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Strategic disclosure for political gain: The case of the corporate alternative minimum tax[†]

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We examine the disclosure choices of firms subject to the Corporate Alternative Minimum Tax of the Tax Reform Act of 1986 (AMT). We find systematic differences in disclosure choices by firms subject to the AMT consistent with their attempting to influence perceptions of the effectiveness of the AMT. We believe these findings support the inference that firms will differentially respond to increased tax disclosures under Financial Interpretation 48 (FIN 48) that will require firms adopting uncertain tax positions to provide extensive disclosures for fiscal years beginning after 12/15/06.

Keywords: Tax, political gain, corporate alternative

INTRODUCTION

At a time when increased disclosure of corporate tax return information has been proposed as a mechanism to achieve greater transparency, it is important to evaluate how effective both voluntary and non-voluntary disclosure of corporations' tax attributes have been in the past. Increasing book tax differences, coupled with concerns about corporate tax compliance generally, prompted recent hearing by the Senate Finance Committee which

the SECs reporting requirements to alter their accounting for, and provide extensive footnote disclosures of uncertain tax positions (see Financial Standards Accounting Board, 2006).

With limited exceptions (Dworin, 1985; Mills et al., 2003; Plesko, 2000, 2003, 2007)) little is known regarding fac-

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included a discussion on the merits of requiring the disclosure of corporations' tax return information to improve the public's knowledge of firms tax position (Grassley, 2006). Similarly, concerns over the adequacy of tax contingencies have led to the issuance by the Financial Accounting Standards Board of Financial Interpretation Number 48 (FIN 48). Fin 48 will require firms subject to

tors that might cause or be associated with differences between actual and disclosed tax status. Nevertheless, much empirical tax research assumes transparent and complete self-disclosure of tax status. To the extent that this assumption of transparent and complete self-disclosure is invalid, inferences drawn from this literature may be misleading. In particular, disclosure choices related to firm specific characteristics may lead to confounded interpretations of the motivations for disclosure choices due to problems related to correlated

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omitted variables.

In this study, we examine the disclosure choices of firms subject to the Alternative Minimum Tax (AMT). One design element of this study that distinguishes it from other disclosure studies is that we are able to observe firm disclosure for financial reporting purposes as well as disclosure for tax purposes. A second design element that distinguishes this study from other disclosure studies is that we can partition sample firms using a “bright line” rule intended to compel disclosure that allows us to effectively separate firms between those that have to disclose specific information (though many do not) from those that voluntarily choose to disclose information (though many do not).

We partition our sample of firms between those that have to disclose their AMT status and those that do not have to disclose their AMT status using a “bright line” reporting rule. For firms in each group, we identify whether or not the firm actually disclosed its AMT status. For firms in each group (have to disclose and do or do not have to disclose and do or do not) we identify whether factors that proxy for costs and benefits of disclosure are significantly related to the disclosure/non-disclosure choice.

For firms that have to disclose, two factors are significantly related to the disclosure choice: NOL status and industry membership. We interpret the higher likelihood of disclosure by firms with NOLs as consistent with these firms “making the case” that they are unduly burdened by the AMT. With respect to industry membership, we interpret the higher likelihood of firm disclosure as a function of firm industry membership as consistent with the proposition that, when a large number of firms within an industry are subject to the AMT, disclosure of AMT status does not entail material incremental costs to the disclosing firm.

For firms that do not have to disclose AMT status, three factors are significantly related to the disclosure choice: the relative significance of the AMT burden, level of pretax income, and, again, NOL status. We interpret the greater likelihood of disclosure of AMT status by those firms with relatively higher AMT burdens as consistent with those firms attempting to gain positive political leverage in an effort to change the AMT. We interpret the lower likelihood of disclosure by firms with high reported incomes as consistent with these firms not volunteering information on the effectiveness of the AMT in increasing their tax burdens. Lastly, we interpret the greater likelihood of disclosure by firms with NOLs as an attempt by these firms to curry political favor, as we did for firms that had to disclose. We draw two major conclusions from this study. First, there are significant and nonrandom, factors that influence the disclosure choice. This finding is consistent with the view that those firms that disclose their AMT status are not representative of the population of firms subject to the AMT. Because the choice to dis-

close is related to specific factors that differ cross-sectionally across firms subject to the AMT, conclusions regarding the disclosure patterns of AMT firms' behavior based upon firms which self-disclose AMT liability should be made cautiously.

Second, our results provide insight into the role of the political process with respect to accounting disclosure. Previous analyses of political effects have focused on the role political considerations play in influencing earnings, with size hypothesized as being positively related to accounting choices that reduce reported earnings.² We consider the political implications of disclosing a given set of information. The results we report indicate that disclosure choices were made in a manner consistent with providing support for desired changes in the law or avoiding negative scrutiny. The voluntary disclosure of firms with high percentages of AMT to regular tax and the voluntary and mandatory disclosure of firms with NOLs appears consistent with an attempt to influence the legislative process to alter the AMT. Conversely, after controlling for other explanatory factors, voluntary disclosure by more profitable firms was less likely than for firms with less income. This pattern of disclosure is consistent with profitable firms attempting to suppress information that the AMT was effective in increasing their tax burden. Such information would have potentially been useful in blunting calls for repeal or alteration of the AMT statute.

In the next section we provide a brief description of the AMT. In section III we review the completeness of financial statement disclosure of AMT status. In section IV we describe sample identification procedures. In section V we describe the model we estimate and discuss our analysis of the results. The final section provides a brief summary.

A brief history of the AMT

The Tax Reform Act of 1986 (TRA86) created a corporate AMT that, for the first time, included financial statement income as a component of taxable income.

The primary rationale for including financial statement income as a component of the AMT was to reduce the number of instances in which firms reporting significant positive financial statement income avoided payment of significant explicit tax. For example, the Senate Finance Committee report from May 1986 that, in part, led to the

²An overview of the way accounting choices might be affected by the political process can be found in Watts and Zimmerman (1986), chapters 10 and 11.

final Tax Reform Act of 1986, stated that the committee found it "unjustifiable for some companies to report large earnings and...yet pay little or no taxes..." This book income adjustment provision motivated a number of earnings management studies that examined its effect on financial statement income (Boynton et al., 1992; Manzon, 1992; Wang, 1994; Choi et al., 2001). Book income was replaced by the adjusted current earnings adjustment for taxable years after 1989.

The corporate AMT parallels the regular corporate tax. Alternative Minimum Taxable Income (AMTI) begins with regular taxable income before Net Operating Losses (NOLs). The corporate AMT parallels the regular corporate tax. Alternative Minimum Taxable Income (AMTI) begins with regular taxable income before (NOLs). Taxpayers then Taxpayers then add back amounts to adjust for differences in accounting methods used for regular tax purposes and the AMT (e.g., less accelerated depreciation may be allowed under the AMT). In addition, various tax preferences are added to AMTI, such as percentage depletion in excess of original cost. The sum of regular taxable income before NOLs and these adjustments and preferences is AMTI before the book income adjustment.

Book income for the AMT was defined as the pretax book income of the consolidated financial entity associated with the consolidated tax entity. However, AMTI before the book income Book income for the AMT was defined as the pretax book income of the consolidated financial entity associated with the consolidated tax entity. However, AMTI before the book income adjustment would generally differ from pretax book income for financial purposes. The reasons for these differences, which can be economically large, may be as simple as differences in depreciation under each system or differences in consolidation between financial and tax reporting.³

For the years 1987 - 1989, one-half of the excess of book over taxable income (if positive) was included in the calculation of AMTI. AMTI in excess of a (phased-out) \$40,000 exemption was taxed at a 20% rate,⁴ compared to 40% under the regular tax in 1987 and 34% thereafter. The use of NOLs and foreign tax credits could offset up to 90% of the AMT, greatly reducing the amount of additional tax that a firm might pay. Firms are required to pay

the greater of the regular tax or the AMT. If a firm is required to pay the AMT, timing differences (such as depreciation or the book income preference) generate a credit that can be carried forward to offset future regular tax liability. Permanent differences, such as tax-exempt interest, generate no AMT credit.

Gill and Treubert (1993) report that 17,370 firms paid the AMT in 1987, rising to 25,237 in 1989⁵ with manufacturing firms responsible for the largest share of AMT payments. In 1987 direct additional tax payments attributable to the AMT were \$2.2 billion out of approximately \$87.0 billion in corporate tax liability and \$9.1 billion for the period 1987 - 1989.⁶

Table 1 provides a distribution of returns with an AMT liability by asset size. It is evident from the data reported in this table that the incidence of the AMT is higher for larger firms, with approximately one in five firms with assets greater than \$50 million dollars paying the AMT in each of the three years examined in this study. Gerardi et al. (1993) analyzed a panel of 10,000 large-corporation tax returns (assets in excess of \$50 million) and found these firms paid 73% of the total AMT liability for all firms from 1987 - 1990, compared to 64% of the regular tax liability. Nearly one-half of all corporations in their sample paid the AMT in at least one year. Of those firms paying the AMT, the AMT increased total taxes paid more than 30% for firms on the AMT one or two years, and more than doubled taxes paid for the 11% of firms on the AMT for three or four years.⁷

If being subject to the AMT exposes a firm to additional economic costs, firms will find it disadvantageous to reveal their AMT payment to either competitors or to financial markets. Dworin (1987a, 1987b) suggested the AMT may reduce firms' leverage, investment and growth rates. Lyon (1990) has shown the AMT will increase firms' cost of capital, depending upon the length of time they pay the AMT and that debt is relatively more expensive for AMT firms.

AMT disclosure

Because of the negative economic consequences to firms

³Dworin (1985) provides a detailed examination of accounting differences using tax return information. Plesko (2002) provides tabulations of the components of differences based on firms' reconciliations on Schedule M1 of the tax return.

⁴In addition, the Environmental Tax (0.12 percent) is levied on AMTI before NOLs in excess of \$2,000,000.

⁵While more than 32,000 firms paid the AMT in 1990 the number is not strictly comparable to earlier years as book income was replaced by adjusted current earnings in the calculation of alternative taxable income.

⁶The distinction of direct payment of the AMT is an important one. If firms took actions that increased their regular tax to avoid the AMT the Treasury would gain revenue from the imposition of the AMT even if no AMT were actually paid. As a result, the revenue figures for the AMT are lower bounds for the total amount of revenue generated by the AMT. To date, no studies have analyzed the extent of this activity.

⁷Gerardi et al. (1993) point out that their results probably understate the effect of the AMT since their panel did not include 1,473 firms with assets exceeding \$50 million.

Table 1. Distribution of corporate returns with AMT as a percent of total returns, by asset class.

Asset Size (\$ thousands)	1987	1988	1989
0 - 1,000	0.2	0.4	0.8
1,000 - 10,000	3.7	5.3	15.1
10,000 - 50,000	12.1	15.2	16.4
50,000 - 100,000	17.3	17.9	16.9
100,000 - 250,000	18.5	18.2	18.1
250,000 - 500,000	17.8	18.4	18.1
500,000 or more	21.2	21.1	19.7
Number of returns with AMT	17,400	25,200	25,300
AMT returns as a share of all returns	0.7	1.1	1.1

Source: Gerardi, Milner, and Silverstein (1993), Table 3.

on the AMT, the AMT status of a firm (both the amount of AMT payment and the preference items) is likely an important factor in an external assessment of the firm's total tax burden. Because the AMT entails payment of additional taxes (currently and potentially permanently) it represents, at a minimum, an increase in the present value of a firm's total tax liabilities, and a reduction in cash available for investors. The extent to which the present value of a firm's tax liability increases as a result of the AMT is a function of the amount of AMT payment and the length of time until any resulting AMT credits could be used to reduce the regular tax. The amount of information disclosed in the financial statement regarding the AMT could help investors determine how much the AMT affected total tax burden as well as help the general public assess the relative effectiveness of the AMT.

In 1987, firms following the guidance of APB-11 or SFAS-96 were required to disclose all significant differences between taxable income and pretax accounting income as well as identify causes of differences between the statutory rate and the firm's effective tax rate. As with many disclosure choices, however, firms face conflicting incentives, depending on expectations of how the information disclosed would be interpreted by the various financial statement users.⁸

An AMT liability was likely to be viewed differently from other federal taxes, because the intent of the AMT was to increase the tax on firms perceived as being too aggressive in using the tax code to reduce their liability. Given the political debate surrounding the AMT, well

summarized in Lyon (1997), disclosing payment of the AMT might be viewed as evidence of the effectiveness of the AMT (to the extent that it resulted in the greater explicit taxation of profitable firms). Conversely, some firms complained that AMTI was too broadly defined and that, as a result, inadvertently affected many firms that were not the intended targets of the AMT. As such, firms that perceived themselves as innocent bystanders collaterally damaged by the AMT might disclose payment of the AMT as evidence that the AMT was not working as intended and, thus, in need of modification.⁹

At least two authors¹⁰ have relied on self-disclosure to identify AMT firms, citing, for example, Accounting Series Release (ASR) 149 that requires firms to disclose certain timing differences. Under ASR 149, firms are required to: Provide reconciliation between the amount of reported total tax expense and the amount computed by multiplying the income before tax by the applicable statutory Federal income tax rate, showing the estimated dollar amount of each of the underlying causes for the difference. If no individual reconciling item amounts to more than five percent ... and the total difference to be reconciled is less than five percent ... no reconciliation need be provided unless it would be significant in appraising the trend of earnings. Reconciling items that are individually less than five percent of the computed amount may be aggregated in the reconciliation.

Reliance on self-disclosure assumes that disclosing firms are not otherwise systematically different from non-disclosing firms. If systematic differences exist between disclosing and non-disclosing firms, drawing conclusions based on the analysis of only those firms that disclose

⁸Gibbons et al. (1990) provide a framework for disclosure choices that considers both rules and a firm's strategic goals. Barth and Murphy (1994) along with Healy and Palepu (2001) (together with the commentary by Core (2001) provide overviews of required financial statement disclosures along with an analysis of their purposes. Elliott and Jacobson (1994) describe the costs and benefits of disclosures made by for-profit enterprises, and discuss the interests of the various users of disclosed information.

⁹In the Spring of 1995, Mobil Corporation devoted two of their "Sensible Solutions" advertisements, which appear in major national publications (e.g., *Time*) to advocating the repeal or modification of the corporate AMT.

¹⁰Manzon (1992) and Wang (1994).

can lead to incorrect inferences regarding the incidence of the AMT, the type of firms affected by the AMT and the response of those firms to the AMT. Such problems, of course, are not likely limited to the AMT disclosure case.¹¹ To the extent that tax disclosure choices respond to specific disclosure incentives, failure to control such incentives in any analysis will likely limit the validity of any tests and resulting conclusions reached.

METHODOLOGY

Sample identification

To determine the extent to which self-disclosure reflects firms' AMT position, we undertook a search of the text of annual reports following the procedure outlined in Wang (1994). First, 153 firms that self-disclosed they paid the AMT in 1987 were identified by a word search of NAARS using the search term "AMT or minimum tax." Data were then drawn for these firms and all others in the Compustat file. This file was then matched to the 1987 Statistics of Income Corporate Source Book File, a stratified sample of approximately 80,000 income tax returns,¹² and unmatched firms were deleted. This matching resulted in a sample of 1,180 firms. From this group, we eliminated 983 firms that did not pay the AMT. The sample we use in this study consists of the remaining 197 firms that paid the AMT. Of these firms, 69 had AMT liabilities greater than 5% of their reported pretax income; 19 (28%) of these 69 reported paying the AMT in their financial statements and 128 had AMT liabilities less than 5% of reported pretax income, 23 (18%) of whom reported paying the AMT in their financial statements. These data are shown in Table 2 along with some descriptive data on the two samples.

As expected, the two samples differ significantly with respect to the amount of AMT they pay relative to a calculated statutory tax liability, with mandatorily disclosing firms (AMTPCT > 5%) having a much higher percentage of their total tax liability attributable to the AMT than those for whom disclosure is voluntary. The two samples of firms have similar effective tax rates (ETR) and similar levels of total assets. Notably, firms which we determine should have been subject to mandatory disclosure of their AMT status were more profitable than firms for which disclosure was voluntary. Each sample has a comparable level of firms with NOLs. Notwithstanding the fact that the percentage of firms with AMT obligations greater than 5% of reported pretax income that reported paying the AMT (28%) is 56% higher than that of firms with AMT obligations under 5% of reported pretax income that reported paying the AMT (18%), it is far from 100%. The lack of uniform disclosure by firms with AMTPCT greater than 5% suggests that the numeric test identified in ASR 149 was either not viewed as binding by many firms or that ASR149 does a relatively poor (though not clearly biased) job in the aggregate in providing the identity of firms that, by rule, had to disclose the AMT.

Our use of matched financial-to-tax return data provides us with a unique setting in which to analyze disclosure. One shortcoming of disclosure research generally relates to the quality of the measures of disclosure (Healy and Palepu, 2001, pp. 426 - 427). In our setting we directly observe both the underlying tax status of the firm and whether there is a disclosure. Thus, we are able to minimize measurement error that could be related to our explanatory variables.

Modeling the disclosure decision

We use the following equation to estimate the significance of factors that proxy for the strategic disclosure choice of firms subject to the AMT in 1987:

$$\text{Disclose}_i = \beta_0 + \beta_1 \text{AMTPCT}_i + \beta_2 \text{ETR}_i + \beta_3 \ln \text{PI}_i + \beta_4 \text{NOL}_i + \beta_5 \text{IndProb}_i + \beta_6 \text{Consol}_i + e_i \quad (1)$$

where:

Disclose = 1 if the firm reported an AMT liability on its financial statements, 0.

AMTPCT = AMT liability (reported on the federal tax return) as a share of the statutory tax liability (pretax income * statutory tax rate). ETR = Effective tax rate¹³ (ratio of current federal taxes payable (Compustat data item 63) divided by pretax income).

lnPI = Logarithm of pretax income¹⁴ (Compustat data item 170).

NOL = Equal to 1 if the firm has a positive federal tax expense and NOL carryforwards (Compustat data item 52), 0 otherwise

IndProb = Probability of a firm in an industry being on the AMT, measured as the number of firms on the AMT in each industry divided by the total number of returns in that industry (excluding entities unaffected by the AMT).¹⁵

Consol = Consolidation variables, measured as the difference between assets reported on the tax return and assets reported on the financial statement, divided by financial statement assets.

We control for the relative significance of the AMT using a variable closely related to that used in our numeric rule to distinguish between firms that had to disclose their AMT status and those that did not. Specifically, AMTPCT is the ratio of AMT tax payment to the statutory tax liability based on reported pretax income and the statutory tax rate.

The primary targets of the AMT were profitable firms that reported low ETRs. The variable lnPI reflects differences in firms' sensitivity to political scrutiny with respect to reporting their AMT status. All else equal, we expect firms with higher levels of pretax income to be subject to increased political scrutiny. We expect that these firms would benefit from not drawing attention to their AMT tax status. Specifically, reporting AMT tax status could be viewed as equivalent to saying that, were it not for the AMT, such firms would have had a significantly smaller federal tax liability. Such a disclosure could be interpreted by proponents of the AMT as consistent with the AMT's effectiveness.

¹¹Relying on disclosure to determine the incidence of the AMT creates two problems. The first, addressed in this paper, is that many firms subject to the AMT may not disclose that information. Second, some research on the AMT has suggested that the largest responses to the AMT were made by firms that, as a result of managing accruals, were able to avoid the AMT altogether. See Boynton et al. (1992).

¹²A complete description of the 1987 SOI corporate sample can be found in IRS (1990).

¹³We follow Omer et al. (1991) in bounding ETR to the interval (-1, 1).

¹⁴The pretax income of firms with negative income were set to one dollar prior to taking the log.

¹⁵We exclude corporations statutorily unaffected by the AMT, such as subchapter S corporations.

Table 2. Actual versus Reported AMT Exposure for Firms with Different Levels of AMT Obligation Relative to Statutory Tax Obligation.

	AMTPCT>5%	AMTPCT<5%	Total
Disclose AMT Liability	19	23	42
Do Not Disclose AMT Liability	50	105	155
Total	69	128	197

Table 2b.

	AMTPCT>5%	AMTPCT<5%
Number of Firms	69	128
AMTPCT	0.161(0.12)	0.02(0.02)
ETR	0.117(0.26)	0.133(0.30)
ln (Assets)	6.040(1.72)	6.398(1.89)
ln (Pretax Income)	2.807(1.94)	1.271(6.43)
NOL	0.246(0.43)	0.242(0.430)
IndProb	.0123(0.003)	0.013(0.003)

(Dollar amounts in millions, standard deviations in parentheses).

In contrast to not disclosing an AMT liability to mitigate adverse political scrutiny is disclosing an AMT liability to obtain favorable treatment via the political process.¹⁶ We expect that firms with relatively high ETRs but subject to the AMT would be more likely to disclose their AMT status as part of an attempt to curry political favor. Other firms that could make the case that they were “inadvertently” or “inappropriately” paying the AMT would include those with NOLs that would not otherwise have an income tax liability in the current year. These firms may well view the AMT as imposing an unfair burden on their operations and make an effective case for AMT repeal. To test for the incentives of loss firms subject to the AMT we include a dummy variable, NOL, which is equal to one for any firm with a positive federal tax expense possessing NOL carry forwards.

The percentage of firms in an industry paying the minimum tax (IndProb) is expected to be positively related to the probability of disclosure because disclosure is less likely to result in a competitive disadvantage.¹⁷ This variable is also related to the political cost variables described above, as industries targeted by the AMT, or which feel they were being unfairly penalized by the AMT, could use disclosure as part of a strategy to influence legislative changes. We include two variables to measure consolidation differences between financial reporting and tax entities: $A_{tax} - A_{book}$ is the amount by which tax return assets exceed financial statement assets, if positive, and zero otherwise; $A_{book} - A_{tax}$ is the amount by which financial statement assets exceed tax return assets, if positive and zero otherwise. Both variables are scaled by financial statement assets. As $A_{tax} - A_{book}$ increases, differences in the tax status of the entities are expected to increase, decreasing the likelihood that the

reported tax status and the actual tax status will be the same. As discussed in Dworin (1985) and Plesko (2000, 2003), differences in entity are a critical factor in reconciling reported tax status with actual tax status. With respect to the AMT, tax-consolidated entities that include finance subsidiaries and generate significant preference items are more likely to be subject to the AMT than firms that do not have finance subsidiaries.¹⁸ Also, firms that make extensive investments in tax-preferred assets or which finance using tax-preferred debt are more likely to be subject to the AMT than firms that do not make such investment and financing choices.

RESULTS AND ANALYSIS

The results of estimating equation (1) are shown in Table 3. We estimate equation (1) for two subsamples of firms: those that we estimate had to disclose AMT status and those that we estimate did not have to disclose. Column (1) provides the results for the sub-sample of 69 firms that we estimate had to disclose an AMT liability following ASR 149. The most striking results are seen in the estimated coefficient on the first three variables, AMTPCT, ETR and lnPI, none of which is statistically significant. This implies that for firms with relatively large AMT liabilities, neither the magnitude of that liability, nor their overall tax burden, are associated with disclosure. Based on the next two coefficients, NOL and IndProb, both of which are positive and statistically significant, the only factors that appeared to play a role in the decision to disclose are whether the firm currently had an NOL and the incidence of the AMT among firms in the same

¹⁶The airline industry, for example, used its exposure to the AMT to lobby for changes in the AMT depreciation preference (Aviation Daily, 1993). In 1989, when hearings were held on modification to the AMT, a broad group of industries testified in favor of changes in the AMT, particularly the treatment of depreciation. These industries included petroleum, utilities, mining, computer lessors, and manufacturers.

¹⁷See Healy and Palepu (2001, p. 424-425) for a brief description of the research on the proprietary costs of disclosure.

¹⁸See Stickney et al. (1983) for a specific example of the complications introduced into the tax reporting problem by the presence of a finance subsidiary.

Table 3. Determinants of disclosure.

	AMT > 5%		AMT < 5%	
	(1)	(2)	(3)	(4)
	Coefficient estimates	Marginal effects	Coefficient estimates	Marginal effects
AMTPCT	3.649 (2.989)	0.636	36.197** (15.368)	3.344
ETR	-0.252 (1.215)	-0.044	-2.768** (1.140)	-0.226
ln(pretax income)	0.185 (0.175)	0.032	-0.111** (0.048)	-0.010
NOL	1.509** (0.636)	0.308	1.988*** (0.596)	0.275
Industry probability	243.195*** (78.282)	4.240	49.769 (90.490)	0.460
Tax Assets - Financial	-0.077 (0.061)	-0.013	-0.630 (0.783)	-0.058
Financial Assets - Tax	-1.096 (4.571)	-0.191	-3.489 (2.977)	-0.322
Constant	-5.548*** (1.229)		-4.539*** (1.831)	
Number of Firms	69		128	
log likelihood	-34.927		-45.243	
Π^2	18.67***		34.54***	
Predictions				
Correct disclose	0.68		0.70	
Correct non-disclose	0.66		0.74	
Correct overall	0.67		0.73	

The dependent variable is equal to 1 if the firm disclosed its AMT status, 0 otherwise. Robust standard errors are reported in parentheses. Marginal probabilities are listed in the second column of each equation. For continuous variables, the marginal probabilities represent the change in the probability a firm would disclose if the variable was increased by one percent from its mean value, calculated at the mean of the explanatory variables with dummy variables equal to zero. Marginal probabilities for share variables were calculated by increasing the share 1 percentage point. The marginal probability of a dummy variable was estimated as a change from 0 to 1. Number of observations: 197, 42 disclosing (21.3%). Significance levels: ***1, 5 and 10%.

industry.

Column (2) reports the marginal effect of each variable.¹⁹ In the case of NOL, the marginal effect of 0.308 implies that the presence on an NOL increased the likelihood that a firm would disclose an AMT liability by slightly more than 30%. The magnitude of the estimated marginal effect for IndProb implies that a one-percentage point increase in the industry probability is associated with a 4.2% increase in the probability that a firm in the industry will disclose their AMT liability. The final two variables are statistically insignificant, suggesting that the degree of consolidation was not associated with the disclosure decision.

The bottom of Table 1 provides information on the model's success in predicting firms' disclosure choice.

Overall, the model correctly identifies 67% of firms that

disclosed their AMT liability, with similar success in predicting the choices of both disclosing firms (0.68) and non-disclosing firms (0.66).

Column (3) presents the results of estimating equation (1) for AMT firms that did not have to disclose AMT status under ASR 149's five percent rule. In contrast to the sample of firms that had to disclose their AMT status, each of the first three coefficients is statistically significant. The coefficient on AMTPCT is positive and significant. This result indicates that, as the relative significance of the AMT increased, firms were more likely to disclose that they paid the AMT even though such disclosure was not strictly required. This is in contrast to the results presented in column (1) that suggest that is the threshold at which reporting AMT status was mandatory the relative significance of the AMT obligation did not affect the likelihood of disclosure.

The coefficient on ETR is negative, indicating that low ETR firms were more likely to disclose AMT status than those with high ETRs. This finding is contrary to expectation. We anticipated that firms with low ETRs that were subject to the AMT would choose not to disclose AMT status so as to reduce the perception that the AMT was, in fact, effectively subjecting to higher immediate taxation firms that were paying a relatively low current tax as a percentage of pretax income.

¹⁹ For continuous variables, the marginal probabilities were based on a one percent change in the value of the variable, calculated at the mean of the independent variables, with dummy variables set equal to zero. Marginal probabilities of dummy variables were calculated as a change from 0 to 1. For ease of interpretation, each estimate was multiplied by 100 so that the listed probability represents the percent change in the estimated probability a firm would disclose. In the case of pretax income, a one percent increase in the log of pretax income of a firm whose disclosure of AMT status is voluntary is estimated to decrease the probability of disclosure 0.012%.

The coefficient on the log of pretax income is negative and significant, indicating that firms with relatively low (high) pretax income were more likely to voluntarily disclose (not disclose) AMT status. This result is consistent with relatively low income firms attempting to influence political opinion with respect to the AMT.

As with the AMTPCT greater than five percent group, the coefficient on NOL is positive and significant, again consistent with the proposition that firms with NOLs that had to pay the AMT wanted to highlight that they were paying the AMT even though they did not fit the profile of firms that the AMT was intended to affect. As in column (1), we interpret the greater disclosure of AMT status by NOL firms as consistent with them pursuing a political agenda to bring about change in the AMT statute.

Taken together, our results with respect to AMTPCT, lnPI and NOL are consistent with the view that firms use disclosure to influence political action or avoid political scrutiny. The coefficient on the industry probability variable is not significant for firms that, under ASR 149, were not required to disclose AMT status. This result is consistent with the proposition that firms within a particular industry, but with less extensive AMT liabilities, did not necessarily have similar reporting objectives. Rather, variables that proxy for political costs are more significant in explaining the disclosure choices of firms that were not required to disclose AMT status than those that were required to disclose AMT status. The common disclosure patterns found in column (1) are not present among firms with lower AMT exposure. Further, as in column (1), the consolidation variables are not significant.

The tabulations presented at the bottom of Column (3) shows that this model correctly identifies 70% of disclosing firms and 74% of non-disclosing firms, with 73% of all firms' disclosure choices correctly predicted.

We draw two conclusions from our regression results. First, there are significant and nonrandom, factors that influence the disclosure choice, suggesting that those firms that disclose are not representative of the population of firms subject to the AMT. Because the choice to disclose is related to specific factors that differ cross-sectionally across firms subject to the AMT, we believe conclusions regarding the disclosure patterns of AMT firms' behavior based upon firms which self-disclose AMT liability should be made with caution.

Second, our results provide insight into the role of the political process on accounting disclosure. Our results indicate that disclosure is predicated on likely political outcomes. The voluntary disclosure of firms with a high percentage of AMT liability to regular tax liability and voluntary and mandatory disclosure of firms with NOLs appears consistent with an attempt to influence the legislative process to alter the AMT. Similarly, the selective non-disclosure of AMT status by more profitable firms appears consistent with these firms attempting to suppress information that the AMT was effective in

increasing their tax burden. Presumptively, such information would potentially be useful in blunting calls for repeal or alternation of the AMT statute.

The results we report are consistent with the broadest description of the political process—that of a competition for wealth transfers—in which disclosure is an additional tool the firm can use to increase or retain wealth.²⁰

Separately, these results are also consistent with the results reported by Wang (1994) on earnings management in response to the AMT and partially address the criticisms of Choi et al. (2001)²¹. Wang developed partitions of firms based on their self-disclosed AMT position. Given our results, his control sample of non-AMT firms may have contained a number of AMT firms that merely did not disclose. Partitioning on the disclosure should have created a bias against his finding statistically significant differences between the two sets of firms. Given the potential bias, his statistical results should be viewed as a lower bound on the extent of AMT-induced accruals.

DISCUSSION

In this study we examine the disclosure choices of firms paying the AMT. The AMT was designed to insure that all firms paid their "fair share" of tax, a largely political objective that grew out of highly publicized instances of profitable firms paying little or no explicit taxes.²² Our access to proprietary IRS data allows us to determine with precision firms reported tax status as well as their actual tax status. The ability to classify with precision the required and actual disclosure status allows us to test different disclosure motivations. Our ability to identify the disclosure requirements and status of firms and develop differential reporting hypotheses as a function of a bright line reporting requirement provides us with a unique disclosure setting to study.

We show that self-disclosure of AMT tax status provides an incomplete picture of firms' actual tax status. The choice to disclose certain tax information is based, in part, on regulatory guidelines. Disclosure choices also appear to be balanced against the potential costs and benefits of disclosure. In particular, we find evidence that political considerations played an important role in firms' choice to disclose. The variables that are significant in explaining the disclosure choice are consistent with the view that firms use disclosure to pursue political goals.

The importance of political factors in firms' tax disclosure decisions has implications for firms that will soon be

²⁰This is also consistent with the results of Jones (1991) who showed that firms may have managed their earnings downwards during periods when they sought regulatory relief from foreign imports.

²¹Dhaliwal (2001) provides a more extensive analysis of the criticisms of Choi et al. (2001).

²²For a brief history and assessment of the AMT from various perspectives, see, U.S. Senate (1995).

reporting under the guidance provided in FIN 48. FIN 48 requires that firms defer the recognition of tax benefits related to uncertain tax positions and to provide footnote disclosure of aggregate uncertain tax positions. Such disclosure may well expose firms to unwanted scrutiny from political actors including the SEC, the IRS and members of Congress. Firms may fail to fully comply with new disclosure requirements (as they have apparently done so with respect to AMT disclosures) or alter the aggressiveness of tax planning activities to avoid attracting unwanted attention.

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