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WASHINGTON—The U.S. corporate tax system is "deeply flawed and in need of reform," according to a report released Friday by an advisory panel to the White House led by former Federal Reserve Chairman Paul Volcker.

The report puts forward several proposals aimed at improving corporate taxes, including cutting the corporate tax rate and limiting businesses' ability to deduct interest costs.

Coming up with ideas to fix the corporate tax system was one of three tasks U.S. President Barack Obama assigned the Volcker panel when it was formed in February 2009. The panel was also asked for options to make tax filing less of a headache, and improve tax compliance.

Options discussed in Friday's report include having the IRS mail out prefilled tax returns, which would only require a signature in some cases, and combining the child tax credit and dependent exemptions into a single "family credit."

The 126-page report provides "helpful advice" to the Obama administration and Congress, according to its preface, but doesn't endorse specific proposals. However, it is likely to inform policy makers' discussions in the coming years on how to simplify and overhaul the U.S. tax system.

The panel's refusal to make firm recommendations was seen by some as a desire to avoid the fate of the 2005 tax-overhaul panel appointed by then President George W. Bush. That panel proposed a comprehensive redesign of the tax system, which was rejected by lawmakers with very little debate.

Members of the Volcker panel voted Friday unanimously to send the report to Mr. Obama. Harvard University economist Martin Feldstein, who spearheaded the tax panel report, said if Congress heeded options put forward in the report, "we'd have a much better tax system."

On corporate taxes, the panel said that limiting deductions for interest expense would lessen a bias in the tax code against equity financing. Specifically, the report suggests limiting deductions for interest expense in excess of $5 million a year. Deductions above that amount could be subject to a 90% limitation.

Such a change would result in a higher tax burden on sectors that invest heavily in physical capital, like manufacturers and utilities.

**The report also highlighted a growing shift by business away from corporate structures toward partnerships and other flow-through arrangements. That has caused the corporate tax base to erode.**

**One way to reverse the trend would be to force large and publicly traded businesses that now pay taxes at the shareholder level only, to pay the corporate income tax.**

**In a conference call with reporters to discuss the report, a senior Obama administration official singled out privately held oil refiner Koch Industries as a "really giant firm" that is structured as a pass-through.**

That creates a narrower base because we've literally got something like 50% of business income in the U.S. going to businesses that don't pay any corporate income tax," the official said.

The U.S. statutory corporate tax rate of 35% is the second highest among developed nations, behind Japan, the

report notes. But corporate tax collections as a share of gross domestic product is among the lowest in the world--in part because of the high proportion of businesses that don't pay corporate income tax.

Taking into account tax credits and deductions, the effective U.S. federal corporate tax rate is about 29%, according to the report.

Mr. Volcker said the panel might follow up with additional work on the corporate tax findings.

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