Investors miss out when tax deals are concealed

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Investors could benefit if they had timely information about non-income tax deals, according to new research from The University of Texas at Austin that finds companies that get them have higher future stock returns.

In 2022, U.S. corporations reaped more than $19 billion in non-income tax megadeals: state and local tax breaks worth $50 million or more. That's according to Good Jobs First, a nonprofit that tracks tax subsidies for corporate facilities.

Unfortunately, investors don't get such information. Accounting rules do not require companies to disclose the deals in financial statements. By the time they make it into GJF's database, they're often months or years old.

"What we show in this paper couldn't be a viable real-time trading strategy," said Brady Williams, associate professor of accounting at the McCombs School of Business. "This paper highlights the inadequacy of the information environment around non-income taxes."

With Michael Drake of Brigham Young University, Ryan Hess of Oklahoma State University, and Jaron Wilde of the University of Iowa, Williams analyzed tax incentive deals from GJF's database. Covering 1,031 state and local governments from 2003 to 2016, the researchers found:

- For companies that got tax breaks, sales the following year were 9.6% higher than for comparable companies that did not.
- Tax breaks boosted their stock returns 4.1%, compared with companies that did not get them.

It's not clear whether the tax breaks helped generate the higher sales and returns, Williams said. He noted that governments tend to award them to companies whose prospects are already bright.

"A major company comes to a city or county and says, 'We have financing secured, we think we have the demand, and we're willing to back that up with hundreds of millions of dollars of investment in your jurisdiction,'" he said. "That's essentially a signal of private information that the market might not be privy to at the moment."

Should companies be required to disclose non-income tax deals in their financials? Not necessarily, Williams said. Making such deals public too soon might discourage governments from offering them and remove one lever they can use to stimulate the local economy.

"The results suggest that (investors) could make more informed trading decisions if they had access to this information," he said.

Provided by University of Texas at Austin

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