauley, "Making Sense of the Profits of Foreign Firms in the United States," *Federal Reserve Bank of New York Quarterly Review* (Summer-Fall 1994).

income tax rate, the subsidiary will pay $140 less in U.S. taxes than it would if the $400 in profits were attributed to it.

Researchers have used direct and indirect methods to estimate the extent to which transfer pricing abuses explain the differences in reported tax liabilities. Direct methods analyze the transfer prices used by corporations and compare them to arm's length prices. This method is difficult to apply because price data are often unavailable and determining the price that would be charged between unrelated parties can be difficult. An alternative, indirect method used by researchers analyzes data about the characteristics of corporations in order to test for a statistical relationship between tax rates and subsidiaries' profitability or tax liability. In some of these studies, statistical methods are used to explain as much of the difference in reported tax liabilities as can be explained by the nontax characteristics and the remaining unexplained difference is identified as the upper limit of the difference that could be explained by transfer pricing abuse.[4] However, how close this upper limit estimate is to the actual effect of transfer pricing abuse depends on how many of the important nontax characteristics have been included in the first stage of the analysis. As noted above, data are unavailable for some important nontax characteristics.

Low tax burdens can be measured in various ways. Zero tax liability is one way. However, corporations paying only small, but not zero, amounts of tax also face low tax burdens. Furthermore, corporations that pay no or little tax over a number of years have a lower cumulative tax burden. Therefore, measures based on a range of tax amounts and tax years may give a fuller description of which types of corporations pay relatively less. Finally, the amount of taxes paid generally corresponds with the size of the corporation, with large corporations on average paying more than small ones. Tax liability can be measured as the amount of tax paid as a percentage of gross receipts or total assets in order to account for differences in the size of corporations.

[4] For examples of studies using direct methods, see Kimberly Clausing, "Tax Motivated Transfer Pricing and U.S. Intrafirm Trade Prices," *Journal of Public Economics* (2003) pp. 2207 – 2223, and Andrew Bernard, J. Jensen and Peter Schott, "Transfer Pricing by U.S.–Based Multinational Firms," *NBER working paper 12493* (August 2006). For examples of indirect methods, see James Hines, "Tax Policy and the Activities of Multinational Corporations," *NBER working paper 5589* (May 1996), pp. 25-30.

FCDCs Reported Lower Tax Liabilities Than USCCs by Most Measures

Our comparison of tax liabilities highlights three measures that are used by tax experts: (1) the percentage of corporations reporting no tax liability, (2) the number of years corporations reported no tax liability, and (3) tax liabilities reported by corporations as a percentage of gross receipts and assets.

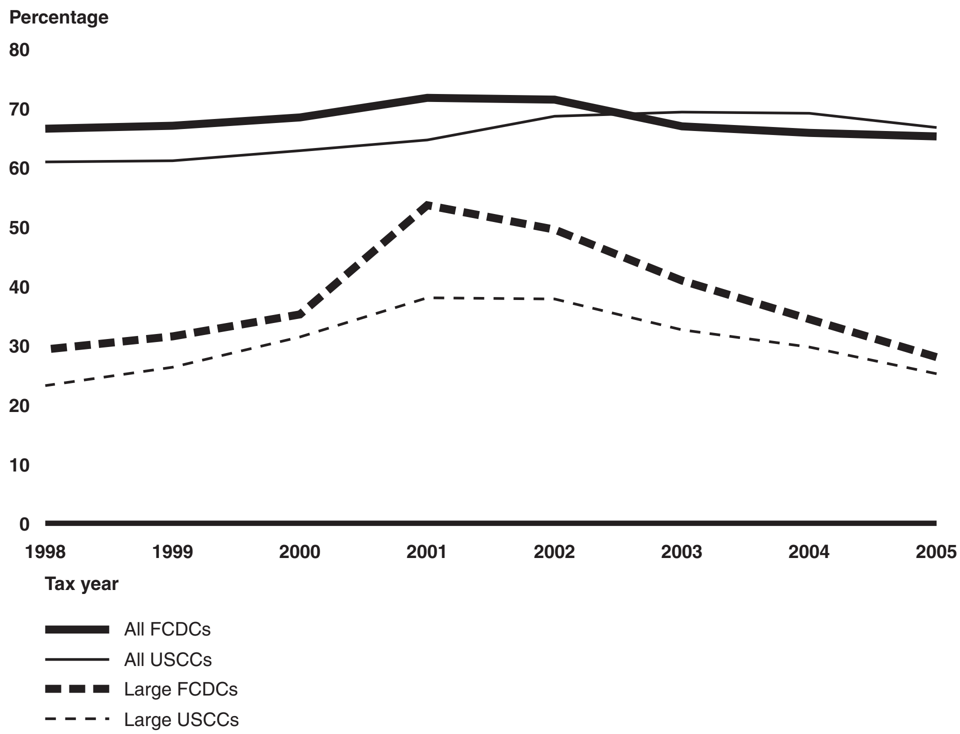
A Large Percentage of Both FCDCs and USCCs Reported No Tax Liabilities

A greater percentage of large FCDCs reported no tax liability in a given year from 1998 through 2005, as shown in figure 1. (See table 1 in app. II for the detailed estimates.) From 1998 through 2001, a higher percentage of all FCDCs reported no tax liability than all USCCs, but differences after 2001 were not statistically significant.

As figure 1 shows, the number of large FCDCs and large USCCs that reported no tax liability peaked around 2001 and 2002. These years correspond roughly with a period of economic recession in the United States. However, we did not do any analysis to determine the effect of the recession on the patterns shown if figure 1.

After 2001, the percentage of large FCDCs and USCCs reporting no tax liability began to converge. By 2005, the difference was reduced to 3 percentage points. For corporations other than those filing tax Forms 1120 and 1120-A, the percentage of corporations that reported no tax liability varied by tax year and tax return type. (For detailed comparisons of these corporations, see table 2 in app. II.)

Figure 1: Percentages of FCDCs and USCCs That Reported No Tax Liability, Tax Years 1998 through 2005



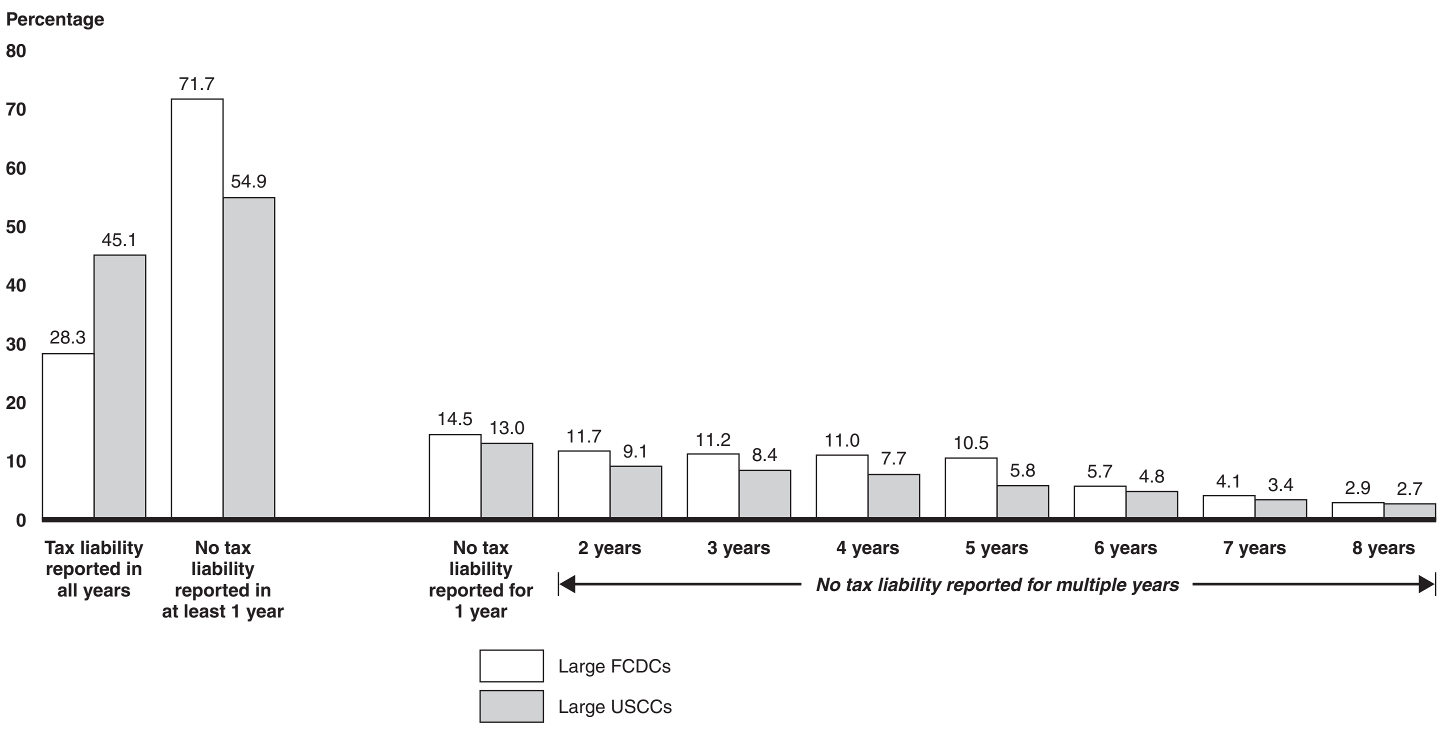
Source: GAO analysis of IRS data.

Notes: "Large" FCDCs or USCCs are those with assets of at least $250 million dollars or gross receipts of at least $50 million dollars. Differences between all FCDCs and all USCCs were not statistically significant in 2002, 2003, 2004, and 2005.

A Greater Percentage of Large FCDCs Reported No Tax Liability over Multiple Years between 1998 and 2005

In the 8 years from 1998 through 2005, large FCDCs in a panel data set that we analyzed consisting of tax returns that were present in the SOI corporate files in every year were more likely to report no tax liability over multiple years than large USCCs in the same panel data set. As figure 2 shows, about 72 percent of FCDCs and 55 percent of USCCs reported no tax liability for at least 1 year during the 8 years. About 57 percent of FCDCs and 42 percent of USCCs reported no tax liability in multiple years—2 or more years—and about 34 percent of FCDCs and 24 percent of USCCs reported no tax liability for at least half the study period—4 or more years. A correspondingly higher percentage of USCCs reported a tax liability in all 8 years, 45 percent for USCCs and 28 percent for FCDCs.

Figure 2: Percentage of Large FCDCs and USCCs That Reported No Tax Liability for Multiple Years between 1998 and 2005



Source: GAO analysis of panel data developed by GAO from the SOI database.

Large FCDCs and USCCs Were Similar in Where on Their Tax Returns They Established Zero Tax Liability

Large FCDCs and USCCs reporting no tax liability in 2005 arrived at that result in similar ways on their tax returns, as shown in figure 3. At a high level, corporate tax returns are organized to (1) calculate gross profit as gross receipts or sales minus the cost of goods sold; (2) calculate total income as gross profit plus other types of income; (3) report various deductible expenses; (4) calculate taxable income as the difference between income and deductions; and (5) calculate the tax liability for the taxable income. Corporations can establish the basis for a zero tax liability at different stages in these calculations by reporting, for example, that they have no total income or no taxable income which results in their having no tax liability. Figure 3 shows the percentage of corporations reporting no tax liability in 2005 by the line on their tax return where they first reported the zero dollar amounts that resulted in no tax liability. For example, the figure shows that 3 percent of large FCDCs and 1 percent of large USCCs established no tax liability by reporting no gross profit on line 3 of their returns.[5] This pattern of similar percentages for large corporations continues throughout the tax return. For example, a similar, small percentage of large FCDCs or USCCs, around 4 to 5 percent, established their zero tax liability on line 11 by reporting zero total income.

As figure 3 shows, the overwhelming majority, about 79 to 80 percent of both large FCDCs and USCCs that reported zero tax liability in 2005, established it on line 28 where they reported zero taxable income before net operating losses. This means that their reported current-year deductions more than offset the positive current-year total income reported on line 11. The two most commonly used deductions, as a percentage of the value of all deductions claimed, were "other deductions"[6] and the deduction for salaries and wages. See table 3 and figure 8 in appendix II for detailed comparisons of tax return line items and deductions.

On the corporate tax return, current-year taxable income is reported before net operating losses from other years are deducted and any tax credits are subtracted from tax liabilities. In 2005, losses from prior years and tax credits had less impact on where on the tax return large corporations first established no tax liability. Figure 3 shows on line 30 that a relatively small number of large corporations—about 10 percent—first established a zero tax liability by carrying forward losses from prior

[5] This is the only line on the tax return shown in figure 3 with a statistically significant difference between the percentage of large FCDCs and USCCs first reporting zero dollars.

[6] Other deductions are all allowable deductions that are not deductible elsewhere on Form 1120. These include travel, meals, and entertainment expenses; dividends paid in cash on stock held by employee stock ownership plans; insurance premiums; and legal and professional fees.

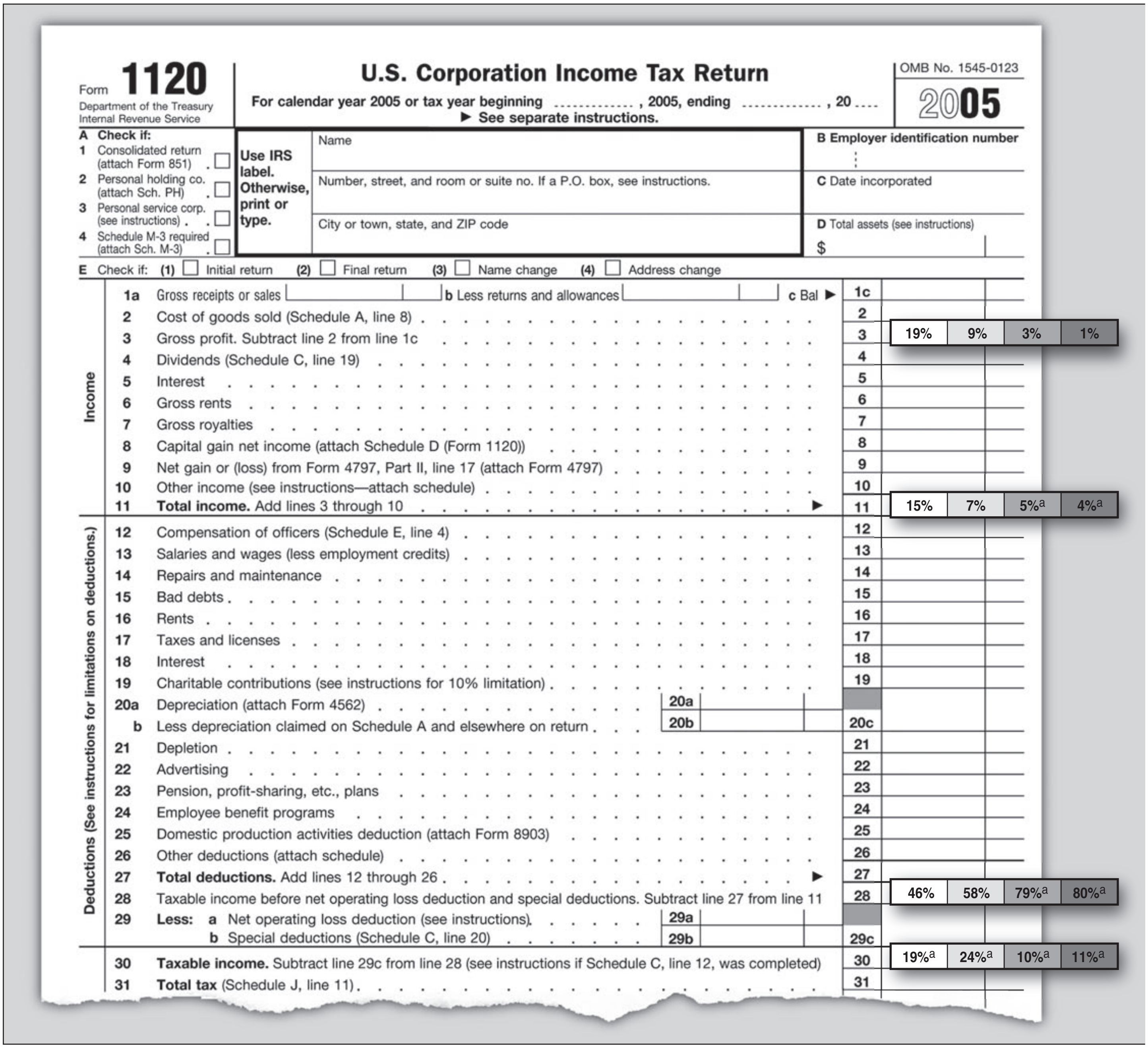
years, and that an even smaller number—about 3 percent—first established no tax liability through their use of tax credits, as reported on line 11 schedule J in the figure.

All FCDCs and USCCs differed in some ways from large FCDCs and USCCs in where on their tax returns they first established no tax liability, reflecting the influence of small corporations. As figure 3 shows, a higher percentage of all corporations established no tax liability on the gross profit and total income lines on their returns than large corporations. All corporations also show a greater impact of losses from prior years, with 19 to 24 percent first establishing no tax liability when they reported taxable income on line 30 after subtracting these losses.

However, there were also similarities between all corporations and large corporations in 2005. As with large corporations, all FCDCs and USCCs were most likely to first establish no tax liability on line 28 of their tax returns—over 46 percent for FCDCs and 58 percent for USCCs. In addition, as with large corporations, tax credits had little impact with only about 1 percent of all corporations first establishing no liability through their use of credits.

Figure 3 also shows that all FCDCs differed from all USCCs more than the large FCDCs differed from large USCCs. Whereas large FCDCs and USCCs differed little in where on the return they established no tax liability, all FCDCs were more than twice as likely to first establish no tax liability on the gross profit and total income lines as all USCCs.

Figure 3: Percentage of FCDCs and USCCs with No Tax Liability by the First Line on Their Tax Return Where They Established No Tax Liability, Tax Year 2005



Form **1120** Department of the Treasury Internal Revenue Service

U.S. Corporation Income Tax Return

For calendar year 2005 or tax year beginning ...., 2005, ending ...., 20....

► See separate instructions.

OMB No. 1545-0123

2005

A Check if:
1 Consolidated return (attach Form 851)
2 Personal holding co. (attach Sch. PH)
3 Personal service corp. (see instructions)
4 Schedule M-3 required (attach Sch. M-3)

Use IRS label. Otherwise, print or type.

Name

Number, street, and room or suite no. If a P.O. box, see instructions.

City or town, state, and ZIP code

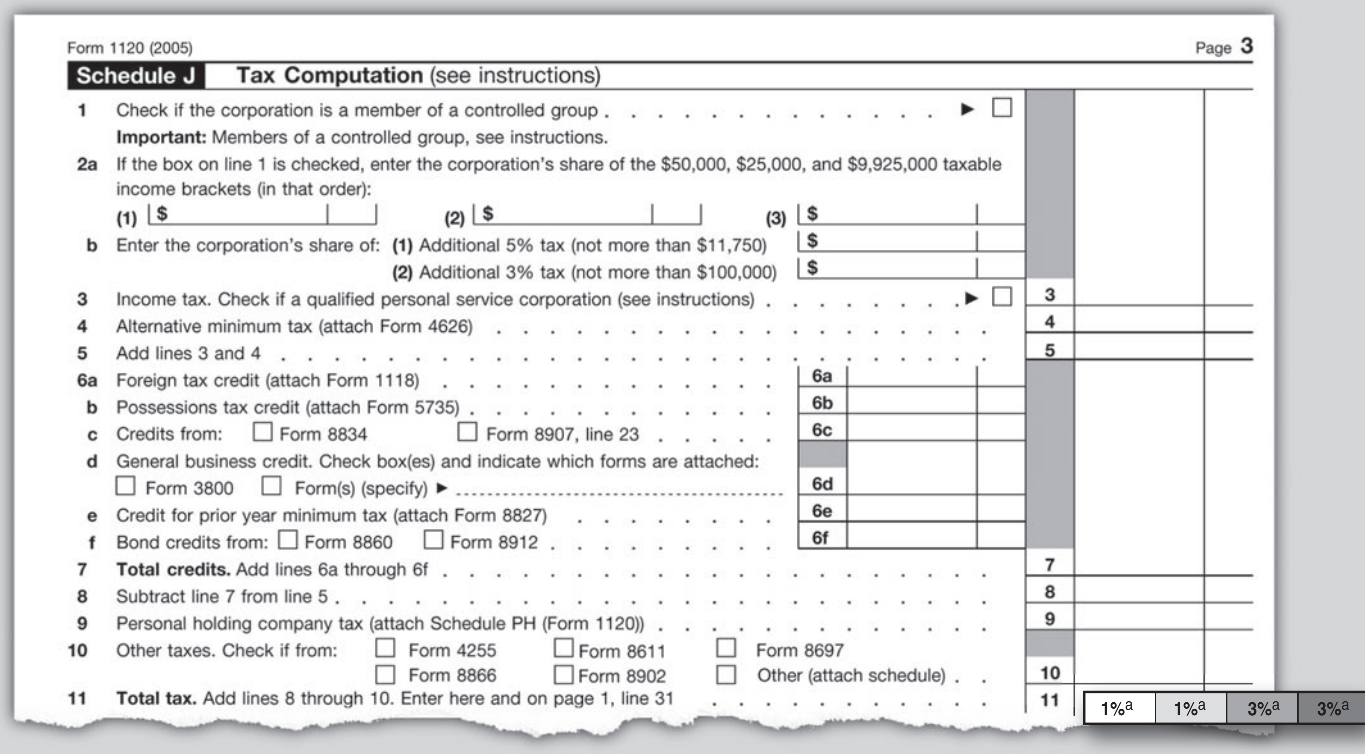
B Employer identification number

C Date incorporated

D Total assets (see instructions) $

E Check if: (1) Initial return (2) Final return (3) Name change (4) Address change

Income	1a	Gross receipts or sales; b Less returns and allowances; c Bal ►	1c				
	2	Cost of goods sold (Schedule A, line 8)	2				
	3	Gross profit. Subtract line 2 from line 1c	3	19%	9%	3%	1%
	4	Dividends (Schedule C, line 19)	4				
	5	Interest	5				
	6	Gross rents	6				
	7	Gross royalties	7				
	8	Capital gain net income (attach Schedule D (Form 1120))	8				
	9	Net gain or (loss) from Form 4797, Part II, line 17 (attach Form 4797)	9				
	10	Other income (see instructions—attach schedule)	10				
	11	**Total income.** Add lines 3 through 10 ►	11	15%	7%	5%[a]	4%[a]
Deductions (See instructions for limitations on deductions.)	12	Compensation of officers (Schedule E, line 4)	12				
	13	Salaries and wages (less employment credits)	13				
	14	Repairs and maintenance	14				
	15	Bad debts	15				
	16	Rents	16				
	17	Taxes and licenses	17				
	18	Interest	18				
	19	Charitable contributions (see instructions for 10% limitation)	19				
	20a	Depreciation (attach Form 4562)	20a				
	b	Less depreciation claimed on Schedule A and elsewhere on return	20b / 20c				
	21	Depletion	21				
	22	Advertising	22				
	23	Pension, profit-sharing, etc., plans	23				
	24	Employee benefit programs	24				
	25	Domestic production activities deduction (attach Form 8903)	25				
	26	Other deductions (attach schedule)	26				
	27	**Total deductions.** Add lines 12 through 26 ►	27				
	28	Taxable income before net operating loss deduction and special deductions. Subtract line 27 from line 11	28	46%	58%	79%[a]	80%[a]
	29	**Less:** a Net operating loss deduction (see instructions)	29a				
		b Special deductions (Schedule C, line 20)	29b / 29c				
	30	**Taxable income.** Subtract line 29c from line 28 (see instructions if Schedule C, line 12, was completed)	30	19%[a]	24%[a]	10%[a]	11%[a]
	31	**Total tax** (Schedule J, line 11)	31				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Schedule J **Tax Computation** (see instructions)

1 Check if the corporation is a member of a controlled group . . . ► ☐

Important: Members of a controlled group, see instructions.

2a If the box on line 1 is checked, enter the corporation's share of the $50,000, $25,000, and $9,925,000 taxable income brackets (in that order):

(1) $ (2) $ (3) $

b Enter the corporation's share of: **(1)** Additional 5% tax (not more than $11,750) $

(2) Additional 3% tax (not more than $100,000) $

3 Income tax. Check if a qualified personal service corporation (see instructions) . . . ► ☐ 3

4 Alternative minimum tax (attach Form 4626) . . . 4

5 Add lines 3 and 4 . . . 5

6a Foreign tax credit (attach Form 1118) . . . 6a

b Possessions tax credit (attach Form 5735) . . . 6b

c Credits from: ☐ Form 8834 ☐ Form 8907, line 23 . . . 6c

d General business credit. Check box(es) and indicate which forms are attached:

☐ Form 3800 ☐ Form(s) (specify) ► 6d

e Credit for prior year minimum tax (attach Form 8827) . . . 6e

f Bond credits from: ☐ Form 8860 ☐ Form 8912 . . . 6f

7 **Total credits.** Add lines 6a through 6f . . . 7

8 Subtract line 7 from line 5 . . . 8

9 Personal holding company tax (attach Schedule PH (Form 1120)) . . . 9

10 Other taxes. Check if from: ☐ Form 4255 ☐ Form 8611 ☐ Form 8697 ☐ Form 8866 ☐ Form 8902 ☐ Other (attach schedule) . . 10

11 **Total tax.** Add lines 8 through 10. Enter here and on page 1, line 31 . . . 11

1%[a]	1%[a]	3%[a]	3%[a]

x%	Percentage of all FCDCs that **first** established no tax liability on this line of their return
x%	Percentage of all USCCs that **first** established no tax liability on this line of their return
x%	Percentage of large FCDCs that **first** established no tax liability on this line of their return
x%	Percentage of large USCCs that **first** established no tax liability on this line of their return

Source: GAO analysis of IRS information.

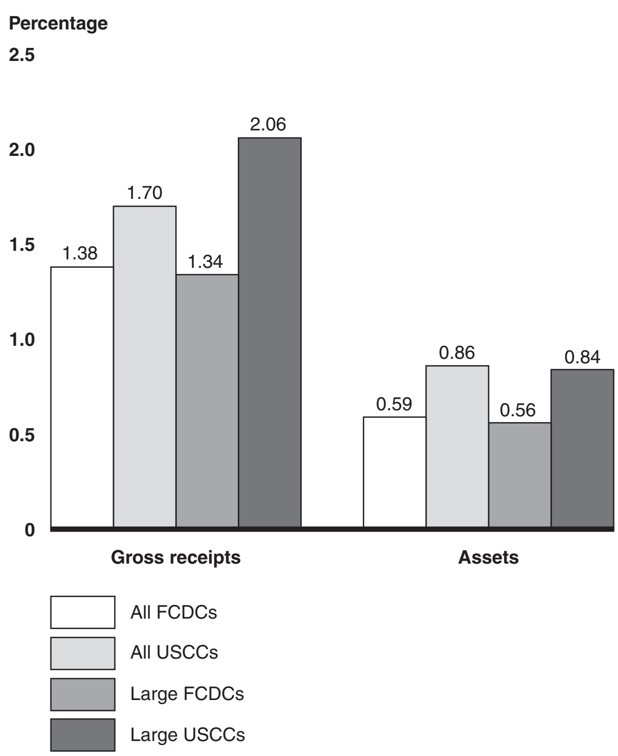
Note: Percentages do not total to 100 due to certain adjustments that IRS made to reported tax return data to account for such factors as a one-time dividend deduction election.

[a]Differences between FCDCs and USCCs are not statistically significant.

FCDCs Reported Less Tax Liability Than USCCs as a Percentage of Both Gross Receipts and Total Assets

Alternative comparisons of FCDCs and USCCs based on ratios of reported tax liabilities to gross receipts or total assets also showed that FCDCs reported less tax than USCCs. Figure 4 shows that taxes as a percentage of gross receipts and assets were higher for USCCs than FCDCs. FCDCs reported lower tax liabilities in 2005 as a percentage of gross receipts than USCCs. For all FCDCs the percentage was about 1.4 percent, while for all USCCs the percentage was about 1.7 percent. This pattern was similar for large corporations where FCDCs had lower tax liability as a percentage of gross receipts-about 1.3 percent compared to about 2.1 percent for large USCCs.

Figure 4: FCDC and USCC Tax Liabilities as a Percentage of Gross Receipts and Assets, Tax Year 2005



Source: GAO analysis of IRS data.

Another comparison of FCDCs and USCCs based on amounts of tax liability in addition to zero tax liability showed that differences between FCDCs and USCCs became smaller as their reported tax liabilities increased. The difference between the percentage of large FCDCs and USCCs that report no tax liability was about 3 percent in 2005, and this difference reduces to 1 percent when we include corporations reporting tax liabilities less than $100,000 in the comparison. The difference is eliminated entirely when we compare those that report less than $1 million in tax liability. (For details of these comparisons, see table 4 in app. II.)

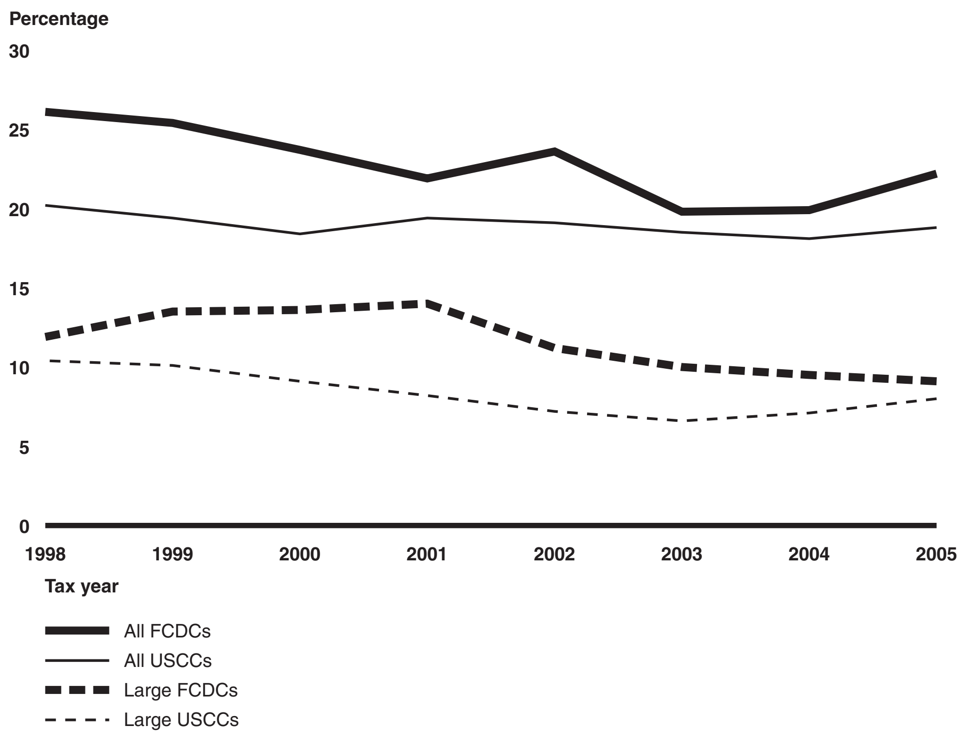
FCDCs and USCCs Differ by Age, Size, and Industry

Differences in age, size, industry and other nontax factors between FCDCs and USCCs could explain some of the differences in their reported tax liabilities. Also, companies in different industries often have different financial characteristics which could affect relative measures of tax liability. For instance, the relative levels of assets and receipts of companies primarily engaged in wholesale trade differ significantly from those primarily engaged in credit intermediation, such as commercial banks. We did not attempt to explain the extent to which these factors or others, such as transfer pricing abuses, might explain differences in the reported tax liabilities of FCDCs and USCCs.

A Higher Percentage of Large FCDCs Than Large USCCs Were New

A higher percentage of large FCDCs than large USCCs were new corporations (incorporated for 3 years or less) for tax years 1998 through 2005, as shown in figure 5. The percentages of large FCDCs that were new ranged from 9 percent to 14 percent, while for large USCCs the percentages ranged from 7 percent to 10 percent. For all FCDCs and USCCs, except for 1998 through 2000, there were no years with a statistically significant difference between the percentages of these types of corporations that were new. (See table 5 in app. II for the detailed estimates.)

Figure 5: Percentage of FCDCs and USCCs That Were New, Tax Years 1998 through 2005



Source: GAO analysis of IRS data.

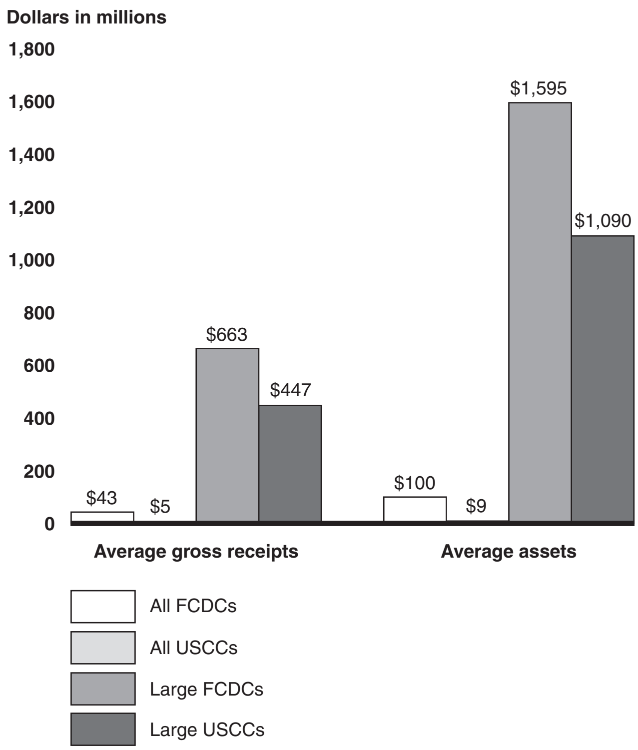
Note: Differences between all FCDCs and all USCCs were not statistically significant in 2001, 2002, 2003, 2004, and 2005.

FCDCs Reported Higher Average Gross Receipts and Assets Than USCCs

FCDCs tended to be larger in that in 2005 they reported higher average assets and gross receipts than USCCs, as shown in figure 6. All FCDCs reported an average of about $100 million in assets compared to about $9 million for all USCCs. Large FCDCs also reported higher amounts of assets—an average of about $1.6 billion compared to about $1.1 billion for large USCCs.

FCDCs reported more average gross receipts in 2005. All FCDCs reported an average of about $43 million in gross receipts, while USCCs reported an average of about $5 million. Although the magnitudes were larger for large corporations, the pattern of gross receipts was similar. Large FCDCs reported higher average gross receipts—about $663 million compared to about $447 million for large USCCs.

Figure 6: FCDC and USCC Average Gross Receipts and Assets, Tax Year 2005

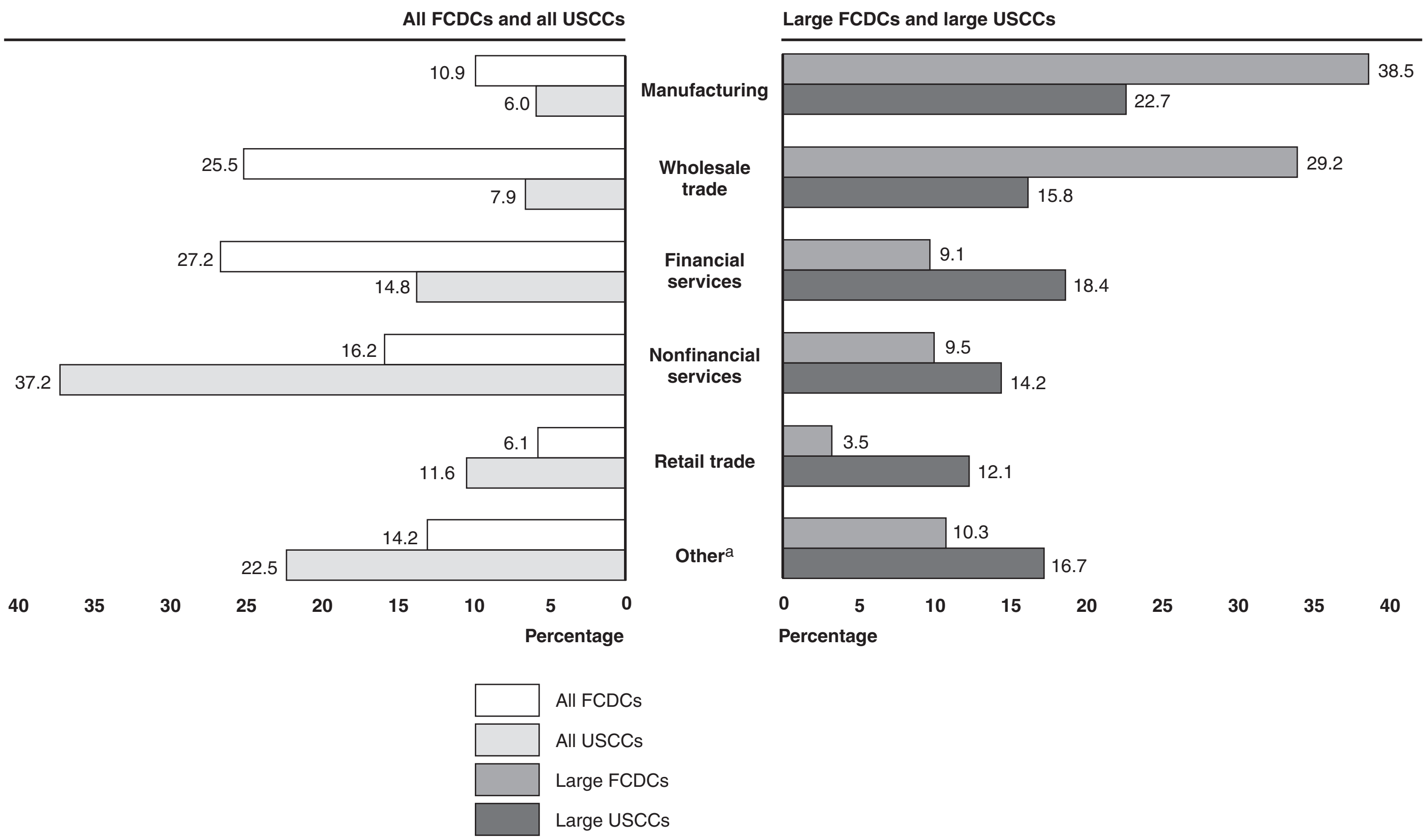


Source: GAO analysis of IRS data.

FCDCs and USCCs Were Concentrated in Different Industries

In 2005, FCDCs and USCCs differed in their distribution across industries. As figure 7 shows, all FCDCs were more concentrated in the wholesale trade and financial services industries, while all USCCs were more concentrated in the nonfinancial services industry. When the focus is limited to large corporations, FCDCs were relatively more concentrated in manufacturing and wholesale trade. Large USCCs were more evenly distributed across the industries shown in figure 7.

Figure 7: FCDCs and USCCs by Major Industry, Tax Year 2005



Source: GAO analysis of IRS data.

[a]Other includes transportation and warehousing; utilities; mining; construction; agriculture, forestry, hunting and fishing; and other trades.

Differences in cost ratios across industries are possible explanations for why industry concentration might affect the reported tax liabilities of FCDCs and USCCs. Cost differences could affect profits, and thus tax liabilities. For example, the higher cost of goods sold relative to receipts could contribute to lower taxable income relative to receipts, and consequently lower tax liability relative to receipts. In tax year 2005, all FCDCs were more likely to have higher cost of goods sold, purchases, and interest as a percentage of gross receipts for most industries than were USCCs. The results were similar for large corporations. (For details of these comparisons of cost ratios, see table 6 in app. II.)

Agency Comments

We provided a draft of this report to the IRS for its comments. On July 21, the Research, Analysis and Statistics unit provided comments via e-mail on technical issues, which we incorporated into this report where appropriate.

As agreed with your offices, unless you publicly announce its contents earlier, we plan no further distribution of this report until 30 days from its date. At that time, we will send copies of this report to the Secretary of the Treasury, the Commissioner of Internal Revenue, and other interested parties. This report will also be available at no charge on GAO's Web site at http://www.gao.gov.

If you or your staff has any questions about this report, please contact me at (202) 512-9110 or whitej@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made contributions to this report are listed in appendix III.

James R. White

James R. White
Director, Tax Issues
Strategic Issues Team

Appendix I: Objectives, Scope, and Methodology

The objectives of this assignment were to study (1) how the tax liability of foreign-controlled domestic corporations (FCDC) compares to that of U.S.-controlled corporations (USCC)—including the percentage of corporations reporting zero tax liabilities for tax years 1998 through 2005 and (2) how corporate characteristics, such as age, size, or industry, compare between FCDCs and USCCs. For both of our objectives, we used data from Internal Revenue Service's (IRS) Statistics of Income (SOI) files on corporate tax returns for tax years 1998 through 2005. These SOI samples were based on returns as filed, and did not reflect IRS audit results or any net operating loss carrybacks from future years. Each tax return is treated as a separate corporation which, in the case of consolidated returns, may be composed of a number of subsidiary corporations. To provide information on the number of years large corporations did not report tax liabilities, we developed a panel data set consisting of the tax returns of large corporations that were present in the SOI corporate files in every year from 1998 through 2005. We did not include corporations that changed ownership status as USCCs or FCDCs during this period. We also did not analyze changes in the composition of corporations that filed consolidated returns. The gross receipts and assets of the corporations present in the panel data set account for on average about 40 percent of gross receipts and assets of all corporations and about 50 percent of the gross receipts and assets of large corporations from 1998 through 2005. Over time, the corporations present in the panel data account for an increasing share of corporate gross receipts and assets. For example in 1998 and 1999 the panel data corporations accounted for about 40 percent of the gross receipts and assets of all large corporations. This percentage increased to about 60 percent by 2005.

To compare all and large FCDCs and USCCs based on the tax liabilities they reported on their U.S. income tax returns, we made estimates for a variety of measures of tax liability. For the purposes of this report, an FCDC is a U.S. corporation with 50 percent or more of its voting stock owned by a foreign person or entity. Foreign control of a U.S. corporation exists when a foreign investor gains control of an existing U.S. company or creates a new company that it incorporates in the United States. Both FCDCs and USCCs are subject to U.S. income tax laws although the tax treatment of some income may differ. Large corporations are those with at least $250 million of assets or at least $50 million of receipts. We also compared differences in FCDCs and USCCs by age and industry sector. We defined new corporations as those for which income tax returns showed incorporation dates within 3 years of the tax year date; all others were considered old corporations. For example, for tax year 2005, new corporations are those with incorporation dates no earlier than 2003. We did not attempt to determine whether corporations were abusing transfer prices. Nor did we attempt to determine the extent to which such abuse explains any differences in the reported tax liabilities of FCDCs and USCCs.

The SOI corporation data we used in our comparison of tax liabilities of FCDCs and USCCs included domestic corporations. We reported separately for corporations that reported tax liabilities on Form 1120 (U.S. Corporation Income Tax Return) and Form 1120-A (U.S. Corporation Short-Form Income Tax Return). We also provided in table 2 of appendix II information on corporations that reported no tax liabilities on Forms 1120-L (U.S. Life Insurance Company Income Tax Return), 1120-PC (U.S. Property and Casualty Insurance Company Income Tax Return), 1120-REIT (U.S. Income Tax Return for Real Estate Investment Trusts), 1120-RIC (U.S. Income Tax Return for Regulated Investment Companies), and 1120S (U.S. Income Tax Return for an S Corporation). Some of these types of corporations, such as REITs and RICs, are pass-through entities that generally do not incur corporate tax liabilities. We did not include foreign corporations in our comparison of FCDCs and USCCs or those that filed Form 1120-F (U.S. Income Tax Return of a Foreign Corporation).

The SOI data in this report is based on SOI's probability sample of corporate tax returns and thus is subject to some imprecision owing to sampling variability. Using SOI's sampling weights, we estimated sampling errors for our estimates, which are reported in appendix II. Caution should be used when comparing estimates because not all differences between estimates are statistically significant. Differences between all FCDCs and USCCs, and large FCDCs and USCCs, are statically significant unless noted at the bottom of each figure or table. To ensure that the data were comparable across years, we converted all dollar-based data to 2005 dollars. The data included tax liabilities, total income, gross receipts, assets, cost of goods sold, interest, and purchases reported.

SOI is a data set widely used for research purposes. SOI data are not available to the public except in aggregate form via published tables. These data tables are publicly available either in printed form or on the irs.gov Web site. IRS performs a number of quality control steps to verify the internal consistency of SOI sample data. For example, it performs computerized tests to verify the relationships between values on the returns selected as part of the SOI sample, and manually edits data items to correct for problems, such as missing items. We conducted several reliability tests to ensure that the data excerpts we used for this report were complete and accurate. For example, we electronically tested the data and used published data as a comparison to ensure that the data set was complete. To ensure accuracy, we reviewed related documentation and electronically tested for obvious errors. We concluded that the data were sufficiently reliable for the purposes of this report.

We requested comments on a draft of this report from the Commissioner of Internal Revenue. We conducted our review from November 2007 through July 2008 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix II: Additional Tables

The tables in this statistical appendix supplement those in the letter and provide population estimates. After each table, notes indicate the sampling errors. We are confident the true estimates would be within these percentage points in 95 out of every 100 samples. Finally, we conducted tests to determine if there were significant differences between all FCDCs and USCCs and between large FCDCs and USCCs. The comparisons that were not statistically significant are noted in each table.

Corporations That Reported No Tax Liability

Table 1: FCDCs and USCCs Reporting No Tax Liability, Tax Years 1998 through 2005

	FCDCs, all		USCCs, all		FCDCs, large		USCCs, large	
Tax year	**Number**	**Percentage**	**Number**	**Percentage**	**Number**	**Percentage**	**Number**	**Percentage**
Forms 1120 and 1120-A								
1998	39,414	66.5	1,322,375	60.9	898	29.3	3,451	23.2
1999	38,687	67.0	1,296,663	61.1	1,007	31.5	3,961	26.3
2000	39,341	68.4	1,316,163	62.8	1,190	35.2	4,804	31.4
2001	41,544	71.7	1,330,859	64.6	1,802	53.6	5,463	38.0
2002	42,567	71.4[a]	1,385,182	68.6[a]	1,600	49.5	5,143	37.8
2003	38,166	66.9[a]	1,367,105	69.3[a]	1,333	40.9	4,386	32.6
2004	36,353	65.8[a]	1,350,332	69.1[a]	1,183	34.4	4,072	29.7
2005	38,483	65.2[a]	1,263,726	66.7[a]	998	28.0	3,565	25.2

Source: GAO analysis of IRS data.

Note: Percentage estimates for FCDCs have sampling errors of less than (+/-) 4 percentage points; percentage estimates for USCCs have sampling errors of less than (+/-) 1 percentage point.

[a]Differences between FCDCs and USCCs are not statistically significant.

Table 2: FCDCs and USCCs Reporting No Tax Liability, Tax Years 1998 through 2005

	FCDCs, all		USCCs, all		FCDCs, large		USCCs, large	
Tax year	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
Forms								
1120-L								
1998	12	16.4	638	33.2	10	17.9[b]	88	16.9[b]
1999	20	25.2[b]	644	35.4[b]	11	19.0[b]	88	17.4[b]
2000	23	24.8[b]	641	36.9[b]	15	23.8[b]	96	20.5[b]
2001	38	39.5[b]	664	38.1[b]	28	40.0	129	25.7
2002	39	39.7[b]	672	38.1[b]	34	45.3	182	31.6
2003	21	34.3[b]	634	36.3[b]	14	33.3[b]	152	24.2[b]
2004	28	28.5[b]	566	33.5[b]	16	21.6[b]	133	20.9[b]
2005	32	28.7[b]	458	29.2[b]	24	27.3	97	15.4
1120-PC								
1998	25	33.3[b]	1,554	43.8[b]	13	32.5[b]	130	26.0[b]
1999	31	42.4[b]	1,742	47.6[b]	19	47.5[b]	154	32.0[b]
2000	37	49.6[b]	1,703	46.6[b]	23	54.3	144	30.1
2001	59	64.0	1,799	46.7	39	69.6	187	40.1
2002	47	53.4[b]	1,794	43.9[b]	26	65.0	170	35.0
2003	42	39.7[b]	1,550	35.1[b]	12	25.4[b]	90	17.3[b]
2004	32	32.7[b]	1,813	32.8[b]	16	34.8	81	15.5
2005	40	36.8[b]	1,502	26.0[b]	23	41.1	73	14.2
1120-REIT								
1998	27	93.1[b]	862	95.4[b]	12	100.0[b]	316	95.8[b]
1999	29	90.7[b]	974	93.8[b]	18	85.7[b]	341	95.0[b]
2000	30	83.3[b]	995	93.6[b]	17	85.0[b]	327	94.0[b]
2001	47	94.0[b]	930	94.8[b]	21	95.5[b]	333	95.4[b]
2002	46	90.2[b]	989	95.2[b]	19	95.0[b]	375	94.9[b]
2003	42	87.4[b]	965	95.5[b]	19	86.4[b]	387	94.6[b]
2004	48	96.0[b]	1,008	94.0[b]	26	96.3[b]	407	93.1[b]
2005	76	96.2[b]	1,104	94.4[b]	33	97.1[b]	430	92.7[b]
1120-RIC								
1998	86	100.0[b]	9,730	99.2[b]	11	100.0[b]	3,299	99.5[b]
1999	93	100.0[b]	10,159	99.4[b]	29	100.0[b]	3,561	99.3[b]
2000	103	100.0[b]	10,817	99.3[b]	34	100.0[b]	3,732	99.4[b]
2001	97	100.0[b]	11,171	99.6[b]	34	100.0[b]	3,739	99.5[b]
2002	104	100.0[b]	10,889	99.3[b]	33	100.0[b]	3,663	99.2[b]

Tax year	FCDCs, all		USCCs, all		FCDCs, large		USCCs, large	
	Number	Percentage	Number	Percentage	Number	Percentage	Number	Percentage
2003	118	100.0[b]	10,787	99.3[b]	50	100.0[b]	4,093	99.1[b]
2004	107	100.0[b]	10,726	99.4[b]	58	100.0[b]	4,309	99.2[b]
2005	257	98.8[b]	10,602	99.2[b]	157	99.4[b]	4,437	99.2[b]
1120S								
1998	[a]	[a]	2,579,022	99.6	[a]	[a]	8,076	93.7
1999	[a]	[a]	2,716,695	99.6	[a]	[a]	8,638	92.3
2000	[a]	[a]	2,846,262	99.7	[a]	[a]	9,453	93.8
2001	[a]	[a]	2,978,696	99.8	[a]	[a]	9,529	94.2
2002	[a]	[a]	3,144,831	99.7	[a]	[a]	9,809	94.4
2003	[a]	[a]	3,334,293	99.8	[a]	[a]	10,651	95.1
2004	[a]	[a]	3,512,014	99.8	[a]	[a]	12,386	95.7
2005	[a]	[a]	3,674,551	99.8	[a]	[a]	12,504	95.2

Source: GAO analysis of IRS data.

Notes: Percentage estimates for all FCDCs have sampling errors of less than (+/-) 17 percentage points; percentage estimates for large FCDCs have sampling errors of less than (+/-) 24 percentage points; percentage estimates for USCCs have sampling errors of less than (+/-) 5 percentage points. S corporations, RICs, and REITs are pass-through entities that generally incur no corporate tax liability.

[a]Not applicable—S corporations are prohibited from foreign ownership.

[b]Differences between FCDCs and USCCs are not statistically significant.

Corporations That Established No Tax Liability by Tax Return Line Item

Table 3: FCDCs and USCCs That Established No Tax Liability by Tax Return Line Item, Tax Year 2005

Tax return line item	Percentage of returns where $0 is first reported	Percentage of returns for line item where deduction or credit was reported[a]	Percentage of returns where $0 is first reported	Percentage of returns for line item where deduction or credit was reported[a]
	All FCDCs, no tax		All USCCs, no tax	
Gross profit—line 3	19.22		8.52	
Total income—line 11	14.98		7.05	
Taxable income before net operating loss deductions and special deductions—line 28	46.35		57.52	
Net operating loss deduction—line 29a		18.51[b]		23.47[b]
Special deductions—line 29b		**0.18**		**0.69**
Taxable income—line 30	18.60[b]		**23.67**[b]	
Income tax—Schedule J, line 3	0.04		**2.18**	
Foreign tax credit—Schedule J, line 6a		**0.06**[b]		**0.02**[b]
General business credit—Schedule J, line 6d		0.73[b]		0.53[b]
Other credits—Schedule J, lines 6b, c, e, f		0.03[b]		0.06[b]
Total tax—Schedule J, line 11	0.81[b]		1.07[b]	
Total	**100.00**		**100.00**	
	Large FCDCs, no tax		Large USCCs, no tax	
Gross profit—line 3	2.92		1.28	
Total income—line 11	4.83[b]		4.30[b]	
Taxable income before net operating loss deductions and special deductions—line 28	79.42[b]		80.44[b]	
Net operating loss deduction—line 29a		9.46[b]		10.37[b]
Special deductions—line 29b		1.50[b]		1.24[b]
Taxable income—line 30	10.11[b]		10.62[b]	
Income tax—Schedule J, line 3	0.00[b]		0.14[b]	
Foreign tax credit—Schedule J, line 6a		1.90[b]		2.20[b]
General business credit—Schedule J, line 6d		0.00		0.72
Other credits—Schedule J, lines 6b, c, e, f		1.00[b]		1.16[b]
Total tax—Schedule J, line 11	2.72[b]		3.22[b]	
Total	100.00		100.00	

Source: GAO analysis of IRS data.

Note: Percentage estimates for all FCDCs have sampling errors of less than (+/-) 6 percentage points; percentage estimates for large FCDCs and USCCs have sampling errors of less than (+/-) 2 percentage points.

[a]These percentages will not total to the corresponding tax return line item percentage since corporations can report multiple deductions and credits.

[b]Differences between FCDCs and USCCs are not statistically significant.

Figure 8: Percentage of Total Deductions for FCDCs and USCCs That First Established No Tax Liability on Line 28, Tax Year 2005

Deductions (See instructions for limitations on deductions.)

Line	Item	Line	Percentage of all FCDCs	Percentage of all USCCs	Percentage of large FCDCs	Percentage of large USCCs
11	**Total income.** Add lines 3 through 10 ▶	11				
12	Compensation of officers (Schedule E, line 4)	12	1.7%	5.5%	1.4%	1.9%
13	Salaries and wages (less employment credits)	13	21.2%	25.0%	20.9%	24.6%
14	Repairs and maintenance	14	1.3%	1.9%	1.3%	1.9%
15	Bad debts	15	0.7%	1.0%	0.6%	1.2%
16	Rents	16	3.6%	5.0%	3.4%	4.4%
17	Taxes and licenses	17	4.4%	5.3%	4.3%	5.1%
18	Interest	18	18.3%	11.6%	19.5%	15.0%
19	Charitable contributions (see instructions for 10% limitation)	19	0.2%	0.2%	0.2%	0.3%
20a	Depreciation (attach Form 4562) 20a					
b	Less depreciation claimed on Schedule A and elsewhere on return 20b	20c	6.9%	5.8%	7.0%	6.5%
21	Depletion	21	0.3%	0.2%	0.3%	0.3%
22	Advertising	22	4.1%	2.7%	4.3%	3.0%
23	Pension, profit-sharing, etc., plans	23	1.6%	1.7%	1.7%	1.8%
24	Employee benefit programs	24	3.6%	3.5%	3.7%	3.7%
25	Domestic production activities deduction (attach Form 8903)	25	0.2%	0.1%	.02%	0.2%
26	Other deductions (attach schedule)	26	32.9%	30.8%	32.2%	30.5%
27	**Total deductions.** Add lines 12 through 26 ▶	27	101.0%	100.3%	101.0%	100.4%
28	Taxable income before net operating loss deduction and special deductions. Subtract line 27 from line 11	28				
29	**Less: a** Net operating loss deduction (see instructions) 29a					
	b Special deductions (Schedule C, line 20) 29b	29c				
30	**Taxable income.** Subtract line 29c from line 28 (see instructions if Schedule C, line 12, was completed)	30				

x% Percentage of all FCDCs

x% Percentage of all USCCs

x% Percentage of large FCDCs

x% Percentage of large USCCs

Source: GAO analysis of IRS information.

Notes: Percentages do not total to 100 due to rounding. All estimates have sampling errors of less than (+/-) .3 percentage points. Figure 8 reports the share of each type of deduction in total deductions for corporations that first established no tax liability on line 28 on their returns. For example, the figure shows that 18.3 percent of the total deductions claimed by FCDCs that reported zero taxable income on line 28 were deductions for interest expense.

Average Gross Receipts and Tax Liabilities

Table 4: FCDCs and USCCs Average Gross Receipts and Tax Liabilities, Tax Year 2005

Distribution by income tax liability	Number of returns	Percentage of returns	Average gross receipts (dollars in millions)	Average tax liability (dollars in millions)	Tax liability/ $1,000 gross receipts (dollars in millions)	Tax liability/ $1,000 total income (dollars in millions)	Tax liability/ $1,000 assets (dollars in millions)
No tax Liability							
All FCDCs	38,483	65.2[b]	$11.30	[a]	[a]	[a]	[a]
All USCCs	1,263,726	66.7[b]	$1.65	[a]	[a]	[a]	[a]
Large FCDCs	998	28.0	$373.09	[a]	[a]	[a]	[a]
Large USCCs	3,565	25.2	$303.45	[a]	[a]	[a]	[a]
$1 or more but less than $100,000							
All FCDCs	14,035	23.8	$10.02	$0.02	$1.69	$5.00	$1.33
All USCCs	594,094	31.4	$1.92	$0.01	$3.64	$8.20	$5.49
Large FCDCs	378	10.6	$263.18	$0.04	$0.16	$0.53	$0.12
Large USCCs	1,755	12.4	$114.12	$0.04	$0.33	$0.94	$0.20
$100,000 or more but less than $1 million							
All FCDCs	4,459	7.6	$56.07	$0.35	$6.26	$18.56	$4.86
All USCCs	29,636	1.6	$27.73	$0.30	$10.67	$25.10	$7.56
Large FCDCs	785	22.0	$263.56	$0.45[b]	$1.70	$5.37	$1.27
Large USCCs	3,367	23.8	$157.90	$0.45[b]	$2.85	$7.35	$2.08
$1 million or more							
All FCDCs	2,043	3.5	$828.14	$16.17	$19.52	$49.22	$6.99
All USCCs	7,364	0.4	$615.83	$18.06	$29.33	$48.37	$11.10
Large FCDCs	1,403	39.4[b]	$1,199.48	$22.28	$18.58	$47.41	$6.65
Large USCCs	5,446	38.5[b]	$826.24	$23.55	$28.50	$47.31	$10.79
Total							
All FCDCs	59,020	100.0	$42.66	$0.59	$13.84	$36.78	$5.91
All USCCs	1,894,819	100.0	$4.53	$0.08	$17.01	$31.11	$8.59
Large FCDCs	3,563	100.0	$662.61	$8.88	$13.39	$36.08	$5.56
Large USCCs	14,132	100.0	$446.72	$9.19	$20.56	$36.77	$8.43

Source: GAO analysis of IRS data.

Note: Estimates in the second column have sampling errors of less than (+/-) 4 percentage points; estimates in the third column have sampling errors of less than (+/-) $24 million dollars; estimates in the fourth, fifth, and seventh columns have sampling errors of less than (+/-) $0.5 million dollars; estimates in the sixth column have sampling errors of less than (+/-) $1.2 million dollars.

[a]Not applicable.

[b]Differences between FCDCs and USCCs are not statistically significant.

Corporations That Were New

Table 5: Percentage of FCDCs and USCCs That Were New, Tax Years 1998 through 2005

Tax year	FCDCs, all	USCCs, all	FCDCs, large	USCCs, large
1998	26.1	20.2	11.9	10.4
1999	25.4	19.4	13.5	10.1
2000	23.7	18.4	13.6	9.1
2001	21.9[a]	19.4[a]	14.0	8.2
2002	23.6[a]	19.1[a]	11.2	7.2
2003	19.8[a]	18.5[a]	10.0	6.6
2004	19.9[a]	18.1[a]	9.5	7.1
2005	22.2[a]	18.8[a]	9.1	8.0

Source: GAO analysis of IRS data.

Note: Percentage estimates for all FCDCs have sampling errors of less than (+/-) 5 percentage points; percentage estimates for large FCDCs have sampling errors of less than (+/-) 2 percentage points; USCCs have sampling errors of less than (+/-) 1 percentage point.

[a]Differences between FCDCs and USCCs are not statistically significant.

Cost Ratios by Major Industry

Table 6: FCDCs and USCCs Cost Ratios by Major Industry, Tax Year 2005

	Cost of goods sold as a percentage of gross receipts		Purchases as a percentage of gross receipts		Interest as a percentage of gross receipts	
Industry	**All**	**No tax**	**All**	**No tax**	**All**	**No tax**
All FCDCs						
Manufacturing	77.8	77.4	65.6	55.8	2.3	3.6
Wholesale trade	82.2	84.9	76.1	76.2	1.0	1.0
Financial services	10.3[a]	26.7	5.2	17.4	156.6	68.5
Nonfinancial services	41.2	37.0	15.4	14.8	3.6	5.1
Retail trade	71.7[a]	79.9	67.0	79.4	1.1	1.2
Other	53.7	54.2[a]	19.1	13.6	5.2	7.1
Total	**73.1**	**71.4**	**60.4**	**51.3**	**6.0**	**4.6**
All USCCs						
Manufacturing	69.8	72.6	48.7	51.6	2.6	4.0
Wholesale trade	80.6	79.6	74.9	71.3	0.9	1.2
Financial services	10.6[a]	13.9	3.5	4.8	87.0	45.2
Nonfinancial services	26.5	23.9	10.5	10.3	1.9	2.0
Retail trade	71.5[a]	74.8	68.3	70.4	0.9	1.0
Other	51.8	52.5[a]	23.2	20.8	4.1	5.0
Total	**59.5**	**54.6**	**42.8**	**36.3**	**5.5**	**4.9**
Large FCDCs						
Manufacturing	77.9	77.4	66.0	55.7	2.3	3.8
Wholesale trade	82.6	87.3	76.4[a]	77.5	1.1	1.1
Financial services	9.4[a]	31.2	4.9	20.5	173.1	82.2[a]
Nonfinancial services	42.3	37.4	15.5	15.2	3.9	5.6
Retail trade	72.4	82.8	67.8[a]	83.2	1.1	1.3[a]
Other	53.9	54.1	19.1	12.3	5.5	7.7
Total	**73.6**	**72.3**	**61.1**	**51.4**	**6.2**	**4.8**
Large USCCs						
Manufacturing	70.3	74.5	49.3	54.4	2.7	4.5
Wholesale trade	82.3	83.2	76.0[a]	72.4	1.0	1.4
Financial services	8.9[a]	11.5	3.3	5.1	129.2	86.9[a]
Nonfinancial services	30.3	29.7	10.1	9.7	2.9	3.9

Industry	Cost of goods sold as a percentage of gross receipts		Purchases as a percentage of gross receipts		Interest as a percentage of gross receipts	
	All	No tax	All	No tax	All	No tax
Retail trade	70.3	74.7	67.3[a]	70.7	1.0	1.2[a]
Other	48.9	48.6	22.3	18.2	5.2	7.2
Total	**61.5**	**59.0**	**44.4**	**38.4**	**6.9**	**7.7**

Source: GAO analysis of IRS data.

Note: All estimates have sampling errors of less than (+/-) 6 percentage points.

[a]Differences between FCDCs and USCCs are not statistically significant.

Appendix III: GAO Contact and Staff Acknowledgments

GAO Contact

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