Most firms pay no income taxes - Congress

Study finds that the majority of domestic and foreign corporations in the United States avoid paying federal income taxes.

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NEW YORK (CNNMoney.com) -- Nearly two-thirds of U.S. companies and 68% of foreign corporations do not pay federal income taxes, according to a congressional report released Tuesday.

The Government Accountability Office (GAO) examined samples of corporate tax returns filed between 1998 and 2005. In that time period, an annual average of 1.3 million U.S. companies and 39,000 foreign companies doing business in the United States paid no income taxes - despite having a combined $2.5 trillion in revenue.

The study showed that 28% of foreign companies and 25% of U.S. corporations with more than $250 million in assets or $50 million in sales paid no federal income taxes in 2005. Those companies totaled a combined $372 billion in sales for the largest foreign companies and $1.1 trillion in revenue for the biggest U.S. companies.

The GAO report, which did not name any specific companies, said that some corporations reported zero income before deducting expenses while others said they had zero net income after deducting expenses. Either way, those companies reported no tax liability, the GAO said.

But many of the companies the report found had paid no tax were likely small businesses that pay other taxes. Generally, many small firms, because they do not have shareholders, are able to shift corporate income to individual income.

"Small businesses that are going to be liable for a lot of income tax are likely to use other tax forms so they only pay individual income taxes," said Eric Toder, a senior fellow at the Tax Policy Center.

The study was requested by Sens. Byron Dorgan, D-N.D, and Carl Levin, D-Mich., in an attempt to determine if corporations are abusing so-called transfer prices.

Transfer prices are charges on transactions between subsidiary companies within a larger corporate group. Companies may try to lessen their U.S. tax hit by improperly transferring income to foreign subsidiaries in countries with lower rates.

The GAO study did not attempt to determine if companies were abusing transfer prices, but it said that potential abuse of transfers could reduce the amount of taxes companies pay in the United States.

"The tax system that allows this wholesale tax avoidance is an embarrassment and unfair to hardworking Americans who pay their fair share of taxes," Dorgan said in a statement.

U.S. politicians disagree about how much income tax the government should levy on corporations. Currently the rate is 35%, but most foreign governments have set their rates below the U.S. level.

"The U.S. corporate tax rate stayed the same while foreign countries have drifted down, which increases the incentive for companies to report income in other countries," said Toder. "If the U.S. drops the rate to 30% but closes other tax loopholes, that may ultimately generate more tax revenue for the government." ■

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