Nuts & Bolts of Corporate Tax Reform

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Presentation for the Alliance for a Just Society

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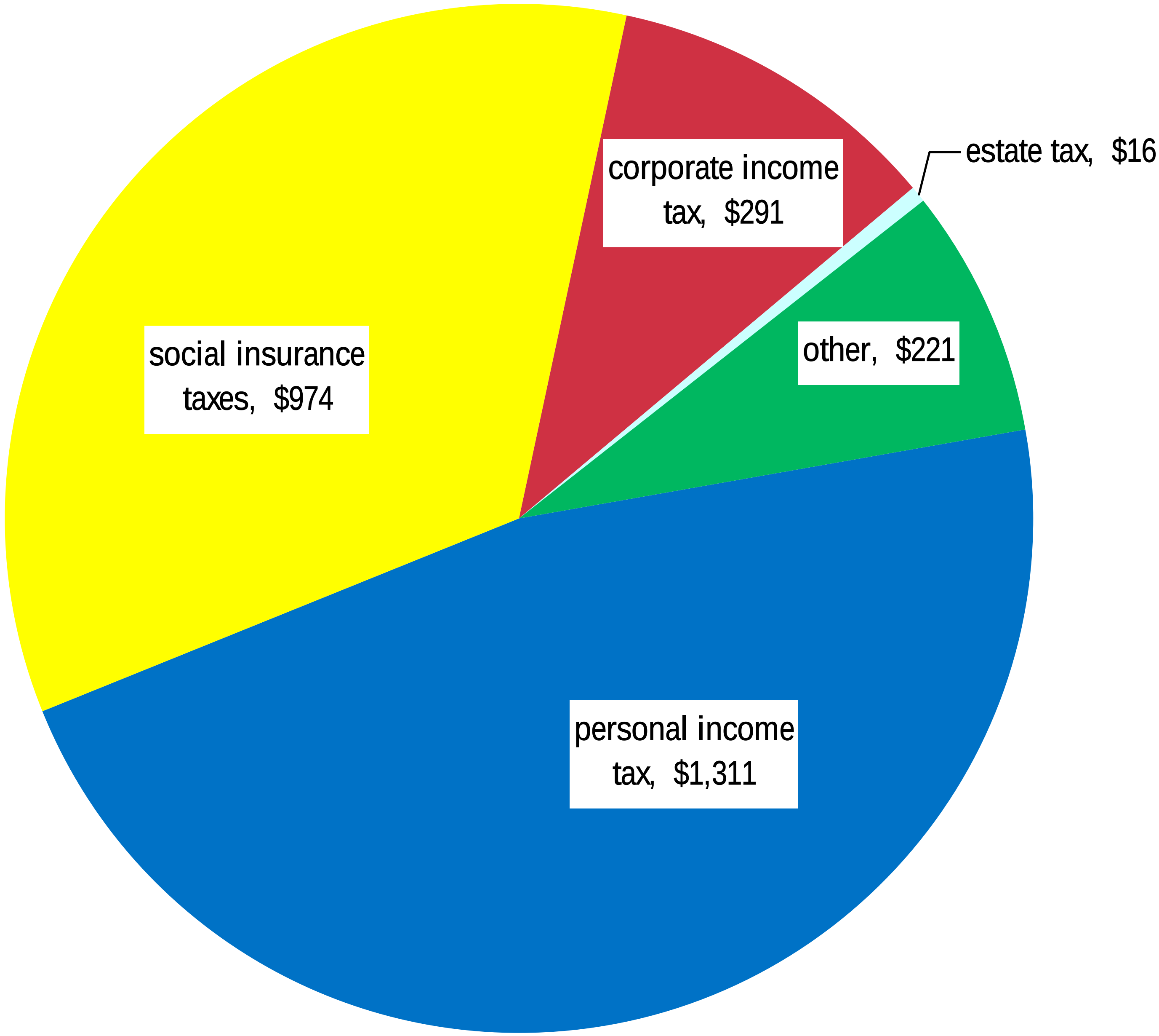
The Work of Citizens for Tax Justice (CTJ) on Federal Tax Policy

- Analyses using our computer model to determine revenue impacts and distributional impacts of the personal income tax and social insurance taxes and proposals to alter them.

- Research on the corporate income taxes paid or avoided by specific corporations.

- Simple-as-possible explanations of tax policy and proposals to change it.

Sources of Federal Revenue in Billions of Dollars in 2013



Source: CBO May 2013 and calculations by Citizens for Tax Justice, May 2013

Summary

1. The U.S. needs more revenue.

2. New revenue must come from progressive sources.

3. The corporate tax is a progressive revenue source.

4. American corporations are undertaxed.

5. One way to get more corporate tax revenue is to close tax loopholes related to offshore tax havens.

6. We must stop current proposals to *expand* these loopholes (territorial tax system, repatriation holiday).

Many Lawmakers and Their Lobbyist Friends Argue Against These Points

- The Republican chairman of the tax-writing committee in the House (Dave Camp) says Congress should <u>*not*</u> raise more revenue.

- President Obama says we should raise more revenue from the personal income tax, but <u>*not*</u> from the corporate income tax.

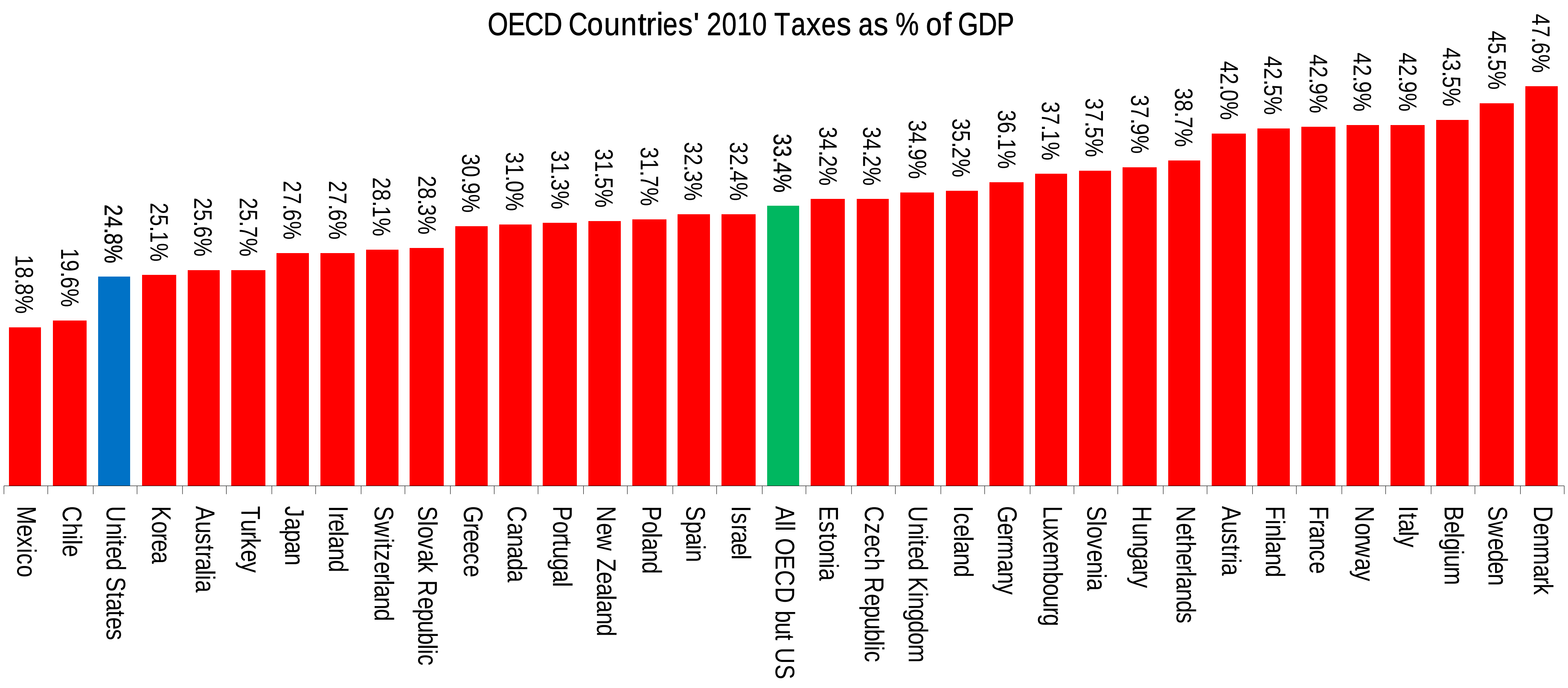
- Many say the tax code is <u>*too*</u> progressive (remember Romney's 47% comment).

- Many say corporations are <u>*overtaxed*</u>.

- Corporations say they need lower rates and a break on offshore profits to be "competitive."

- They're all <u>*wrong*</u>.

The U.S. Needs More Revenue



For more, see CTJ report from 4/8/2013

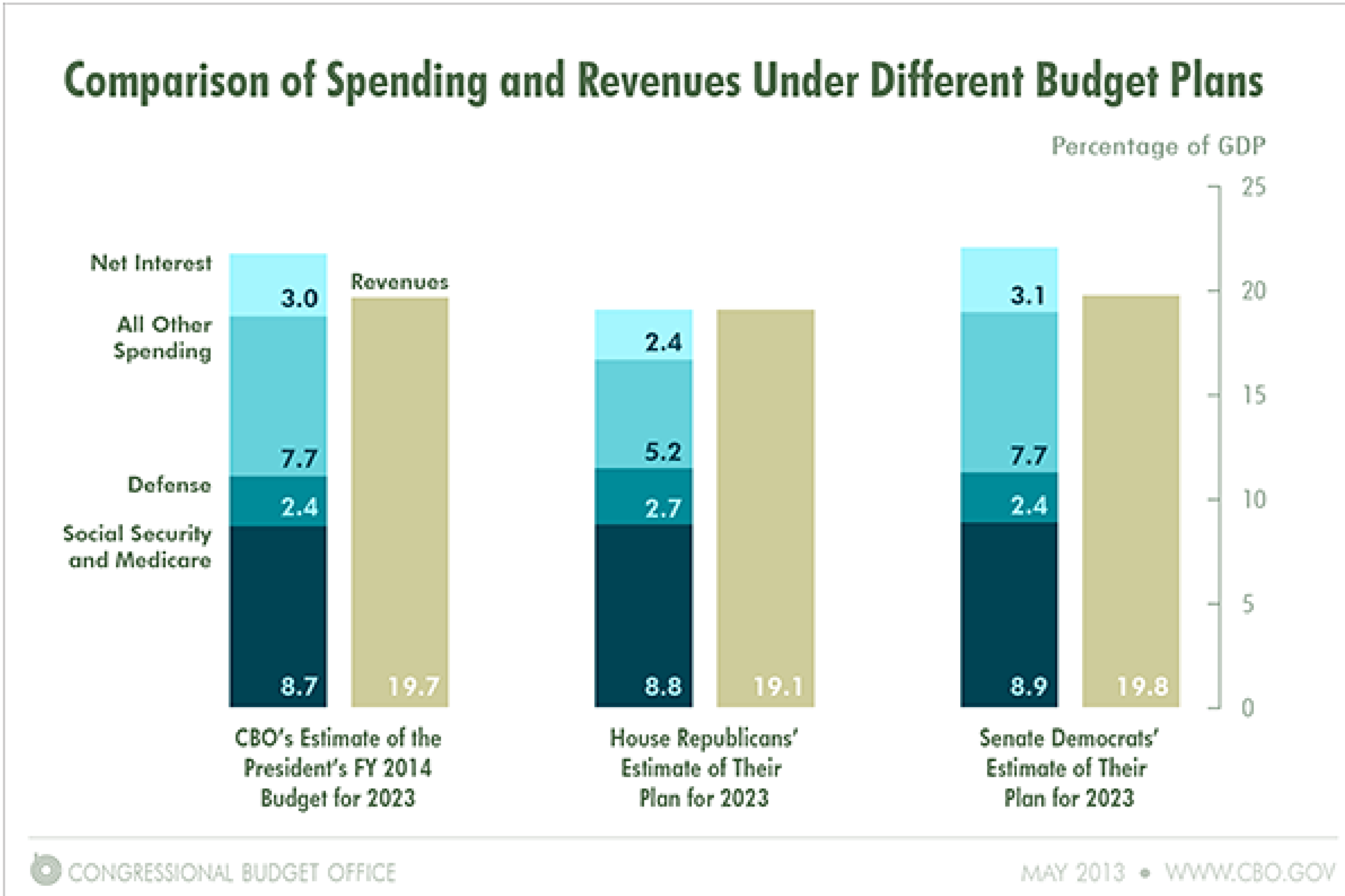
The U.S. Needs More Revenue

- Federal spending during the Reagan years ranged from 21.3% to 23.5% of the U.S. economy.

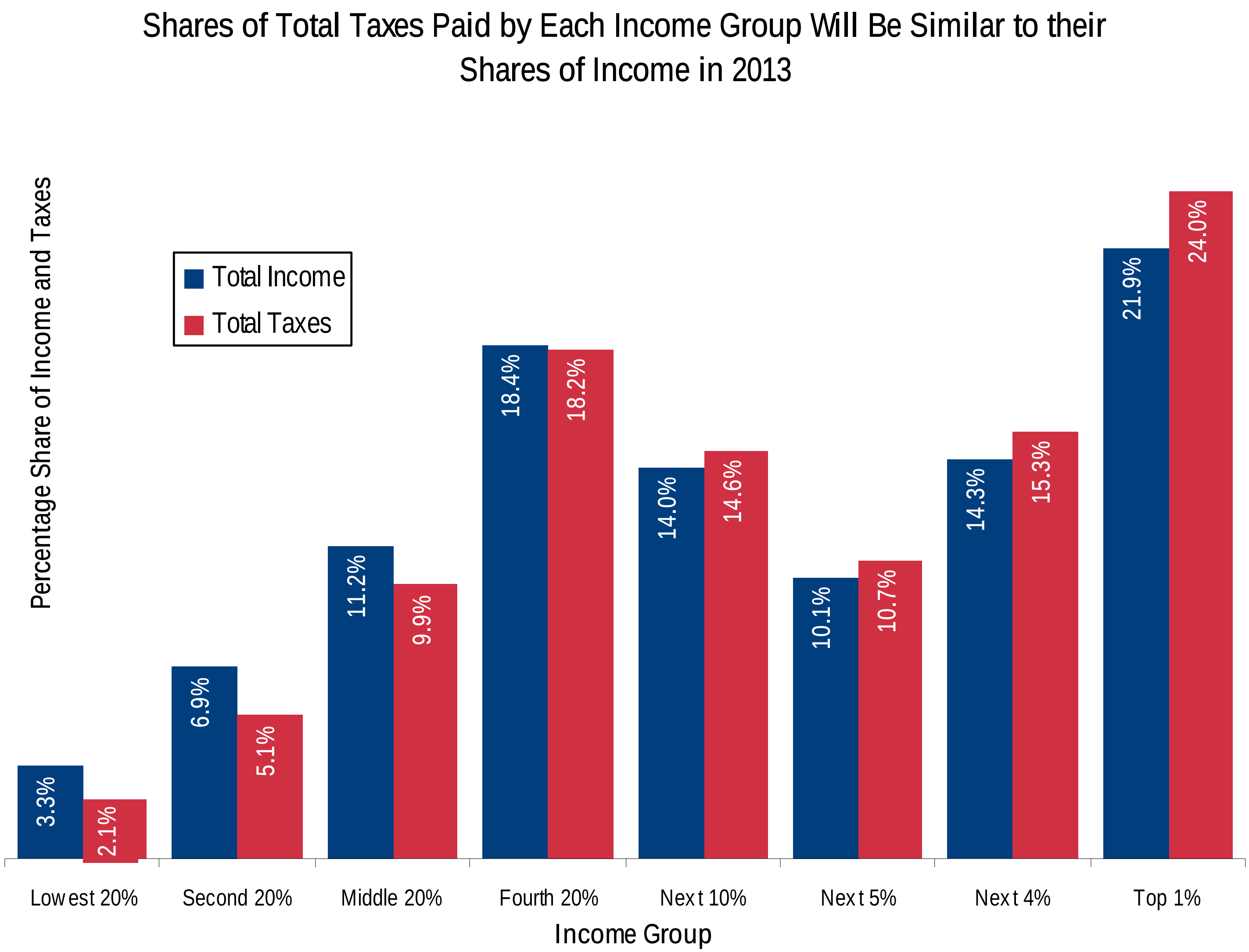
- Spending cannot reasonably be lower over the coming decades as the baby boomers retire.

- Our current tax laws will collect federal taxes equal to only about 19.1% of our economy within a decade.

The U.S. Needs More Revenue

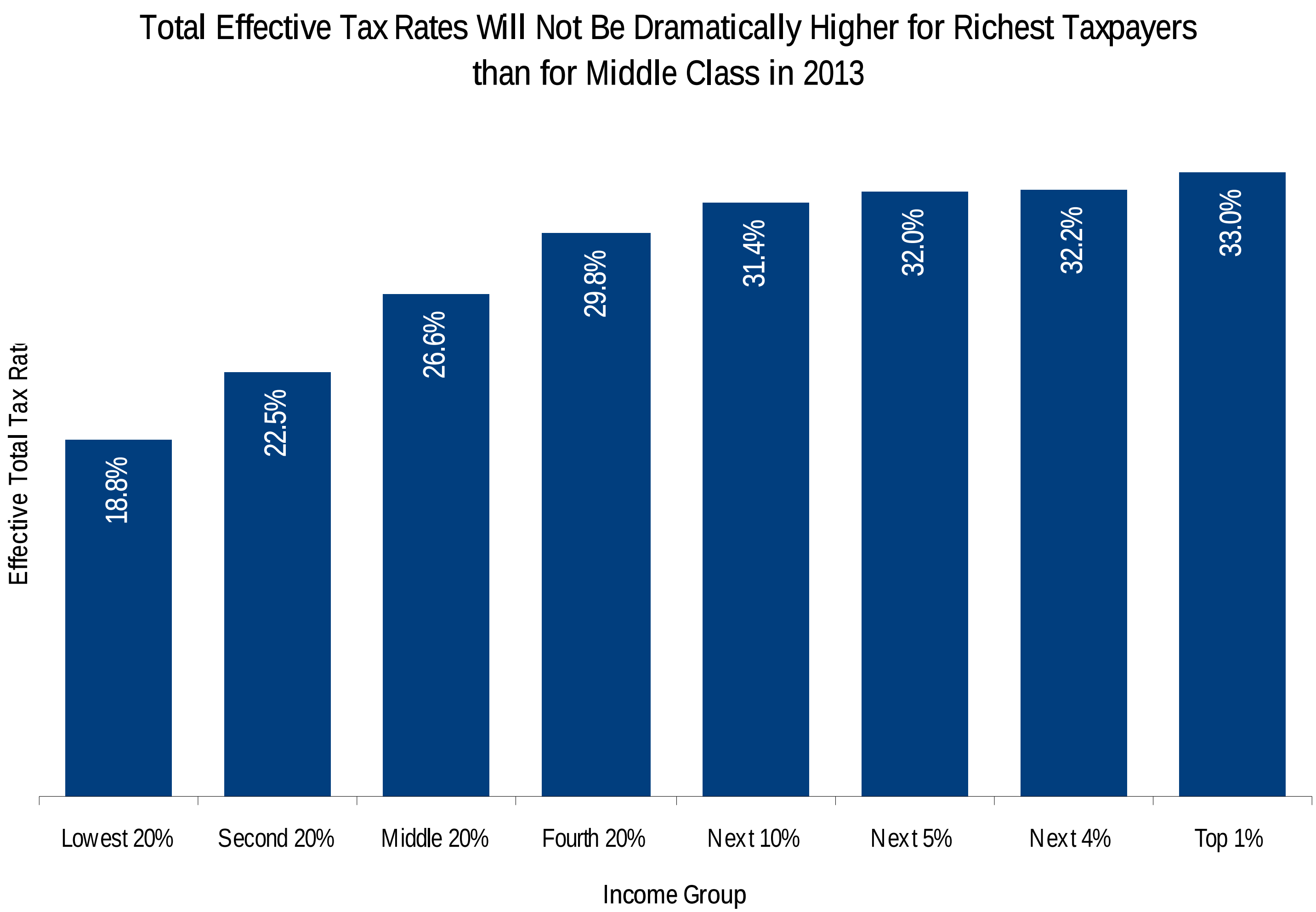


Revenue Must Come from Progressive Sources



Source: Institute on Taxation and Economic Policy (ITEP) Tax Model, April 2013
Citizens for Tax Justice, April 2013.

Revenue Must Come from Progressive Sources



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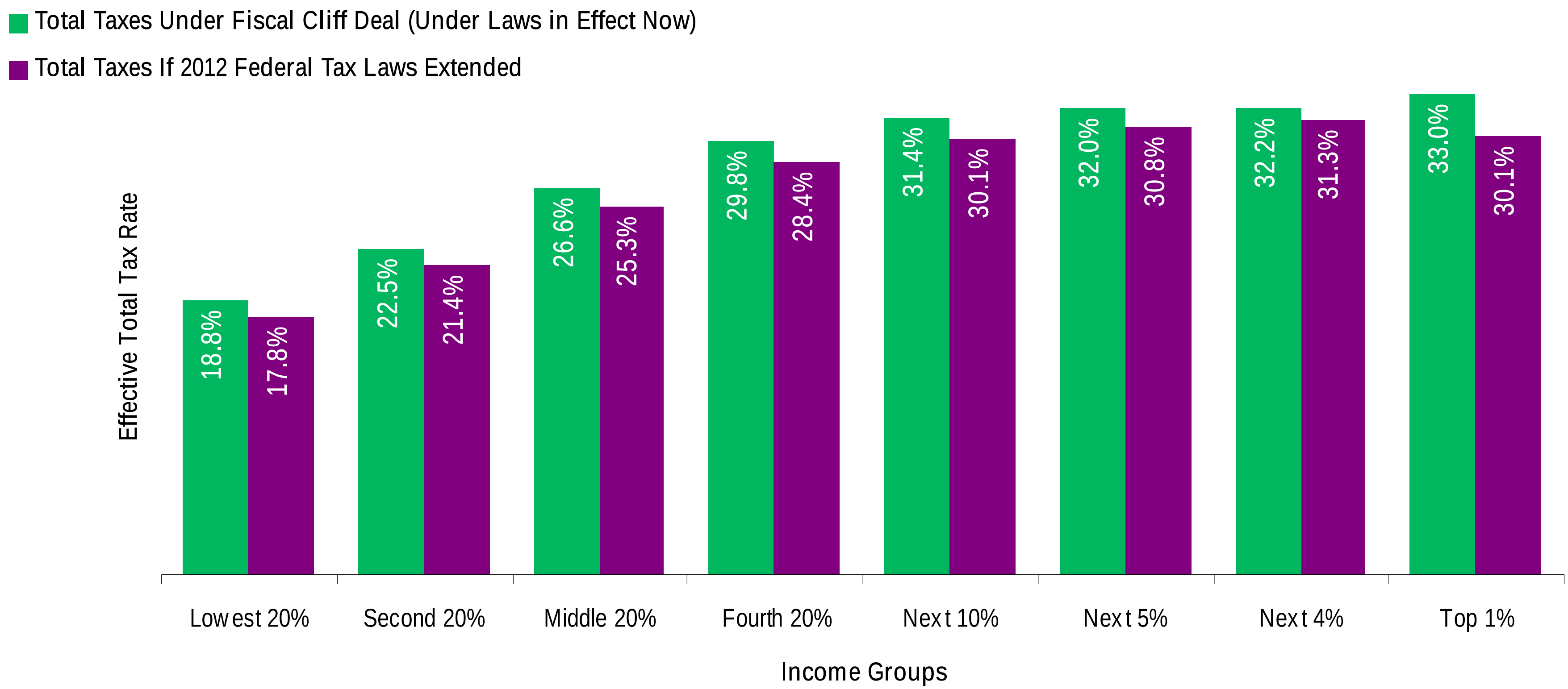
Revenue Must Come from Progressive Sources

Effective Total Tax Rates (including Federal, State & Local Taxes) in 2013 Are Slightly Higher Under Fiscal Cliff Deal than They Would Be Under 2012 Federal Tax Laws



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The Corporate Income Tax Is a Progressive Revenue Source

- Who ultimately pays the corporate tax? The shareholders who receive lower stock dividends as a result of it, and owners of business assets generally.

- Corporate lobbyists claim that the corporate income tax is ultimately paid by workers, because the tax causes investment to leave the U.S. and this depresses wages.

- If corporate CEO's didn't think their shareholders (who they answer to) ultimately paid the corporate tax, then they wouldn't lobby Congress to lower it!

- Researchers from the Congressional Budget Office, Congressional Research Service, and Tax Policy Center, conclude the vast majority of the corporate tax is borne by capital (by the owners of stocks and other business assets).

American Corporations Are Undertaxed

- CTJ’s November 2011 study looked at most of the Fortune 500 corporations that had been profitable each year from 2008-2010 and found:
  - The average effective tax rate was 18.5%.
  - For 30 corporations the average effective tax rate was negative.
  - 2/3 of the multinational corporations paid higher taxes in the foreign countries where they do business than they pay in the U.S.
  - We’ve started updating this data to cover 5 years, and so far we have similar findings…

American Corporations Are Undertaxed

A Few Examples of the Many Corporations That Paid Far Less in Federal Income Taxes than Average Americans in 2012 and/or over the Past Five Years

	2012			2008-12 Totals			Industry
$-millions	**US profit**	**Fed Tax**	**Rate**	**US profit**	**Fed Tax**	**Rate**	
Apache	$ 1,606	$ –153	–9.5%	$ 7,595	$ –169	–2.2%	Oil & gas exploration & production
Facebook*	1,062	–429	–40.4%	3,871	92	2.4%	Web-based social media
FedEx**	2,706	–135	–5.0%	6,953	–98	–1.4%	Delivery services
General Electric	7,903	651	8.2%	27,518	–3,054	–11.1%	Conglomerate (finance, aerospace, etc.)
Interpublic Group	372	–3	–0.8%	1,362	–28	–2.0%	Advertising and marketing services
Pepco Holdings	480	–76	–15.8%	1,743	–575	–33.0%	Electric utility
Principal Financial	919	–137	–14.9%	3,875	269	6.9%	Investment management
Ryder System	230	–5	–2.3%	1,073	–51	–4.7%	Truck rentals and services
Southwest Airlines	673	–45	–6.7%	2,142	156	7.3%	Airline
Tenet Healthcare	323	–3	–0.9%	905	–51	–5.6%	Health care services
Totals these 10 corps.	**$ 16,275**	**$ –335**	**–2.1%**	**$ 57,036**	**$ –3,508**	**–6.2%**	

*2010-12 for 2008-12 totals (no data for previous years).
**2011 in 2012 columns and 2008-11 for 2008-12 totals (2012 10-K annual report not yet filed).

Source: Corporate 10-K Annual Reports

Closing Corporate Offshore Tax Loopholes

- **Deferral** — the rule allowing American corporations to “defer” paying U.S. taxes on their offshore profits until those profits are “repatriated” (until those profits are brought back to the U.S.)

Closing Corporate Offshore Tax Loopholes

- Deferral encourages American corporations to:
  - *move operations (jobs) offshore* to a lower tax country
  - *artificially shift profits offshore* — in other words, tell the IRS that profits generated in the U.S. are actually generated in a country that won't tax them (an offshore tax haven).

Closing Corporate Offshore Tax Loopholes

- Example of shifting profits to tax haven:
  - U.S. corporation has a “subsidiary company” in Bermuda that is really nothing more than a post office box.
  - U.S. corporation transfers patent to subsidiary company in Bermuda for a very low price.
  - Bermuda subsidiary (which is really controlled by the U.S. corporation) charges the U.S. corporation inflated royalties for use of the patent.
  - U.S. corporation tells the IRS it has no profits because it had to pay big royalties.
  - Bermuda subsidiary (on paper) has made huge profits, but Bermuda doesn’t tax corporate profits.
  - U.S. corporation gets to “defer” the U.S. tax that would be due if the profits were properly recognized as U.S. profits.

Closing Corporate Offshore Tax Loopholes

- *The U.S. has rules to prevent this sort of abuse, but they're obviously failing.*
- For example, "transfer-pricing" rules are supposed to require the U.S. corporation in my example to charge a fair market price for the patent and require the Bermuda subsidiary to charge royalties at a fair market price.
- But when a tech company like Apple or a pharmaceutical company like Pfizer has a patent for a new invention, the IRS has no idea what the fair market price is!
- How do we know this is a problem? The profits that U.S. corporations told the IRS they had in Bermuda in 2008 equaled 1,000% of Bermuda's economy! (CRS)

Closing Corporate Offshore Tax Loopholes

- The most straightforward solution is to repeal deferral.

- Repealing deferral would ***not*** mean corporate profits would be double-taxed.

- U.S. corporations receive a credit against their U.S. taxes for taxes they pay to another country, and this would not change.

Closing Corporate Offshore Tax Loopholes

18 Companies That Likely Hold Profits in Tax Havens

Company Name	Unrepatriated Income $ Millions	Estimated Tax Bill $Millions	Implied Tax Rate
Shaw Group	$ 288	$ 111	39%
Express Scripts	66	24	37%
Amgen	22,200	7,900	36%
Advanced Micro Devices	386	137	35%
Qualcomm	16,400	5,800	35%
Gilead Sciences	7,250	2,540	35%
Wynn Resorts	334	117	35%
Eli Lilly	20,980	7,343	35%
AK Steel Holding	24	8	35%
Western Digital	6,300	2,100	33%
Tenneco	728	239	33%
Nike	5,500	1,800	33%
Dell	19,000	6,200	33%
Baxter International	10,600	3,400	32%
Microsoft	60,800	19,400	32%
Apple	82,600	26,071	32%
American Express	8,500	2,600	31%
Oracle	20,900	6,300	30%
Subtotal	**282,854**	**92,090**	**33%**

NOTE: All figures are for the end of each company's most recent fiscal year. Apple has subsequently released data for the first quarter of FY13 showing that its offshore holdings have increased to $102 billion.

Source: Most recent 10-K annual financial reports for each company

Closing Corporate Offshore Tax Loopholes

- Other proposals would be less far-reaching but still steps in the right direction:
  - Senator Carl Levin’s Cut Unjustified Loopholes Act.
  - Proposals in President Obama’s budget plans.

Stopping Proposals to Expand Corporate Offshore Tax Loopholes

- Corporate lobbyists and many lawmakers want to expand deferral into an even bigger break for corporate profits that are claimed to be "offshore."

- They want to expand deferral into an *exemption* for corporate offshore profits.

- If allowing corporations to defer U.S. taxes on their offshore profits encourages them to shift jobs and profits offshore, then *exempting* the offshore profits from U.S. taxes will logically increase those terrible incentives.

Stopping Proposals to Expand Corporate Offshore Tax Loopholes

- Proposals to *permanently* exempt offshore corporate profits from U.S. taxes are commonly called a *"territorial tax system."*

- Proposals to *temporarily* exempt offshore corporate profits from U.S. taxes are commonly called a *"repatriation holiday."*

Stopping Proposals to Expand Corporate Offshore Tax Loopholes

- The Republican chairman of the tax-writing committee in the House, Dave Camp, argues that a ***territorial system*** can have provisions that prevent offshore tax avoidance.

- But we already rules to prevent these abuses (like “transfer-pricing” rules) and they have failed.

- How could it be easier for such rules to work in a “territorial” tax system, which provides an even bigger reward for making U.S. profits appear to be “foreign” profits in a tax haven?

Stopping Proposals to Expand Corporate Offshore Tax Loopholes

- Corporate lobbyists say that making American corporations operating abroad pay U.S. taxes makes them “uncompetitive.”

- The real competition we should worry about is between domestic U.S. companies (which are often smaller) and the big multinational U.S. companies that can get a tax advantage by using tax havens.

Stopping Proposals to Expand Corporate Offshore Tax Loopholes

- Some lawmakers and lobbyists instead want to enact a *temporary* exemption for offshore corporate profits — a “repatriation holiday,” which Congress did once before in 2004.

Stopping Proposals to Expand Corporate Offshore Tax Loopholes

- Another “repatriation holiday” would increase incentives for job offshoring and offshore profit shifting.

  - One reason why the Joint Committee on Taxation concluded that a repeat of the 2004 “repatriation holiday” would cost $79 billion over ten years is the likelihood that many U.S. corporations would respond by shifting even more investments offshore in the belief that Congress will call off most of the U.S. taxes on those profits again in the future by enacting more “holidays.”

Stopping Proposals to Expand Corporate Offshore Tax Loopholes

- The Congressional Research Service concluded that the offshore profits repatriated under the 2004 tax amnesty went to corporate shareholders and not towards job creation.
  - In fact, many of the companies that benefited the most actually reduced their U.S. workforces.