CRS INSIGHT

Public Disclosure of Corporate Tax Returns

July 16, 2018 (IN10929)

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Federal corporate tax returns are confidential and protected from public disclosure under Section 6103 of the Internal Revenue Code (IRC), as enacted by the Tax Reform Act of 1976 (P.L. 94-455). Before 1976, corporate tax returns where classified as part of the "public record" to varying degrees. Since 1976, there have been occasional calls for the privacy veil to be lifted in response to aggressive tax planning and evasion. This Insight examines several issues surrounding public disclosure of corporate tax returns; however, the discussion below does not address important legal and constitutional issues related to tax return disclosure. When considering the issues discussed below, it is important to note that tax disclosure is not all or nothing. Policymakers may seek a balance between corporate confidentiality and the public's desire to review certain corporate tax information it believes would be informative.

Tax Compliance

Public disclosure of corporate tax returns could increase tax compliance. If corporate returns were public information, the number of people who could scrutinize them would increase significantly—tax accountants, attorneys, and economists, as well as the public in general. These observers could potentially serve as tax watchdogs, reviewing corporate returns and highlighting discrepancy or suspicious tax strategies. Additionally, corporations may be more careful to avoid errors in their tax preparation. This argument is sometimes summarized in the research literature as "sunshine is the best disinfectant."

It is not clear, however, whether widespread public access would improve tax compliance given the complexity of corporate tax returns and federal tax law. Corporate tax returns can run into the thousands of pages, as can the tax law that includes statute and regulations. There is the possibility that untrained investigators could misinterpret tax information and draw misinformed conclusions. Additionally, the Internal Revenue Service (IRS) currently audits the largest corporations nearly continuously, and in some cases maintains a physical presence in a company's office.

Disclosure could also increase tax compliance via "public shaming." If corporations know that the public will see what they are paying in taxes and the strategies they are using to avoid taxes, they may refrain from using tax planning techniques that could damage the company's public reputation.

The evidence on the effectiveness the public shaming is mixed. A 2009 study by professors Michelle Hanlon and Joel Slemrod looked at stock price responses to revelations of corporate tax aggressiveness and found limited evidence of public backlash. Similarly, professors Chelsea Rae Austin and Ryan Wilson did not find evidence that tax avoidance had reputational costs for companies in a 2013 study.

However, in 2012, Starbucks volunteered to pay an extra £20 million in taxes in response to reports and a UK Parliament hearing that revealed the company had generated losses in the United Kingdom and, as a result, had no UK corporate tax liability for 14 years. In 2014, when the issue of corporate inversions was well reported in the press, Walgreens considered inverting but eventually decided against it. Some said public backlash was the reason, although the company said otherwise.

Tax compliance and collections could also unintentionally suffer if greater disclosure increases tax planning aggressiveness. Depending on the degree of disclosure, corporate competitors would be able to see each other's actual tax liability and tax planning strategies. This could lead corporate tax departments to take more aggressive positions in attempt to lower their company's tax bill to stay competitive with industry counterparts. Additionally, public disclosure could allow corporate tax departments and outside tax advising firms to use the information to develop models to predict the likelihood of an IRS audit from pursuing a particular tax strategy.

Corporate Oversight

A potential justification for public release of corporate tax returns is that it will improve the government's ability to regulate and oversee corporations. The Securities and Exchange Commission (SEC) requires corporations to publicly release financial accounting statements so that investors and regulators can make informed decisions about the health of companies. Whether or not publicly releasing corporate tax returns will assist regulators depends on the information government regulators would gain beyond what they already have access too. The IRS already requires reconciliation of financial statement income with net and taxable income on Schedule M-3 of the corporate tax return. In nontax criminal investigations, government attorneys may obtain tax returns via court order. The SEC can request tax return information directly from corporations in civil security cases. Furthermore, the Justice Department can obtain tax return information when investigating criminal financial security cases.

Financial Market Functioning

Some proponents of corporate tax disclosure argue that the additional information could improve financial market functioning. Investors need accurate information to make informed investment decisions. The information that investors rely on mostly comes from SEC-required financial statements. If financial statements lack or do not accurately provide some tax-related information, investors could potentially benefit from tax disclosure.

Inform the Public and Policymakers

Granting access to corporate tax returns could help to educate the public and inform policymakers by showing what corporations pay in taxes and which tax incentives they benefit from. Corporate tax rate figures reported in the press are typically based on SEC financial filings, which rely on different accounting standards than required by the IRS for tax purposes. This makes it difficult to know with any certainty how much a particular corporation pays in taxes. For example, while public corporations are required to report their effective tax rate in their SEC 10-K filing the rate is computed using generally accepted accounting principles (GAAP), not tax accounting standards. Additionally, corporations only have to report a consolidated worldwide effective tax rate, not the effective tax rate for each country where it has operations. Current disclosure law also makes it difficult to know which tax incentives individual corporations are benefiting from. Increased disclosure could assist policymakers when drafting legislation, and also help shed light on corporate tax planning, which may be useful to the general public.