TALKING TAXES

State Corporate Tax Disclosure: Why It's Needed

Corporate income taxes are in decline. Corporate tax revenues represent a smaller piece of the federal and state tax pie than at almost any time since World War II. While it is possible to diagnose some of the reasons for this decline on the federal level, very little public information is available to help policymakers evaluate the health of the corporate taxes collected by state governments. For this reason, some policymakers have called for better public disclosure of how much the biggest corporations are paying in state taxes. This policy brief evaluates arguments in favor of (and against) requiring detailed state corporate tax disclosure.

The Problem: Corporate Taxes Are in Decline

On both the federal and state level, corporate taxes have diminished in importance. In 1969, the federal corporate income tax represented 20 percent of federal taxes, and 3.9 percent of Gross Domestic Product (GDP). But the tax has declined steadily, to the point that in 2003 the corporate tax was just 8 percent of federal tax revenues—and 1.3 percent of GDP. Federal corporate taxes are now approaching their lowest levels in fifty years. This decline has occurred despite robust growth in corporate profits throughout this period. And Congress has not cut corporate tax rates. So how can the decline of the corporate income tax be explained?

Corporate Tax Disclosure on the Federal Level

At the federal level, lawmakers have the ability to at least partially diagnose the ailments of the corporate tax. This is because federal law requires all publicly held corporations to file annual reports with the Securities and Exchange Commission (SEC). These reports include data on corporate profits and federal taxes paid, and often include information on specific tax breaks claimed by each corporation. This information is available on the SEC's Internet site.

Corporate Tax Disclosure Helps Inform Tax Reform Efforts

These SEC filings allow analysts to determine how much the nation's largest corporations have paid in federal taxes and compare this to their reported profits. In a series of reports, ITEP and Citizens for Tax Justice (CTJ) have shown that many profitable corporations pay little or no federal income tax. A 1985 CTJ report surveyed 250 of the nation's most profitable corporations, and found that more than half of these companies paid absolutely nothing in federal income taxes in at least one year between 1981 and 1985. CTJ's report also documented the extent to which these zero-tax corporations were benefitting from special tax breaks—and showed that these loopholes often treated direct competitors in the same industry very differently, putting some companies at an unfair competitive disadvantage.

Largely because of outrage arising from the release of information like this, Congress passed—and President Reagan signed—federal tax reform legislation in 1986 that eliminated many of the tax breaks that made these "zero-tax corporations" possible. Congress toughened the federal Alternative Minimum Tax (which most states still lack)

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and repealed various wasteful tax loopholes.

The most compelling argument for corporate tax reform in 1986 was that corporations were not paying their fair share in taxes. But this argument could never have been made convincingly if the disclosure of corporations' taxable profits and tax payments was not required. Thanks to these same federal disclosure requirements, we now know that the widespread tax avoidance of the early 1980s has resurfaced. A September 2004 CTJ/ITEP report found that 275 of the most consistently profitable Fortune 500 corporations collectively paid less than half of the nominal federal corporate tax rate of 35 percent in the two-year period between 2002 and 2003, and that 82 of these companies paid no federal tax at all at least once between 2001 and 2003.

Corporate Tax Disclosure in the States

Unfortunately, neither the SEC nor most state governments require corporations to release detailed information on their state corporate tax payments—so it's hard to identify which corporations are not paying their fair share at the state level. A few states have now implemented some form of corporate tax disclosure. For example, Massachusetts now requires disclosure of basic information about profits, taxes paid and tax credits received. But most states still have no such requirements—and states that currently have such requirements tend not to enforce them.

False Arguments Against Corporate Tax Disclosure

Opponents of corporate tax disclosure contend that it violates corporate privacy and will hurt businesses. They say that corporate secrets will be disclosed. But these scare scenarios are unfounded. Most of the necessary information is already available on the national level for publicly-traded companies, thanks to SEC filing requirements. And no one has argued that existing federal reporting requirements have hurt businesses.

Nor should states fear that businesses will move to other states if a corporate disclosure law is passed. Businesses consistently cite state taxes as a minor factor in their locational decisions—and if disclosure leads to a fairer tax structure, this will lead to a more attractive tax environment for companies seeking to compete in a state.

The real basis for corporate complaints about disclosure is that corporations not paying their fair share are afraid they will be found out. When CTJ's studies of federal tax avoidance made it clear that many profitable corporations were paying no taxes, while others were paying at relatively high rates, the high-tax segment of the business community showed considerable support for federal reforms. Disclosure of similar discrepancies in state taxes is likely to prompt calls for a level playing field on the state level, too.

Corporate Disclosure: An Important Tool for Tax Fairness

Tax fairness is important. The perception that state and local taxes are treating individuals and corporations fairly is a cornerstone of public support for the tax system and for the government. But the fairness of corporate taxes cannot be evaluated without some basic information about how much companies pay in taxes, and how much they earn. If some corporations are paying less in taxes than they should be, then we need to know how and why. If some companies are paying a lot relative to other tax-avoiding corporations, policy makers should know this too. Corporate tax disclosure is the best means available to ensure that each corporation is treated fairly—and that corporations as a group pay their fair share of taxes.

To find out more about this issue, contact ITEP at (202) 626-3780