DATE: January 26, 2015

TO: Director of Research and Technical Activities
    Project No. 19-20E

FROM: Teresa MacCartney, State CFO, Director of OPB
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RE: Tax Abatement Exposure Draft

The State of Georgia appreciates the opportunity to respond to the Government Accounting Board’s exposure draft relative to Tax Abatements. While we agree that providing information to our stakeholders and continuing to strive for transparency is important, we do not believe the financial statements are the most appropriate medium for disclosures relative to tax abatements. The financial statements already reflect the net tax collected, and any future refunds due at the end of the fiscal year and therefore already reflect the impact of any tax abatements in the reporting period. We believe the requirements in the ED stretches the traditional concept of public accountability within financial reporting perspective, and in some cases, as described below, will create more confusion and questions rather than clarity.

The Board has clearly recognized that governments grant tax abatements in response to a promise to take a specific action that benefits the government or its citizenry. The Board, however, has elected to require disclosure of only the tax abatement and not the associated benefits. We are concerned that the Board is considering a standard to address “financial statement users need for information about certain limitations on a government’s ability to raise resources” without providing the reader the tools to do so. The premise that tax abatements limit a government’s ability to raise future revenues is debatable, and a reader without access to both the realized abatement and the actual benefits generated could not draw an informed conclusion that the abatement created such limitation.

We do agree with the Board that benefits deriving from tax abatement agreements vary and may not be readily quantifiable, and, therefore, should not be included in financial reporting. However, we also believe that disclosing the initial reduction in tax collections without also discussing the potential benefits fails to faithfully represent the underlying events and conditions of the tax abatements will mislead report users. For example, a government may stipulate in a tax abatement agreement that a company produce a certain number of jobs and
maintain that level of employment for a given period of time. As a result, it is possible for the increase tax revenues from those newly created jobs to exceed the revenue abated. In such a circumstance, the disclosures required in this ED would be misleading as it pertains to the effect of the abatement and the government’s future ability to raise resources and meet its financial obligations. Therefore, if it is not practical to disclose information about the benefits then one should also not disclose information about the abatement.

We agree with the Board that tax abatements are used by governments for economic growth. We believe that if governments invest in economic growth (abate taxes) then the overall revenue base from which resources are derived is broadened. This process allows you to raise resources and kick start an underperforming asset (such as undeveloped land). We would also suggest that disclosure of this information could be detrimental to the government making such a disclosure since other taxpayers and other governments would become more aware of these incentives and use this information for negotiation and/or competitive purposes. Ironically, disclosure of this information could have a far larger negative impact on the government’s future ability to raise resources and meet its financial obligations than the abatement itself.

We also believe that GASB’s decision to exclude “disclosure of the amounts remaining to be abated in future years under existing tax abatement agreements” is contradictory to an anticipated result of the ED that “users would be better equipped to understand (1) how tax abatements affect the government’s future ability to raise resources and meet its financial obligations.” We recognize that arrangements may exist where future abatements may be difficult to reliably quantify and agree with the Board’s decision to exclude them from disclosure. However, this is another example demonstrating the limitations of historical financial reporting as an appropriate avenue for providing a complete picture of the nature and magnitude of tax abatements, including how it pertains to economic condition.

For all of the aforementioned reasons, we do not believe that financial statements are a good medium for disclosing tax abatement information. However, if GASB’s intent is that financial statements are the best means of disclosure for tax abatements we urge further consideration of the following items:

1. Legal and Confidentiality issues:

States have confidentiality laws that generally prevent the state from disclosing aggregate tax information when the data collected comes from fewer than three taxpayers in order to avoid disclosing confidential taxpayer information. The Board’s proposed reporting requirements would be in conflict with State’s taxpayer confidentiality laws with respect to tax abatements received by fewer than three taxpayers. If a government is not legally able to disclose tax abatement information in certain circumstances, would reporting the legal restrictions on disclosing confidential information exempt the government from meeting the requirements of the proposed standard? We believe the Board should clarify this position.
2. Abatements don’t always reduce revenue:

The limitation of the ED to only tax abatements where a “promise from the recipient to subsequently perform a beneficial action in order to lower its tax obligation” excludes other forms of economic incentive programs that may also affect revenue of the government such as fee rebates. This also excludes any agreement to abate taxes for a period where there is no expectation for a subsequent action. If GASB is intent on using the financial statements as the vehicle of disclosing this type of information, it seems arbitrary and potentially misleading for GASB to limit the applicability and scope of this standard to the one revenue stream as defined in the ED.

3. Materiality:

Taxes are typically a major revenue source for governments. Since the provisions of the proposed standard would not be applied to immaterial items, we believe the public would expect but not necessarily get a comprehensive picture of a government’s tax abatement programs via financial statement disclosure. A state could easily have $20 billion in tax revenue and $100 million in tax abatements which could be suggested are immaterial in relation to overall tax revenue and as a result no disclosure would be made. Of course, we don’t suggest eliminating materiality from the ED, but we do suggest that folks wanting transparency information such as tax abatements usually do so without the concept of materiality.

This standard seems more applicable to transparency initiatives already underway in various forms outside of the CAFR process and we believe that is a more appropriate vehicle for this topic. Multiple states, including Georgia, are already providing some level of tax expenditure and/or tax abatements disclosures. In many cases, these disclosures are required by state law and provide states with more flexibility on the level of detail disclosed.

4. Definition of taxpayer:

Lastly, we think the term “taxpayer” in the ED should be clarified as stated in the “Definition of a Tax Abatement,” paragraph. The term “taxpayer” could be interpreted as excluding those entities where all corporate taxes are abated for a specific time period, which could occur for an entity new to the governmental jurisdiction that will not pay taxes until after complete abatement of taxes ends, and therefore is not yet a taxpayer.

5. Definition of tax abatement:

The ED states that an agreement must precede the taxpayer’s action. A tax abatement agreement does not exist if the government does not commit to the tax reduction until after the taxpayer has performed the activity. In other words, mutual promises of performance must exist prior to the taxpayer action. We believe that in many cases it will be very difficult to differentiate between a unilateral promise by a government to provide a tax benefit if certain conditions are met, and mutual promises that a taxpayer will
perform an action and the government will in return provide a tax benefit that necessarily cannot occur until after performance. We believe the determination of whether an agreement exists will be open to substantial debate.

We are also concerned that not all tax abatements reduce tax revenues. For example, property tax exemptions do not necessarily result in reduced taxes for the taxing districts. This is because the exempt taxes are shifted onto non-exempt properties whose owners pay higher taxes. Unless a taxing district’s levy rate is at its statutory maximum, the exemption will not reduce the amount of property taxes received by the taxing district. Should a government be required to report information about tax abatements that do not reduce the amount of tax revenues received by the government?

6. Recapture provision

The Board should reconsider requiring disclosure of tax abatement amounts that were recaptured and/or eligible for recapture for the reporting period. The Board notes that amounts recaptured during the year would be recognized as revenues and amounts eligible for recapture would be recognized as receivables, but concedes that these amounts may not be readily available to financial statement users. Therefore, the Board should consider explicitly disclosing these amounts.

In conclusion, we are concerned that the ED starts a journey from a historical fact-based discussion of “what did happen” as presented in the CAFR to a discussion of “what could happen”. Are we going to disclose revenue associated with discretionary abatements such as speeding tickets not written by a police officer, fines not imposed by a judge, an annual fuel tax surcharge increase not imposed, or toll roads discontinued?

The State takes the financial reporting process extremely serious and wants to provide accurate and timely financial reporting in support of our AAA bond ratings and will endeavor to continue properly applying all GASB standards. We appreciated the opportunity to provide our thoughts on the proposed statement and hope the Board will consider our feedback when determining how to proceed.

Respectfully submitted,

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Alan Skelton