GAO Highlights

Highlights of GAO-15-16, a report to the Chairman, Committee on Finance, United States Senate

October 2014

INDIVIDUAL RETIREMENT ACCOUNTS

IRS Could Bolster Enforcement on Multimillion Dollar Accounts, but More Direction from Congress Is Needed

Why GAO Did This Study

In 2014, the federal government will forgo an estimated $17.45 billion in tax revenue from IRAs, which Congress created to ensure equitable tax treatment for those not covered by employer-sponsored retirement plans. Congress limited annual contributions to IRAs to prevent the tax-favored accumulation of unduly large balances. But concerns have been raised about whether the tax incentives encourage new or additional saving. Congress is reexamining retirement tax incentives as part of tax reform.GAO was asked to measure IRA balances and assess IRS enforcement of IRA laws.

This report (1) describes IRA balances in terms of reported FMV aggregated by taxpayers; (2) examines how IRA balances can become large; and (3) assesses how IRS ensures that taxpayers comply with IRA tax laws. To address these objectives, GAO analyzed 2011 IRS statistical data, reviewed IRS documentation and relevant literature, and interviewed government officials, financial industry stakeholders, and academics. GAO compared IRS enforcement plans and procedures with law and criteria for evaluating an enforcement program.

What GAO Recommends

Congress should consider revisiting its legislative vision for the use of IRAs. GAO makes five recommendations to IRS, including approving plans to fully compile and digitize new data on nonpublicly traded IRA assets and seeking to extend the statute of limitations for IRA noncompliance. IRS generally agreed with GAO's recommendations.

View GAO-15-16. For more information, contact James R. McTigue, Jr., at (202) 512-9110 or mctiguej@gao.gov or Charles A. Jeszeck at (202) 512-7215 or jeszeckc@gao.gov.

What GAO Found

For tax year 2011 (the most recent year available), an estimated 43 million taxpayers had individual retirement accounts (IRA) with a total reported fair market value (FMV) of $5.2 trillion. As shown in the table below, few taxpayers had aggregated balances exceeding $5 million as of 2011. Generally, taxpayers with IRA balances greater than $5 million tend to have adjusted gross incomes greater than $200,000, be joint filers, and are age 65 or older. Large individual and employer contributions sustained over decades and rolled over from an employer plan would be necessary to accumulate an IRA balance of more than $5 million. There is no total statutory limit on IRA accumulations or rollovers from employer defined contribution plans.

Estimated Taxpayers with Individual Retirement Accounts (IRA) by Size of IRA Balance, Tax Year 2011

	Number of taxpayers			Total IRA fair market value balances (Dollars in billions)		
IRA Balance	Estimate	95% confidence interval		Estimate	95% confidence interval	
$1 million or less	42,382,192	42,094,009	42,670,375	$4,092	$4,038	$4,147
> $1 million to $2 million	502,392	470,897	533,887	674	632	717
> $2 million to $3 million	83,529	72,632	94,426	198	173	224
> $3 million to $5 million	36,171	30,811	41,531	133	114	153
> $5 million to $10 million	7,952	6,120	9,783	52	40	64
> $10 million to $25 million	791	596	985	11	8	13
> $25 million	314	115	650	81	8	225

Source: GAO analysis of IRS data. | GAO-15-16

Notes: The taxpayer reflects a taxpaying unit including individuals as well as couples filing jointly, which may have more than one IRA owner. The IRA balance aggregates the value of all IRAs owned, including inherited IRAs.

A small number of taxpayers has accumulated larger IRA balances, likely by investing in assets unavailable to most investors—initially valued very low and offering disproportionately high potential investment returns if successful. Individuals who invest in these assets using certain types of IRAs can escape taxation on investment gains. For example, founders of companies who use IRAs to invest in nonpublicly traded shares of their newly formed companies can realize many millions of dollars in tax-favored gains on their investment if the company is successful. With no total limit on IRA accumulations, the government forgoes millions in tax revenue. The accumulation of these large IRA balances by a small number of investors stands in contrast to Congress's aim to prevent the tax-favored accumulation of balances exceeding what is needed for retirement.

The Internal Revenue Service (IRS) has enforcement programs covering specific aspects of IRA noncompliance, such as excess contributions and undervalued assets. As recommended by an internal task team, IRS plans to collect data identifying nonpublicly traded assets comprising IRA investments. IRS expects the data will help it identify potential IRA noncompliance. However, research on those taxpayers and IRA assets at risk will hinge on getting resources to effectively compile and analyze the additional data. IRS officials said IRA valuation cases are audit-intensive and difficult to litigate because of the subjective nature of valuation. Additionally, the 3-year statute of limitations for assessing taxes owed can pose an obstacle for IRS pursuing noncompliant activity that spans years of IRA investment.