Funding the Future

US corporations pay tax at 17% - and that's just not en...

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Prof Kim Clausing sent me a link to a new report from the United States Government Accountability Office entitled 'Corporate Income Tax: Effective Tax Rates Can Differ Significantly from the Statutory Rate'. A number of things are worth highlighting from this report. The first is on why they did the study:

*Proponents of lowering the U.S. corporate income tax rate commonly point to evidence that the U.S. statutory corporate tax rate of 35 percent, as well as its average effective tax rate, which equals the amount of income tax corporations pay divided by their pretax income, are high relative to other countries. However, GAO's 2008 report on corporate tax liabilities (*GAO-08-957) found that nearly 55 percent of all large U.S.-controlled corporations reported no federal tax liability in at least one year between 1998 and 2005.

Given the difficult budget choices Congress faces and its need to know corporations' share of the overall tax burden, GAO was asked to assess the extent to which corporations are paying U.S. corporate income tax. In this report, among other things, GAO (1) defines average corporate ETR and describes the common methods and data used to estimate this rate and (2) estimates average ETRs based on financial statement reporting and tax reporting. To conduct this work, GAO reviewed economic and accounting literature, analyzed income and expense data that large corporations report on the Schedules M-3 that they file with Internal Revenue Service (IRS), and interviewed IRS officials.

As they then concluded:

Effective tax rates (ETR) differ from statutory tax rates in that they attempt to measure taxes paid as a proportion of economic income, while statutory rates indicate the amount of tax liability (before any credits) relative to taxable income, which is defined by tax law and reflects tax benefits and subsidies built into the law. Lacking access to detailed data from tax returns, most researchers have estimated ETRs based on data from financial statements. A common measure of tax liability used in past estimates has been the current tax expense–either federal only or worldwide (which comprises *federal, foreign, and U.S. state and local income taxes). The most common measure of income for these estimates has been some variant of pretax net book income.*

I have, of course, used this method myself, and have always stood by it. Some pro-business groups and right-leaning academics have criticised it, but as the GAO has noted, there has been no real alternative.

However, as they noted:

GAO was able to compare book tax expenses to tax liabilities actually reported on corporate income tax returns. For tax year 2010 (the most recent information available), profitable U.S. corporations that filed a Schedule M-3 paid U.S. federal income taxes amounting to about 13 percent of the pretax worldwide income that they reported in their financial statements (for those entities included in their tax returns). When foreign and state and local income taxes are included, the ETR for profitable filers increases to around 17 percent. The inclusion of unprofitable firms, which pay little if any tax, also raises the ETRs because the losses of unprofitable corporations greatly reduce the denominator of the measures. Even with the inclusion of unprofitable filers, which increased the average worldwide ETR to 22.7 percent, all of the ETRs were well below the top statutory tax rate of 35 percent. GAO could only estimate average ETRs with the data available and could not determine the variation in rates across corporations. The limited available data from Schedules M-3, along with prior GAO work relating to corporate taxpayers, suggest that ETRs are likely to vary considerably across corporations.

The GAO draws no conclusions from this. I will though.

First, quite clearly you do not have to be a flat tax aficionado to realise allowances and reliefs distort tax payments too significantly in this case.

Second, reducing rates and reducing allowances may be appropriate in this case - if tax neutraility is sought. But when capital takes too large a share of GDO, as now, just reducing allowances may be more appropriate.

Third, this issue leaves aside profit shifting to some degree. That still needs to be addressed.

The result is that if US corporations are paying tax at only 17% at best if and when they agree to declare a profit capital is being under taxed inequality is being maintained and injustice continues - as is al too apparent in US society.

Companies do pay tax - as I have argued here. They are not paying enough either side of the Atlantic. And ordinary people suffer as a result. That is my conclusion from this report.