Corporate Tax Disclosure: A Review of Concepts, Theories, Constraints, and Benefits

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Abstract
The aim of this paper is to offer an impression of the issues raised by the disclosure of companies’ tax information by supplying existing and historical viewpoints from the aspects of concepts, theory, constraints, benefits and measurements. We are concerned that full disclosure of organizations’ tax information could result in firms weakening tax information, hampering tax enforcement, and maybe, in a weakened structure, disclosing private data that could give a competitive benefit to those organizations that are not requested to do such a disclosure. Hence, some studies do not underpin full disclosure. On the other hand, full tax disclosure could have numerous beneficial impacts. It might put pressure on regulators to develop the tax system and it might incite companies to oppose aggressive tax decrease strategies. We anticipate and expect interested parties to take into consideration the best practices of tax disclosure in implementing their future plans.

Keywords: disclosure, tax disclosure, tax return, income tax

1. Introduction and Background
Pomp (1993) claimed that the issue of state company tax disclosure was raised in 1987 by a staff study for New York State's Legislative Tax Study Commission. Since this date, three states (Arkansas, Massachusetts, and West Virginia) have embraced regulations requiring some state-level disclosure by corporations. While Wisconsin has had a disclosure regulation since 1923, it has just as of late been utilized for tax policy purposes (Mazerov, 2007). Currently, activists around the globe call on governments to request disclosure of information for public users from companies about what, what amount and where on the globe firms, particularly multinational firms, pay taxes (Christians, 2013). Their point is to stir public thoughtfulness to the systemic under-taxation of multinational companies, to demonstrate that this is linked to the failure of development in developing countries, and to persuade law-makers that the public is curious in changing this model. In their mission for financial transparency through tax disclosure, activists are admitting themselves to an elite policy-making yard that has customarily been dominated by the political elites and seeking change. Tax transparency through applying tax disclosure norms challenges the tax policy standards developed within this yard, whilst the interest for activists in non-governmental organizations challenges the institutional foundations of contemporary worldwide tax policy-making (Christians, 2013).

Furthermore, Christians (2013) argued that, during recent years, the global financial crisis has produced and coordinated rescue operations across the rich countries. Adverse effects on large financial interests and commercial sectors, together with high budget deficits and budget cuts, have led to growing public concern about poverty and global financial inequality. During this time period, however, several multinational companies announced record profits for their operations in all parts of the world, whilst seemingly escaping the charges (Reuters, 2011). In a same vein, Fenster (2011) said that the international tax transparency is an universal phenomenon versus this occurrence and backdrop. Tax transparency activists seek to ask and respond to the question: how is it that the globe’s biggest profit centers are contributing so little to public revenue needs especially in developing nations? This is the question posed by activists, with an emphasis on the search for information rather than a request for a change (Christians, 2013). It is by no means the initial time tax information has been sought with respect to firms in the U.S. or somewhere else. Pomp (1993) discussed the U.S. experience with the disclosure of corporate tax and the development of the national policy.
In the next section this paper illustrates a review of the literature and background of tax disclosure, which involves definitions of and discussions on tax disclosure in companies. The following section reviews and discusses the underlying theories and previous literatures of the theories that link to tax disclosure. Further analyses and review follow in sections three and four on the practice of efficient tax disclosure by revising objectives, boundaries, motivations, and advantages of tax disclosure. The fifth part of this paper reviews literature in the measurement of tax disclosure and, finally, the last part is concluded.

2. Definitions of Tax Disclosure

Mazerov (2007) argued that state companies’ income tax disclosure was broadly discussed in the early 1990s, when legislature in Massachusetts was amended to implement a disclosure regulation. To contribute to the Massachusetts discussion, Prof Pomp (Note 1) wrote a major report in 1993 on companies’ tax disclosure (Pomp, 1993). Tax disclosures (TD) have been defined as a term utilized to depict two separate situations: “The first is the legal requirement to provide current taxation information to the other party. The second is related to transactions that may be viewed as tax sheltering that must be disclosed to the government when filing income taxes” (Francois, 2012, Para 1.2).

Moreover, Amir, Kirschenheiter, and Willard (1997) and Amir and Sougiannis (1999) found evidence that the independent disclosure of deferred tax liability (DTL) and deferred tax asset (DTA) components also supplies relevant information. Another merit of taxation disclosure that is worth mentioning is the provision of public access-by the disclosure of tax revenues in the U.S.-to annual income of tax exempt companies and the yearly reports of insurance firms. From the 1970s, the U.S. presidents have voluntarily disclosed their returns tax income publicly (OECD, 1999).

Among the OECD countries Lenter, Shackelford, and Slemrod (2003), found that only Finland, Sweden, Norway, and Japan allow several forms of public access to taxation information. In Japan, taxable income figures are overtly liberated if the company reports more than forty Million Yen (around 332 thousand $) in taxable revenue. In 2000, nearly around 70 thousand companies recorded enough taxable returns to request disclosure. None of the components of taxable revenue (interest, cost of goods sold, revenues, and so on.) were made publicly obtainable. Taxable revenue is disclosed publicly for all Swedish firms, and Norway makes information on both tax liability and taxable income publicly available. However, if a corporation records a tax loss, the total of the loss is not recorded. Instead, the tax authorities disclose a zero amount of taxable revenue and none of the components of the taxable revenue are made available to the public access. On the contrary, Finland supplies open admission to a database containing information on natural capital, income tax, and the amount of taxes to be paid amongst other figures. Reconciliations between book numbers and tax are also disclosed publicly for Finnish firms (Lenter et al., 2003).

Many researchers and practitioners expressed concern that Financial Interpretation No, (FIN) 48 disclosures supply a roadmap to the tax enforcement agents (Frischmann, Shevin, & Wilson, 2008; Mills, Robinson, & Sansing, 2010). In accordance with IRS's Large & Midsized Business Field Examiners’ Guide (2007), the disclosures required under FIN 48 must provide the service to some extent better inspection of a taxpayer’s uncertain tax positions; however, the disclosures are still not detailed enough to allow an ideal view of the issues and amounts at risk (Robinson & Schmidt, 2013). For instance, there may be a conditional tax liability listed in the tax footnotes of a big multinational taxpayer with the description “tax credits”; tax credits, however, could be the U.S., foreign, or state tax credits. Therefore, the “tax credits” in this instance may or may not in this case have the U.S. tax influence (IRS, 2007). While FIN 48 does not require the disclosure of information about exact operations, the level of tax reserves and disclosures concerning uncertain tax positions are utilized by enforcement agents to plan their own audits. Thus, managers have a motivation to supply lower tax reserves and low quality disclosures, since even the size of the reserve tax will be an indicator of tax planning and utilized by the IRS (Blouin, Gleason, Mills, & Sikes, 2010; Frischmann et al., 2008).

Managers of companies who are using tax planning do not wish to disclose information about these activities (Gleason & Mills, 2002). In accordance with FIN 48, disclosures would be more expensive and costly for companies in tax planning. Frischmann et al. (2008) documented negative market responses to the release of FIN 48, indicating that these reactions were based on the assumption that tax planning would be costly for the companies involved. This is because tax planning requires the integration of the institute with more staffing and increased budgets (John, 2003). Mills, Erickson, and Maydew (1998) postulated as an example that the expenditure of disclosure by companies with the largest tax planning ought to be higher. This is because companies that disclose tax information to the public undertake higher levels of tax planning and, as a consequence, owe increased amounts to the IRS, thus increasing the cost of disclosure (Gross, 2011). In order to avoid being
liable for large IRS fees, some investors avoid investing in companies with high levels of tax planning. Taxes and fees imposed by the IRS upon companies employing illegal tax avoidance measures can also increase the cost of disclosing tax information (Mills et al., 1998). Therefore, it could be costly for companies with higher levels of tax planning that have too much to hide and could get more control over their tax reserves (Sidhu & Whittred, 2003). Hence, Gross (2011) expected that higher corporate tax planning offers decreased disclosure quality and lower tax reserves.

3. Theories of Tax Disclosure

There are a few theories, which discuss tax disclosure as a whole. Individual aspects of disclosure are examined in theories like political cost theory, signaling theory, and legitimacy theory. There are many reasons why companies provide or disclose differing levels of information, which are discussed below.

3.1 Political Costs Theory

Political costs "are costs that groups external to the company might be able to impose on the company as a result of political actions" (Watts & Zimmerman, 1978, p. 115). For instance, if a company accounts high returns, this might be utilized as a justification for lobby groups or trade unions to take action for an increased share of that return in the form of higher wages. Therefore, companies may use returns-reducing accounting methods (Watts & Zimmerman, 1990). Furthermore, Deegan and Hallam (1991) gave another instance that may sustain political costs such as environmental factors like "carbon footprints". Disclosure made by a corporate in relative to their negative or positive influence on their physical environment might in addition be a technique to decrease any political costs. Political cost theory consequently can also make clear why many companies implement voluntary environmental and social disclosures in their yearly reports. Moreover, the political cost theory explains why other parties who want more information about the firm's tax policies and ask for increased levels of disclosure lead companies to adopt tax disclosure (Deegan & Hallam, 1991). Changes in accounting procedures are not costless to firms (Watts & Zimmerman, 1978). Accounting standard changes, which either raise disclosure or require corporations to change accounting methods, raise the firms’ book-keeping costs (including any necessary raises in cost in relation to disclosing information about taxes).

The political sector has the authority to affect wealth transfers between numerous groups. Tax law is one factor affecting management wealth, but is not directly tied to financial accounting standards, with the exception of a few cases (e.g., the last-in-first-out). If management expects a suggested financial accounting process to impact future tax regulations, their lobbying behaviour is affected by the future tax regulation effects (Moonitz, 1974).

Deegan and Hallam (1991) adopted a political cost perspective to voluntarily disclose value added statements in the yearly reports. Particularly, they hypothesized that value added statement disclosure is associated to labour intensity, company tax payments, rate of return, industry volatility, and company size. The study found that size (market concentration and absolute after tax profits), tax, and the industry to which a company belongs were all associated to the happening of value added statement disclosure.

Political cost theory can assist in explaining the decisions of voluntary reporting (e.g. Leftwich, Watts, & Zimmerman, 1981). Considerations of political costs, such as taxes and regulation, and the determinants that affect the welfare of management assistance are to better understand the origin of the pressures that drive the development of accounting standards (Watts & Zimmerman, 1978). The costs of contracting include agency, transaction, information, renegotiation, and bankruptcy costs, which are all crucial for the selection of accounting models (Watts & Zimmerman, 1990).

In contrast, managers have incentives to make a voluntary disclosure when the advantages outweigh the indirect and direct costs involved. Both mandatory and voluntary disclosures are to reduce the information asymmetry between informed and uninformed market participants, and between the taxpayer and the IRS. Such information helps correct any errors of evaluation of the firm. As a result, they help to reduce the cost of capital for the firm Botosan and Plumlee (2002), raise the demand of investors, reduce the bid-ask spread, and increase institutional interest and analytical following (Diamond & Verrecchia, 1991; Li, Richardson, & Thornton, 1997). Sengupta (1998) indicated that the benefits of the cost of capital resulting from the disclosure of the quality of the cost of capital also extend to include the cost of debt capital.

In summary, according to political cost theory, companies that are subject to high political costs (which highly relies on the size of the firm) are probably to supply and disclose further information about tax (Watts & Zimmerman, 1978). The political cost hypothesis states that large corporations, rather than small companies, are more likely to utilize accounting choices that decrease declared profits (Watts & Zimmerman, 1990).
3.2 Signalling Theory

In markets with information asymmetry, signalling theory states corporations issue "signals" about who they are and "what they believe" (Spence, 1973, p. 355). Spence (1974) defines market signals as altering the belief of, or conveying information to, other groups in the marketplace regarding some unobserved activity. Signaling information, therefore, is essential to decrease agency costs and information asymmetry between firms and the market.

From another side, companies’ disclosures of information, including information about tax, falls somewhere between no disclosure and full disclosure, depending on their motivations (Premuroso, 2008). These motivations differ and have different effects on the level of disclosure between companies, and from one country to another. This is based on numerous factors, such as regulations, tax law, and political cost. All companies, at least partially, disclose information about their business prospects in order to signal whether they have or do not have good investment opportunities (Bhattacharya & Ritter, 1980).

Another possibility of using signaling theory is that managers may desire to decrease information asymmetry existing in the market regarding the company's performance. For instance, disclosures may serve as "signals" if they reflect information about unobservable attributes of a company's decision (Morris, 1989). In such a scenario, managers of higher quality firms with private information can distinguish themselves from lower quality companies via disclosures. In this context, managers can use tax disclosure to send signals to related parties that need information about tax in order to help them in their decisions. At the same time, managers of an underperforming firm may signal that the firm is taking steps to improve performance by disclosing a decision related to outsourcing. The finance literature tests company information disclosures using signaling theory in numerous ways. Ross (1977) contended that when managers possess inside information, the financial structure of the corporation (i.e. the amount of debt) signals information to the market. In another study, cash dividends functioned as a positive signal by the manager of expected cash flows when investors had imperfect information about companies’ profitability (Bhattacharya, 1979). Recent research also applied signaling theory to undervalued companies announcing stock repurchases to separate themselves from overvalued corporations (Utpal & Dittmar, 2003). In such scenarios, it is clear to see how companies can send signals under signaling theory to the users of information or financial statements. In the same context, tax information can be sent as signals to IRS or users through tax disclosure.

In the case of asymmetric information, Akerlof (1970) who referred to the theory, suggested that firms with superior performance (good firms) utilize financial information (including tax information) to send signals to the market, users, and IRS. Therefore, managers can be motivated to provide or disclose specific information on a voluntary basis. This is because they are expected to supply (and to be interpreted as) a good indication of the performance of their companies in the market, and how to decrease the asymmetry of information.

3.3 Legitimacy Theory

“Legitimacy is a generalized perception or assumption that the actions of an entity are desirable, proper, or appropriate within some socially constructed system of norms, values, beliefs, and definitions” (Suchman, 1995, p. 574). A significant issue to be recognized is that there are, in fact, already two major categories of legitimacy theory. These are graphically reported in Figure 1. The “macro-theory” of legitimating, acknowledged as institutional legitimacy theory, deals with how organizational structures in their entirety (government for instance, or capitalism) have gained approval from society. “Within this tradition, legitimacy and institutionalization are virtually synonymous. Both phenomena empower organizations primarily by making them seem meaningful and natural” (Suchman, 1995, p. 576).
This suggests that organizations constantly strive to ensure that they operate within the limits and rules of their respective societies. It is based on the idea that there is a social agreement between the company and the community, forcing the firm to voluntarily submit and disclose information on activities perceived as certain activities of the society (Guthrie, Petty, Yongvanich, & Ricceri, 2004). From the viewpoint of legitimacy theory, information disclosure is used as a tool for companies to show that they operate according to the values of the society and are socially responsible, as well as providing a picture to get or maintain social legitimacy (Patten, 1991, 2002). According to Guthrie et al. (2004) the theory of legitimacy is closely linked to disclosure of intellectual capital. Companies are more likely to report and disclose their assets as intangible if they have a specific need to do this and cannot legalize their status through "hard" assets that are recognized as a symbol of success in traditional companies (Guthrie et al., 2004).

Furthermore, from the stakeholder tactic of analysis perspective, legitimacy theory is the interpretative lens of number of performance studies and environmental reporting that are disclosed by the companies. Legitimacy theory is utilized as an interpretation for company responses to intimidations to its legitimacy Vis-a-Vis the social agreement. Voluntary disclosures, fundamentally in yearly reports, are a communication mechanism by companies attempting to satisfy outer pressures to conform to socially satisfactory rules, substituting this communication technique for any substantive behavioural performance (Mobus, 2005).

In summary, in view of previous literature of the related theories about tax disclosure, it can be concluded that political cost theory, signaling theory, and legitimacy theory are the theories that examine the relationship of tax disclosure and society. Political cost theory indicates the costs companies incur when they disclose information about their tax. Moreover, political cost theory also makes it easy to see why many companies approve voluntary environmental and social disclosures in their yearly reports (Deegan & Hallam, 1991). In contrast, signaling theory explains how firms can send signals to end users, shareholders, practitioners, and stakeholders, in the form of information in financial statements. Additionally, tax information can be sent as signals to IRS or any other parties requiring this information through tax disclosure (Utpal & Dittmar, 2003). Finally, theory of legitimacy is closely linked with the disclosure of intellectual capital. Consequently, companies are likely to report and disclose their assets as intangible if they have a specific need for this kind of disclosure (Guthrie et al., 2004).

4. Constraints and Objectives of Tax Disclosure

4.1 Tax Disclosure Objectives

The immediate aim of tax disclosure is to broaden general knowledge regarding the universal incomes obtained by the multinational companies (Brauner & Stewart, 2013). However, the ultimate goal is to stimulate popular movements of the tax reform as communities interact with the knowledge acquired. Activists aim to report as an experimental fact a universal financial settlement that systemically lets multinationals companies to escape taxation in roads that are expected and foreseeable, if not intentionally planned by lawmakers. Murphy (2011) in Country-by-Country Reporting (C-B-C-R) found that activists discovered that corruption and non-compliance by companies and the government is an advantage of this universal settlement, but this is not their merely, or even
elementary, concern. Alternatively, they attempted to reveal the lawful and institutional framework that permits multinational companies to avoid taxation in full acquiescence with all viable tax regulations. This is an extension of a large follow-up of the objectives of transparency beneath the ‘Publish What You Pay’ (PWYP) scheme. The purpose is to disclose cooperation between companies and governments that encourage corruption and non-compliance with tax legislations. Beneath C-B-C-R, the purpose is to disclose cooperation between companies and governments that promote under taxation of multinationals companies as an issue of systemic design (Christians, 2013).

Proponents of transparency propose that several constituencies want to utilize the data collected throughout more inclusive requirements of tax disclosure to do best-informed market decisions (Christians, 2013). The primary intended audience for this tax translucence is investors, who would superficially have further data to invest in unsteady system of government, tax shelters, and other sensible regions (Murphy, 2011). In the U.S., giving shareholders admission to company tax information and making corporate tax returns public were features of early current company returns tax, which was quickly passed under pressure from the business lobbyists (Note 2) (Christians, 2013; Pomp, 1993).

4.2 Constraints of Tax Disclosure

Blank (2011) argued that boosted disclosed information about tax would give tax payers with both an inspiration and a road map to decrease their personal tax, whilst hindering the capacity of governments to preserve a picture of the tax scheme and providing a balanced tool for the rule of regulation. Furthermore, those in favour of more tax transparency (disclosure) argued that the disclosure of tax increases has little effect on compliance (Kornhauser, 2005; Mazza, 2003). An experience with better detection may supply a resource of information for needful analysis, however the modern overt discourse through tax transparency proposes that the dearth of empirical evidence will not obstruct powerful support on either aspect (Christians, 2013).

According to the U.S. Treasury Department Secretary the SEC does not advantage from access to the company tax revenues as much information it yields is unrelated to the SEC. Neither would it be in the interest of the public to expose the proceeds of the tax on public companies, because the complexity would lead to confusion, with companies and individuals making "misinformed, inexpert analysis" (Lenter et al., 2003, p. 806). Likewise, the Treasury Department Secretary answered to the chairman of the Senate-Finance-Committee that there is a probable huge damage to both companies and government tax management if organizations’ tax portions or returns therefrom are made openly accessible (Lenter et al., 2003). However, different alternatives may enhance tax and financial statements: the Schedule M-1, which is filled with companies’ tax income, accounting income and reconciled tax, could be enhanced, the disclosure of tax information in financial reporting might be modified, and a number of the variations between tax accounting and book might be eliminated (Lenter et al., 2003).

Lenter et al. (2003) argued that making firms’ tax returns publicly infringes the established rules of confidentiality that would produce misinformation and confusion about a company’s activities. Both of these issues are addressed below, along with a discussion of three other possible interceptions to the disclosure: one lawful, one depends on the fears of the government power, and one possibly unintended result.

4.2.1 Disclosure of Tax Information Violation Confidentiality

Public tax disclosure would break a key feature of the tax regulations: confidential tax information. Based on this view, a breach of privacy would be unwise for two causes. The initial reason that is linked to respect for compliance other than privacy is that the disclosure will lead firms to say less and thus pay less. The Tax Executives Institute (TEI) made this argument in its submission to the Treasury and the SEC, turning topsy-turvy the argument for disclosure on the basis of incremented acquiescence. It documented, that the field of data needed by the Internal-Revenue-Code is at once daunting and unusually delicate, and that the ability of tax-payers to reveal private data is reinforced by affirmations that their confidentiality benefits will be protected by the government (Note 3) (Lenter et al., 2003, p. 822). If a firm’s tax manager knows that the data they involve in the firm’s tax income will be publicly, the managers may withhold sensitive information. The tax liabilities of the company will then reduce, either directly through a simple understatement of tax returns or indirect as a consequence of the inability to accurately assess the IRS tax liability because of a lack of the required necessary information (Traubenberg, 2010).

Other evidence is that the public disclosure of tax data would detect the valuable and contrary confidential business data to competing companies. In its statements to the Treasury and the SEC, the Tax Executives Institute (2002) showed instances of business items that are desired to be detected on tax income, and stated that, the items would provide a great advantage to competitors of the company. These items contain the sources, character, and nature of a firm's expenses and revenues, details about the firm's lawful structure, advertising,
licensing, sales, other selling expenses, leasing revenues by jurisdiction and lawful entity, and the environment and position of the firm's industrialization expenses by functional kind. If the information revealed is global, it might put a competitive benefit to those companies that have moderately significant proprietary data. Moreover, if the detection is not global, it could suggest a benefit to those firms that are not subject to the demands of disclosure. Generally, it would decrease the motivation to invest in acts whose return relies in part on their nature of the proprietary data (Lenter et al., 2003).

4.2.2 Tax Disclosure Could Create Confusion

Public disclosure of a firm's tax information as well alleged that those revenues are lengthy and complicated and, if disclosed, could cause confusion about a company's activities, tax practices and accounting. According to, Tax Executives Institute (2002) considering the level and scope of variances in tax and financial accounting necessities, overt disclosure of organizations’ tax income poses extraordinary probable for befuddling rather than enlightening investors. In his response to the chairman of the Senate Finance Committee, the Treasury Department Secretary affirmed that they have genuine worries that overt disclosure of a big company’s income would result in major embarrassment amongst the public and would render the companies to misguided, unskilled analysis of their operating and finances exercises. Such “misanalysis” and perplexity can prompt unsubstantiated loss of confidence in the company, which might importantly (and improperly) harm that corporation's remaining amongst investors (Lenter et al., 2003, p. 824).

4.2.3 Information to Government

According to Lenter et al. (2003), another argument against the disclosure of a company’s tax information—not to the overt in general, however, the SEC and different agencies that making income accessible to government authorities outer the IRS will provide a previously influential federal bureaucracy an over the top measure of information to utilize versus tax-payers. The issue with this plea is that the additional data is presumably not significant. As described in the connection of business privacy, worries about confidentiality and government intervention have conventionally been raised against the disclosure of information about individual, not company’s data. This concentrate was surely the case in 1934. The confidentiality issues and worries raised by the disclosure of tax information when the individual becomes less resonant disclosure by companies are at issue (Lenter et al., 2003).

4.2.4 Unintended Behavioural Responses to Disclosure

Disclosure of a company’s tax increases the expense of performing business in a type that is liable to disclosure. For instance, disclosure is limited to corporations that are liable to SEC administrative supervision, that is, firms that are exchanged on open trades. Because no firms are traded on an open market presently disclose their tax income or important tax income data, it presumes that directors accept that the expenses of such disclosure surpass the advantages. If disclosure was mandated for public firms, several of them would choose to leave from the public capital markets, instead of disclose their tax data through tax disclosure. Such behaviour could subsequently increase the expense of acquiring capital (Lenter et al., 2003; Securities Commission Malaysia, 2007, 2012).

Likewise, if disclosure was restricted to tax income for companies (private and public), this could lead to reformation and liquidation of organizations as co-partnership or other inflow, that is, bodies that would not be liable to disclosure. Similarly, if disclosure was authorized for whole U.S. companies, the expense of being in the U.S. would raise compared with other nations. This raise could give a competitive benefit to outside firms and as a consequence firms would migrate out of the U.S. In brief, it is unattainable to authorize an entire tax income disclosure for all firms in the globe. Whether disclosure is expensive or not, a number of firms will react to disclosure by working on presumably and alternative suboptimal structures in respect to evade the requirement of disclosure (Lenter et al., 2003).

4.2.5 Potential Obstacles among Tax Disclosure Costs

Christians (2013) argued, however, that the requests of the market for information increases the likelihood that the flow of information may have unintended results on the behaviour of market entrants. In a short historical experience with the U.S. firm tax disclosure, the opponents of companies tax disclosure debated that publishing a company's tax income failed to raise income, supported tax evasion (Ratner, 1980), and served to provide business competitors something of worth at the expense of the tax-payer.

5. Benefits of Tax Disclosure

Disclosures require companies to disclose greater tax-related detail. As known in the majority of countries, companies' tax disclosure regulation does not supply policymakers and other users with enough information to
inform and motivate tax reform (FAST FACTS, 2007). When asking firms to disclose information regarding tax in details, there is a very important question that has been raised: why should a company’s tax income (or tax information) be disclosed? What are the motivations behind that? Public disclosure of a company’s tax income information will motivate and aid government regulators. Tax disclosures also motivate and develop the functioning of the financial markets. Tax disclosure motivates and promotes tax compliance and leads to and aids increased political pressure for better tax policy (FAST FACTS, 2007).

Lenter et al. (2003) argued that high transparency of tax could have numerous helpful effects. First, tax disclosure can put pressure on regulators to develop the tax system. Second, tax disclosure may force companies to resist effective strategies to reduce tax planning. For example, if they fear that the disclosure of payments of lower tax would lead to negative reactions from the consumer’s response (where it causes the negative reaction of investors) responses are less clear, such as increasing transparency and stimulating the race to the bottom of the lower tax-liability. Third, it can contribute to improving the performance of financial markets, which highlights on the information contained in financial reports. Finally, disclosing information about tax in the financial reports of companies is more useful and beneficial to help investors understand the tax situation of the company and will provide public access to tax returns (Lenter et al., 2003).

5.1 Measuring Companies’ Tax Loopholes

One advantage of tax disclosure is that companies can illustrate the tax loopholes that permit very profitable companies to evade taxes. Two mainly problematic loopholes have been newly identified at the state level and can be addressed through a policy disclosure of information, which is good. The first one is the “Toys R Us-style loophole,” in which companies go from multi-state taxable income in high tax states to “passive income” and branches in countries with low or no taxes on corporate income. Therefore, Toys R Us was fundamentally moving income from non-taxing states to a taxing state. One way to disclose this loophole is to require companies tax disclosure of royalty payments to subsidiaries and interest (FAST FACTS, 2007).

According to FAST FACTS (2007), multistate companies occasionally take benefit of tax state “nexus rules,” which set the standard as a "physical presence" of the company—there must be a state responsible for charges for a sales office in the region. One way to expose this gap or loophole is for companies who believe they have duties, in a particular case, to disclose why they should not be taxed on revenues from sales in the state.

Tax disclosure helps companies by levelling the playing field. Generally, the comprehensive results of tax disclosure lead to a fairer tax system and more equitable tax that would improve the business environment anywhere by attracting many companies to countries with tax transparent and more tax disclosure. Because these policies tend to lead to the inspiration of the tax burden more equitably across companies, they offer the best disclosure and reveal information to new entrants and, more importantly, help to bridge loopholes that lead to these tax benefits. In addition, corporate tax disclosure leads to the public gaining more confidence in the company. Disclosure inevitably reveals that many of the companies pay their fair share of taxes, with a focus on good corporate citizenship (FAST FACTS, 2007).

5.2 Tax Disclosure Motivate and Aid Government Regulators

One argument of the rationales for making a company’s tax income publicly disclosed is to develop government legislation of companies. In this regard, making firm tax returns accessible to the SEC would aid government efforts to control corporate governance and to make sure that firms file the right financial statements. Two ideas support this contention. The first key idea is that companies need to be well controlled. Even though there is disagreement about how better to answer to the numerous current instances of organization wrongdoing, it is difficult to contradict that at some rank corporate governance performed weakly in several cases. The next key idea is that the information currently accessible to government legislator—both those officials occupied in administering the tax regulations and officials at the SEC—is ineligible, and companies’ tax income might act as a helpful instrument to government regulators in their efforts to regulate firms (Lenter et al., 2003).

5.3 Develop Financial Markets Functioning

The disclosing of companies’ tax return information would assist financial markets function further effectively by developing financial statements quality. This logic is, in a sense, a generalisation of the argument that it shall help the SEC in its goal of defending investors by regulating the impartiality of the market securities. Debatably, public detection of tax revenues levied on companies could aid the financial markets, even if it does not help the SEC (Kleinbard & Canellos, 2002; Lenter et al., 2003).
5.4 Tax Disclosure Motivate and Promote Tax Compliance

Disclosure of companies’ information about income tax return decreases aggressive tax avoidance and outright evasion for two reasons (Lenter et al., 2003). Firstly, if company officials are worried that a firm’s taxable returns were revealed to be doubtfully low, the finding could produce an unfavourable public reply. Several firm officials might feel ashamed for being the officers of the firms exposed to be lesser than good companies' citizens. Further significantly, they fear an opposite influence on the firm's bottom-line since their business depends on their clients’ confidence that they are good public citizens (Lenter et al., 2003).

The second reason, albeit less direct, is that the disclosure of information about corporate tax encourages increased compliance. Tax disclosure facilitates the reconciliation of the main differences between tax and book, either because the company itself provides these reconciliations or since reconciliations are computed by relevant parties, like the business journalism and academics. These reconciliations could help the IRS in discovering a company’s tax evasion. Accordingly, firms may be further irresolute to involve in aggressive tax planning (Lenter et al., 2003). For example, one may book an expanded tax reconciliation and shed light on the tax shelter transactions. In the context of the current policy, the process may not have been disclosed separately in the note of the tax balances (in a financial statement), as detailed in the Schedule M-1 or not (Lenter et al., 2003).

5.5 Tax Disclosure Increases Political Pressure for Good Tax Policy

The public tax disclosure of a company’s income tax returns will help raise political pressure for better tax approach and policy. Hanlon (2003) discussed that the information provided in the financial reports is not in general enough to pinpoint the company’s payments or yearly tax liability. Disclosure would guarantee that a demonstrable and, to a certain degree, comparable number is in the public area. If a firm thinks that the disclosed number is misguiding with regards to its right tax status, it would have the chance of releasing additional descriptive information (Lenter et al., 2003).

If this increases the responsiveness to change the general impression that the tax system is reasonable, there may be at least two possible advantages. Firstly, in a democracy, respect for regulations and management is good in and of itself, and depends on the legitimacy of the government in this respect. Secondly, it may be the public perception of justice that would raise voluntary compliance with tax legislations. Certainly, these arguments can be reversed if disclosure reduces public dependability on the fairness of the tax system or the perception that it safeguarded tax-payers' confidentiality (Lenter et al., 2003).

5.6 Motives for Managers to Manipulate Reserves and Disclosures

To reconcile the interests of managers with shareholders, managers get the equity incentives in the firm; this provides an incentive to reduce the cash outflows of tax (Fama & Jensen, 1983; Jensen & Meckling, 1976). FIN 48 restricted the efficiency of tax planning to the use of what has been disclosed and amounts reserved by the tax authorities. Blouin et al (2010) argued that if the managers of the companies think that the IRS will utilize the number of disclosed tax reserves, as above mentioned, as one of the several references for aggressive tax, they will favour to disclose lesser tax reserves. Poor disclosure shows that the managers are scared regarding how the IRS will be using their FIN 48 disclosures, that is, the amount of tax reserves. Consequently, companies with poor disclosure are encouraged to report lesser reserves. Several managers may have other motivations that are most significant to defend the positions of tax. For instance, they could preserve reserves as financial “cookie jars” to meet the covenants and debt, rewards, and thresholds or profit goals (Watts & Zimmerman, 1990).

5.7 Potential Advantages of Poor Disclosure Managers

Managers will prefer to be less transparent in their disclosures since they think that these disclosures or statements could be utilized to undermine or weaken their status of tax and the expenditure of disclosure will outbalances the advantages. Robinson and Schmidt (2013) found that the market sets the value as less than the tax reserves of the companies with a high-goodness disclosure, which indicates that investors believe that poor disclosure assists managers to safeguard the tax centres. Hence, Gross (2011) expected that companies with poor disclosure of the information will pay less tax in their future cash flow.

5.8 Potential Benefits of Excess Disclosure Managers

Company managers with administrative capacity and a large tax reserve will have a motivation to supply disclosure if it gives truthfulness to their budgets and makes the company looks less aggressive. In accordance with Verrecchia (1983), companies decide to disclose if not the expense of disclosure outweighs the advantages. Proprietary costs contain any cost that decreases the current amount of cash flows. Li, Richardson, and Thornton (1997) applied proprietary cost theory to environmental disclosures showing Verrecchia’s (1983) partial
equilibrium holds for the expenditure of government investigations. Thus, managers must supply further disclosure of information if they believe the costs outweigh the advantages. Moreover, it is expected that managers provide additional disclosure of information to promote attitudes of the tax or limit the scope of tax audits (Gross, 2011).

6. Measurements of Tax Disclosure

Tax disclosure measurements are rarely tested by previous studies. The measurement should vary greatly depending on how data can be measured, the availability of data, and the interest of researchers in the general or specific approach to tax disclosure. Indices of disclosure are wide lists of certain disclosure items which are properly measured (depended on the objective criteria of usefulness in achieving the objectives of the user group) to measure the extent of disclosure (Marston & Shrives, 1991). As a self-constructed measure, the main obstacle is the subjective judgment engaged in the substructure of the index. Additionally Singhvi and Desai (1971) argued that difficulty happens in reproducing the analysis and making comparisons. Tax disclosure can be measured using an index of tax disclosure; empirical research on disclosure has been used as a tool to assess the quality and extent of information disclosed by companies, of both a voluntary and mandatory nature (Portela de Lima Rodrigues, Oliveira, & Craig, 2005).

In the U.S. the Statement of Financial Accounting Standards (SFAS) 109 discussed that the following disclosure items must appear in a company’s yearly financial reports: (i) the returns tax synopsis, which details the important components of returns tax expenditure, (ii) the rate reconciliation, reconciling presented returns tax cost with the amount that would come from applying the local federal statutory rate to pre-tax returns, and (iii) the schedule of deferred tax status, which supplies information regarding DTLs and DTAs (FASB, 1992). These three essential disclosures are in general reported in a tabular form. Companies in addition are predicted to disclose data about the amount and expiry dates of credit carry-forwards and loss, the division of tax expenditure between all other items and continuing operations, the composition of earnings before income taxes (total, local, and foreign), and temporary differences for which the company has not registered a deferred tax liability, counting permanently reinvested foreign earnings. In many cases, these additional disclosures are supplied in the text format (IRS, 2012).

In addition, FIN 48 introduced instructions for measurement, the recognition, and required disclosures of doubtful tax advantages in financial statements. The FASB aims for measurement and the recognition of unrecognized tax advantages beneath FIN 48 to decrease variety in practice, and for the disclosure requirements to give more information about tax uncertainty (Robinson & Schmidt, 2013). The aim of FIN 48 is to provide consistent guidance for the recognition of these unknown tax advantages in financial reports when any likely tax disputes remain unresolved. According to introduced the guidelines of FIN 48, constituents anticipate that the FIN 48 disclosures would entail some of items in the financial statement.

Similarly, Koester (2011) argued that FIN 48 supplies recognition threshold and measurement attributes for financial report measurement and recognition of the status of the taxes. Recognition threshold requires that it is further probably than-not that a tax status will continue upon audit. The threshold depends only on the technical advantages, assuming the position of the authority of taxation has all the related data, and ignoring the possibility of the audit. Characteristic of measurement is the biggest number of advantage that has a probability of more than 50 per cent likelihood of being recognized upon settlement. The resulting unrealized tax advantage is registered as a conditional liability. FIN 48 applies merely doubtful tax status and does not modify to another 109 SFAS deferred tax accounting and the utilize of the evaluation allowance account for deferred tax assets.

7. Conclusions

This paper discussed some studies and conclusions with a summarised overview of the associated literature related to tax disclosure in order to verify the gaps in the current body of knowledge. Obviously, tax disclosure is relatively a new area of corporate reporting research, and there is a limitation in previous literature this one of the big difficulties in researching this topic. In summary, by definition, offering disclosure implies that some data that is presently confidential becomes public. However, it is believed that there is no constitutional obstruction to forging the confidentiality of this data, and hence the case should be made on base of whether or not there are substantial advantages. This case has been found to be compulsory and we can look forward to the following step of bearing in mind the most excellent position of tax disclosure and its implementation details (Lenter et al., 2003). The movement of tax transparency seems to prove the basis, as other initiatives to reform tax policies do not have that compression on the system and should be used from the outside. It is indicated that the movement currently engages individuals and the leaders in the management of fiscal policy could not be relied upon to focus on the distribution of tax burdens in an appropriate manner with wider social values. It remains to be seen
whether the awakening public attention to international tax planning will lead to enough attention to the imposition of a political shift.

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the impact of tri data availability. *Accounting Forum*, 26(2), 152-171. http://dx.doi.org/10.1111/1467-6303.t01-1-00007


Notes
Note 1. Prof Pomp from University of Connecticut School of Law.
Note 2. This is according to “44 Congress Rec. 4000 (1909) (Senate debate in the Payne-Aldrich Tariff Act of 1909, the predecessor of the current U.S. corporate income tax system); Pomp supra note 5 at 387-388 (discussing the efforts of the Illinois Manufacturing Association to prevent company tax disclosure)”.

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