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Surge in Corporate Income Tax Collections Offers Opportunity for Tax Reform

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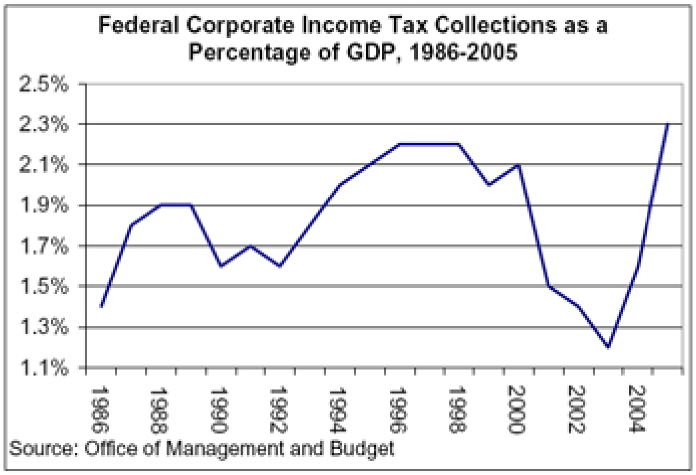
As the House Ways and Means Committee prepares to hold a series of hearings on corporate tax reform and international competitiveness, they will be confronted by recent data that show a precipitous increase in corporate tax collections over the past two years. These increasing corporate tax receipts give lawmakers a window of opportunity to invest in tax code improvements for the long term: lowering the corporate income tax rate, broadening the tax base and integrating the corporate income tax with the individual income tax system.

In February, the Office of Management and Budget (OMB) released the final revenue figures for Fiscal Year 2005. Corporate tax collections totaled $278 billion, up from $195 billion in 2004 and $139 billion in 2003 (all in real 2005 dollars). That represents a real rate of growth of over 100 percent over two years. A new study by the Congressional Budget Office (CBO) shows this trend has continued into 2006. As of April 2006, corporate income tax receipts are up nearly 30 percent over receipts during the same period in 2005.

The recent surge in corporate income tax collections has substantially increased corporate tax collections as a percentage of Gross Domestic Product (GDP) from 1.2 percent of GDP in FY 2003 to 1.6 percent in FY 2004 and, most recently, 2.3 percent in 2005. By this measure, corporate tax collections in 2005 were higher than in any year since 1980.

Figure 1. Rising Corporate Income Tax Collections as a Percentage of GDP



Source: Office of Management and Budget

Corporate income tax collections have also become a more important revenue source for the federal treasury in recent years. During the 1990s, corporate tax collections ticked upward to an average of 10.5 percent of federal receipts. This was due to remarkably strong economic activity and President Clinton's 1993 tax package, which raised the top statutory corporate income tax rate from 34 percent to 35 percent.

The recession that began in 2001 forced down corporate tax collections along with the larger economy. Corporate income taxes accounted for just 7.6 percent of federal revenues in 2001. Revenues remained low for three years, and in 2003 corporate income taxes raised 7.4 percent of total federal revenue. As the economy rebounded, corporate income taxes rose to 10.1 percent of federal revenue in 2004, and 12.9 percent of federal revenue in 2005—their highest share of total receipts since 1979.

As this roller coaster of corporate collections shows, economic conditions are the main determinants of corporate tax revenue. Because corporate profits are volatile—rising sharply in booms and falling steeply in recessions—so too are government receipts from the corporate income tax. Over the long term, however, the trend of federal corporate tax receipts is steadily upward.

Growth in S-Corporations

During the 1990s, a trend began toward companies organizing as S corporations rather than traditional C corporations. Because the income of S corporations is taxed through the individual income tax rather than the corporate tax, this resulted in a sharp increase in the amount of business income that was channeled into the individual income tax system. (Please see related "Fiscal Fact" at http://www.taxfoundation.org/publications/show/1477.html.)

Considering the rapid growth of S corporations since the individual income tax cuts in 2003, the dramatic growth of corporate tax collections from traditional C corporations in the past two years is remarkable. These surging collections place U.S. lawmakers in a unique position to compete with the corporate tax rate reductions recently enacted by many of the U.S.'s major trading partners in the OECD. (Please see related "Fiscal Fact" at http://www.taxfoundation.org/publications/show/1466.html.)

Table 1. U.S. Corporate Income Tax Collections, 1976-2005

Year	Corporate Income Tax Collections ($millions)	Percentage of Total Federal Receipts	Percentage of GDP
1976	41,409	13.9%	2.4%
1977	54,892	15.4%	2.8%
1978	59,952	15.0%	2.7%
1979	65,677	14.2%	2.6%
1980	64,600	12.5%	2.4%
1981	61,137	10.2%	2.0%
1982	49,207	8.0%	1.5%
1983	37,022	6.2%	1.1%
1984	56,893	8.5%	1.5%
1985	61,331	8.4%	1.5%
1986	63,143	8.2%	1.4%
Top statutory rate lowered from 46% to 34% as part of the Tax Reform Act of 1986 (an overall tax increase on corporations)			
1987	83,926	9.8%	1.8%
1988	94,508	10.4%	1.9%
1989	103,291	10.4%	1.9%
1990	93,507	9.1%	1.6%
1991	98,086	9.3%	1.7%
1992	100,270	9.2%	1.6%
1993	117,520	10.2%	1.8%
Top statutory rate raised from 34% to 35% as part of the Omnibus Budget Reconciliation Act of 1993 (an overall tax increase on corporations)			
1994	140,385	11.2%	2.0%
1995	157,004	11.6%	2.1%
1996	171,824	11.8%	2.2%
1997	182,293	11.5%	2.2%
1998	188,677	11.0%	2.2%
1999	184,680	10.1%	2.0%
2000	207,289	10.2%	2.1%
2001	151,075	7.6%	1.5%
2002	148,044	8.0%	1.4%
2003	131,778	7.4%	1.2%
2004	189,371	10.1%	1.6%
2005	278,282	12.9%	2.3%

Source: Office of Management and Budget, Tax Foundation

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