

# CIC Placement and Reporting Effects

Andrew Zilles

1 May 2024

- “Furthermore, we conjecture that some managers may simply be **unable to credibly communicate information** about the firm’s tax planning without **divulging too much information to the tax authorities.**” [1]
- “Further, managers cannot costlessly disclose the accrual because **the tax authority could use that information** to pursue additional claims” [2]

Firms want tell us more, but that would lead to a higher chance of audit

- The IRS has an LB&I division and established a CIC program
- This ensures the largest and most complex companies will face audit certainty every year.
- "We estimate that firms assigned to the CIC program account for **between 65 and 70 percent** of the U.S. market capitalization in 2011." [3]

**Do Firms change how they communicate under audit certainty?**

Prior literature has identified size and complexity as determinants of CIC assignment [4] [5]

$$CIC_{Firm} = \alpha + \beta Size + \gamma Complexity + \epsilon$$

The IRM Internal Revenue Manual (IRM) also outlines official determinants of complexity. These can be categorized into Size and Complexity variables.

Items from the IRM outline include:

- Total Assets
- Net Sales
- Number of Geographic Segments
- Number of Business Segments
- Foreign Sales
- Foreign Tax

$$CIC_{Firm} = \alpha + \beta_1 AssetPoints + \beta_2 GrossReceiptsPoints + \gamma_1 GeoSegPoints + \gamma_2 BusSegPoints + \gamma_3 ForeignSalesPoints + \gamma_4 ForeignTaxPoints + \epsilon$$

## Utilized Compustat Segments and Fundamental Annual through WRDS



- Creating a table that counted the number of Geographic and Business segments reported by each firm for each fiscal year
- Merging datasets on a unique firm identifier and fiscal year end to combine financial data and segment data
- Implementing the point system guidance from the IRM based on financial and segment data
- Data cleaning and model setup

# Findings

*CICFirm* = 1 if firm is  
assigned to CIC  
program during  
current year

[1]

*Constant* -5.822\*\*\*  
(0.091)

*AssetPoints* 0.339\*\*\*  
(0.012)  
[0.025]

*GrossReceiptsPoints* 0.502\*\*\*  
(0.018)  
[0.038]

*GeoSegPoints* 0.221\*\*\*  
(0.021)  
[0.017]

*BusSegPoints* 0.154\*\*\*  
(0.019)  
[0.012]

*ForeignSalesPoints* 0.052\*\*  
(0.023)  
[0.004]

*Foreign TaxPoints* 0.224\*\*\*  
(0.047)  
[0.017]

Additional sample cuts None

*N* 23,094

Pseudo  $R^2$  (%) 59.71

Area under ROC curve (%) 94.02

Coefficients:

	Estimate	Std. Error	z value	Pr(> z )	
(Intercept)	-1.069e+01	2.422e-01	-44.15	<2e-16	***
at	8.253e-04	2.562e-05	32.21	<2e-16	***
sale	2.210e-03	6.405e-05	34.50	<2e-16	***
GEOSEG	9.128e-01	2.960e-02	30.83	<2e-16	***
BUSSEG	1.172e+00	3.479e-02	33.70	<2e-16	***
ForeignSales	4.045e-03	2.087e-04	19.38	<2e-16	***
ForeignTax	2.454e-02	1.952e-03	12.57	<2e-16	***

Signif. codes: 0 '\*\*\*' 0.001 '\*\*' 0.01 '\*' 0.05 '.' 0.1 ' ' 1

(Dispersion parameter for binomial family taken to be 1)

Null deviance: 21440.7 on 15500 degrees of freedom  
Residual deviance: 3893.3 on 15494 degrees of freedom  
AIC: 3907.3






I utilized AI for my project in the following ways:

- ChatGPT for debugging code and helping me write LaTeX
- Github Copilot extension in R to speed up typing long chunks of code
- Claude for checking the boxes and making sure everything is polished
- "Hey Google, play Taylor Swift"
- Hundreds of hours watching Instagram videos and YouTube algorithms for "mental health breaks"

In intend to take this framework farther over the summer and look at how firms are communicating in their 10-Ks, 10-Qs, conference calls, and other public releases to see if there are differences in the level and nature of communication between firms in vs. those not in the CIC program.



# References

-  Balakrishnan, Blouin, Guay. (2019) "Tax Aggressiveness and Corporate Transparency". *The Accounting Review*.
-  Dhaliwal, Gleason, Mills. (2004) "Last-Chance Earnings Management: Using the Tax Expense to Meet Analysts' Forecasts". *Contemporary Accounting Research*
-  Ayers, Seidman, Towery. (2019) "Tax Reporting Behavior Under Audit Certainty". *Contemporary Accounting Research*
-  Mills. (1998) "Book-tax differences and Internal Revenue Service Adjustments". *Journal of Accounting Research*
-  Hanlon, Mills, Slemrod. (2007) "An empirical examination of corporate tax noncompliance. In *Taxing Corporate Income in the 21st Century*", eds, Auerbach, Hines, Slemrod. Cambridge, UK: Cambridge University Press, 171–210.)