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GAO

United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-254135

July 22, 1993

Senator Arlen Specter
United States Senate



149612

Dear Senator:

Your April 28, 1993, letter asked for our views on a taxpayer's suggestion about information reporting. Specifically, the taxpayer questioned the need to receive separate information reporting of interest payments via an Internal Revenue Service (IRS) Form 1099-INT, Interest Income when he also received this information via an annual cumulative bank statement.

Congress addressed this issue in the Interest and Dividend Tax Compliance Act of 1983 (PL 98-67). The Act repealed withholding of tax from certain interest and dividends but expanded information reporting of this income. Specifically, section 6049(c)(2) of the Internal Revenue Code was amended to require the separate mailing of IRS Form 1099 for reporting of interest payments. Currently, the subsection states

"(2) Time and form of statement. The written statement under paragraph (1)—
(A) shall be furnished (either in person or in a statement mailing by first-class mail which includes adequate notice that the statement is enclosed) to the person on or before January 31 of the year following the calendar year for which the return under subsection (a) was required to be made, and
(B) shall be in such form as the Secretary may prescribe by regulations."

The legislative history of PL 98-67 specifically addressed the taxpayer's question on the need for Form 1099 reporting in circumstances where taxpayers received annual cumulative bank statements. The 1983 Conference Committee report stated

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"Under present law, information returns need not be provided to payees on separate Forms 1099 in all circumstances. Rather, such information in some cases may be provided to payees on end-of-the-year business statements (such as bank statements)...."

In explaining adoption of the Senate proposal to require separate information reporting, the Conference Committee report stated that

"payors must provide payees with information statements with respect to interest, dividend, or patronage dividend payments in the form required by Treasury regulations. The conferees expect that the Treasury will require a separate official form be supplied to payees which contains a clear statement that the income being reported is subject to tax, and has been reported to the Internal Revenue Service, and if not reported will generate a negligence penalty.

Under the conference agreement, these information statements must be provided to the payee in a separate mailing which contains no additional information other than information relating to the correction of taxpayer identification numbers."

Although the legislative history does not explain the necessity of the separate mailing, perhaps the added visibility provided by a separate mailing increases taxpayer compliance more so than bank statements containing other information unrelated to taxes. The Treasury Department has directed that interest income be reported on IRS Form 1099-INT.

Information reporting is viewed by IRS as central to its Compliance 2000 program. Compliance 2000's objective is to maximize voluntary compliance while minimizing taxpayer burden and government costs. In 1991 hearings on the information returns program, the then IRS Commissioner testified on the role and benefits of information reporting within the Compliance 2000 framework. Overall, IRS estimated that between 35 to 45 percent of all individual tax returns are based solely on data provided under the information reporting program. In the absence of information reporting, IRS has found that individuals voluntarily reported between 15 to 75 percent of the income they received (depending on the type of income). In contrast, individuals who

received information returns voluntarily reported between 85 to 99 percent of their income (again depending on type of income).

Reporting of interest and dividend information was cited as one area that showed the benefits of providing taxpayers with timely, accurate, and usable information. The former Commissioner noted in 1991 that IRS enforcement yield from its activities in these areas had declined over the past several years. From IRS' perspective, this was clear evidence that information reporting increased voluntary compliance and reduced IRS' tax code administration costs.

We support the use of information reporting (including separate mailing) to improve compliance and reduce costs. For example, our 1993 report on forgiven debts found that information reporting and subsequent IRS computer matching of debts forgiven by a federal agency raised compliance levels for taxpayers with forgiven debt income from 1 percent to 68 percent. Had IRS pursued another 32 percent who may have underreported forgiven debt income, the compliance level might have been higher.

Regarding the taxpayer's suggestion that middlemen such as banks forward Forms 1099 to payees, section 6049(d)(4) already requires this. The subsection currently states

"Financial institutions, brokers, etc., collecting interest may be substituted for payor. To the extent and in the manner provided by regulations, in the case of any obligation—
(A) a financial institution, broker, or other person specified in such regulations which collects interest on such obligation for the payee (or otherwise acts as a middleman between the payor and the payee) shall comply with the requirements of subsections (a) and (c), ..."

By April 2, 1993 correspondence, IRS advised the taxpayer that his bank as a middleman should be providing him with a Form 1099-INT in this situation.

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If you have any further questions about IRS' information reporting program, please call Al Stapleton or Tom Short of my staff on (202) 272-7904.

Sincerely yours,

A handwritten signature in cursive script that reads "Jennie S. Stathis".

Jennie S. Stathis
Director, Tax Policy and
Administration Issues