CONNECTICUT VOICES FOR CHILDREN

Increasing Public Disclosure of Business Tax Credits: Why It Is Important & How It Can Be Done

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The secrecy surrounding corporate tax reduction strategies should be eliminated.[1]

Disclosure of Business Tax Credits is Essential for Informed, Accountable Legislative Decision Making

- **Legislators cannot make informed budget decisions without understanding spending on the tax side of the budget.** Neither legislators nor the public are privy to critical data, including which companies are claiming tax credits and in what amounts, whether given tax expenditures tend to benefit or burden large or small businesses (or in-state or multi-national corporations), and what return on investment the state is receiving for the hundreds of millions of dollars of economic development funds granted through tax expenditures (that is, credits as well as preferential deductions and exemptions). For income years 2002 and 2003, 18 of the *largest* 100 businesses headquartered in Connecticut (based on 2003 sales) paid the minimum $250 corporate income tax and 18 paid the $250 business entity tax.[2]

- **Corporate tax credits often become hidden entitlements.** Unlike direct appropriations, tax expenditures are not subject to annual review by the legislature, despite their significant cost to the state. They become entitlements, remaining in place even during difficult budget times or when the circumstances that justified the enactment have changed.

- **The cost of corporate tax credits can increase unpredictably without legislative review**. Unless the total amount of an available credit is capped, when more businesses take advantage of the credit the state can lose revenues without oversight, resulting in unpredictable revenue streams and often in great cost to the state. For example: the Fixed Capital Investment Credit cost the state an estimated $52.8 million *more* in 2005 than in 1999. Between 1987 and 2005, the *total* number of returns claiming tax credits increased from 289 to 9,655 and the revenue loss due to tax credits climbed from an estimated $2.7 million to $175.3 million.[3]

- **The public expects and is entitled to transparency and accountability with respect to budget decisions.** Connecticut's Legislative Program Review and Investigations Committee recently completed a study of Connecticut's tax system. Among the key criteria it used to evaluate Connecticut's tax system was *accountability*. The report found that in order to be accountable the "system should be explicit in how revenues are raised, changes should be well publicized, and costs and benefits of tax policy should be examined."[4]

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[1] N. Byrnes & L. Lavelle, Special Report: Corporate Tax Game: How Blue Chip Companies Are Paying Less and Less of the Nation's Tax Bill, Business Week (March 31, 2003)

[2] *Connecticut's Tax System*, Legislative Program Review and Investigations Committee, January 19, 2006, p. 49. These entities may also have paid state sales and property tax, but no other state income tax.

[3] OFA, *CT Tax Expenditure Report,* 2004. The 2005 numbers are projected estimates.

[4] Connecticut Legislative Program Review and Investigations Committee, *Key Points: Preliminary Staff Findings Regarding Connecticut's Tax System,* Available at: http://www.cga.ct.gov/2005/pridata/Studies/CT_Tax_System_Briefing_Key_Points.htm

New Haven Office: 33 Whitney Ave. • New Haven CT 06510 • Phone: 203.498.4240 • Fax: 203.498.4242
Hartford Office: 53 Oak St. Suite 15 • Hartford CT 06106 • Phone: 860.548.1661 • Fax: 860.548.1783
Web Site: www.ctkidslink.org
E-mail: voices@ctkidslink.org

Some Suggestions for Increasing Public Disclosure

- **Require Company Specific Data For Publicly-Traded Companies and Other Large Business Entities (such as S-Corporations, LLCs and LLPs over a certain size)**: Require public access to company-specific information concerning Connecticut state taxes owed and paid, tax credits claimed, and/or other specific tax benefits enjoyed, including apportionment of income, by specific companies.

- **Increase Transparency And Accountability In The Use Of Tax Credits And Other Tax Expenditures**: Require firm-specific reporting of the companies that are claiming tax credits, how much each is claiming each year, and data about jobs created or lost (as is done in Arkansas, West Virginia, Massachusetts and Wisconsin[5]).

- **Sunset Tax Expenditures:** Current tax expenditures should expire unless re-approved after weighing the benefits of the tax expenditure against other potential uses for the funds; new tax expenditures should sunset within a specified time.

- **Expand OFA's Tax Expenditure Report**: Expand current tax incidence reporting by showing not only the approximate number of taxpayers who benefit from each tax expenditure (as is currently done), but also by providing more description of who these taxpayers are (individual or corporate; approximate size of taxpaying entity; geographic location; nature of business or company; average income of individuals/businesses; and number of employees).

- **Include A Tax Incidence Impact Statement In Fiscal Notes On Tax Expenditure Bills**: For fiscal notes on bills proposing new taxes, tax expenditures, or tax cuts, require the inclusion of not only potential revenue loss (or gain) but also a "tax incidence impact statement" that explains which taxpayers (by type of taxpayer, by income level, and – for businesses – by size of business) will derive the benefit (or bear the cost) of the tax change.

- **Develop A Unified Development Budget Report**: Connecticut could require that OFA and/or DECD publish a biennial Unified Development Budget Report that includes all state on-budget and off-budget economic development spending through grants and loans by public and quasi-public agencies, as well as through preferential tax breaks. This is especially important in light of the finding by Program Review Y Investigations Committee that:

> *[L]egislative efforts at spurring economic development through tax credits and incentives appear to have little positive effect on job growth or in enhancing the state's competitive position.*[6]

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[5] See Judith Lohman, *OLR Research Report: Tax Disclosure for Companies Receiving State Tax Exemptions and Credits*, 2005-R-0114, February 4, 2005, available at http://www.cga.ct.gov/2005/rpt/2005-R-0114.htm.

[6] *Connecticut's Tax System*, Legislative Program Review and Investigations Committee, January 19, 2006, pp. 1-2.