

Promote Dividend Repatriation

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To stimulate the U.S. economy, enhance the competitiveness of U.S. companies, and increase federal tax revenues, we propose that a provision similar to section 965 that would promote the repatriation of dividends from foreign entities be adopted and made permanent.¹ Such a provision could be made even more effective than section 965 (and make the United States more attractive to multinationals) by not incorporating some elements of the existing statute, such as the base period limitation of section 965(b)(2).

Congress enacted section 965 as part of the American Jobs Creation Act of 2004 to encourage the repatriation of foreign earnings of controlled foreign corporations to their U.S. corporate shareholders. Subject to certain requirements, special rules, and limitations, section 965 permitted domestic corporations that were U.S. shareholders² of CFCs to elect, for one tax year, an 85

¹Other bills have been proposed that have made some modifications to the original version of section 965. In the 111th Congress, Sen. Barbara Boxer, D-Calif., and Senate Finance Committee member John Ensign, R-Nev., offered a version as a secondary amendment to H.R. 1, and House Ways and Means Committee members Kevin Brady, R-Texas, Wally Herger, R-Calif., and Sam Johnson, R-Texas, introduced a version as H.R. 507. In the 110th Congress, Ensign offered a version as an amendment to the Economic Stimulus Act of 2008 during the Finance Committee markup of that bill; then-Ways and Means member Phil English introduced a version as stand-alone legislation in H.R. 7044 and as a provision in a broader stimulus bill, H.R. 6152; and Rep. Steve King, R-Iowa, included a version as a provision in a stimulus bill introduced as H.R. 7264.

²For the general definition of U.S. shareholder, see section 951(b). For a special rule, see section 965(c)(5).

percent dividends received deduction (DRD) on certain cash dividends received during the relevant tax year from their CFCs. The DRD effectively amounted to a 5.25 percent federal tax rate on qualifying dividends — before any applicable credit that may have been permitted by section 965.³

According to IRS statistics, section 965 resulted in vast sums of foreign earnings of CFCs being repatriated back to the United States. Specifically, 843 U.S. corporations took advantage of the provision, and those corporations repatriated \$312 billion in qualified dividends for a total combined deduction of \$265 billion. Manufacturers were responsible for 81 percent of the qualifying dividends.⁴ The amount of money repatriated matched the most ambitious estimates and appears to have exceeded the expectations of Congress's official scorekeeper, the Joint Committee on Taxation, which originally predicted that the provision would raise about \$2.8 billion in new revenue in 2005. Thus, despite the 85 percent DRD, the provision resulted in an increase in federal tax revenue.⁵

A provision similar to section 965 that would promote the repatriation of dividends from foreign subsidiaries would have several demonstrably positive effects. By providing a lower effective tax rate on qualifying dividends, the proposal would help alleviate some of the implications of a complex corporate income tax system that has one of the highest corporate tax rates.⁶ It also would help alleviate the financial crisis in the

³See Notice 2005-64, 2005-2 C.B. 471.

⁴See the IRS's Spring 2008 *Statistics of Income Bulletin*.

⁵See, e.g., Robert Shapiro and Aparna Mathur, "Using What We Have to Stimulate the U.S. Economy: The Benefits of Temporary Tax Relief for U.S. Corporations to Repatriate Profits Earned by Foreign Subsidiaries," (Sonecon: Jan. 2008); and Joann M. Weiner, "Bring Back the Repatriation Tax Holiday," *Tax Notes*, Feb. 2, 2009, p. 573.

⁶The United States has one of the highest corporate income tax rates of all industrialized nations. See Figure 1 of Weiner, *supra* note 5. The 27 countries of the European Union have an average tax rate under 24 percent, with eight taxing at 20 percent or lower. The U.S. system for the taxation of the foreign business of its companies, including the repatriation of foreign profits, is more complex and burdensome than that of any of our trading partners, and perhaps more complex than that of any other country. See generally Fred Murray, ed., *The NFTC Foreign Income Project: International Tax Policy for the 21st Century*, National Foreign Trade Council, Washington, 2001. For an analysis of other measures of the high U.S. relative tax rates, including effective tax rates, on business income, see Peter R. Merrill, "Competitive Tax Rates for U.S. Companies: How Low to Go?" *Tax Notes*, Feb. 23, 2009, p. 1009; and Kevin Markle

United States and liquidity problems faced by U.S. companies by providing not only a short-term economic stimulus, but also an efficient way for U.S. companies to fund their U.S. operations over the long term. That funding could replace costly external domestic borrowing and reduce the cost of capital. That, in turn, would make U.S. companies more competitive in the global marketplace.

Another possible collateral benefit of the proposal would be a reduction in the number of companies that may consider relocating their headquarters outside the United States (possibly reversing a trend in which the United States has been losing headquarters⁷), along with decreasing the pressures on the U.S. tax system that have resulted in the enactment of anti-inversion provisions such as section 7874. The proposal would also be consistent with measures other nations are taking to change their international tax systems to promote the repatriation of foreign earnings and, in general, to try to be more attractive locations for multinationals (see, for example, the recent adoption of a foreign dividend exemption system by Japan and the United Kingdom).⁸ Moreover, despite the lower effective tax rate on qualifying

and Douglas Shackelford, "Corporate Income Tax Burdens at Home and Abroad," University of North Carolina, Jan. 30, 2009.

⁷Ominously, studies have shown for many years that the United States and Japan are tied as the least competitive G-8 countries for a multinational company to locate its headquarters, taking into account taxation at both the individual and corporate levels. See generally OECD, *Taxing Profits in a Global Economy: Domestic and International Issues* (1991). In fact, of the world's 20 largest companies (ranked by sales) in 1960, 18 were headquartered in the United States. By 2000 that number had dropped to 8. (Data provided by the International Tax Policy Forum based on an analysis of the *Forbes* International 500 list.) The location of companies' headquarters has important consequences for future domestic growth and employment trends. See Laura D'Andrea Tyson, "They Are Not Us: Why American Ownership Still Matters," *The American Prospect* (Winter 1991), pp. 37-49. (Tyson is the former chair of the Council of Economic Advisers and former chair of the National Economic Council in the Clinton administration White House.) These issues also are discussed in the NFTC report, *supra* note 6, at note 36, Volume 1, Part One, Chapter 6.

⁸Jim Carr, Jason Hoerner, and Adrian Martinez, "New Dividend Exemption Systems in Japan and the U.K.: Tax Considerations for Distributions From U.S. Subsidiaries," *Tax Management International Journal*, Bureau of National Affairs, Vol. 38, No. 6, June 12, 2009. Pursuing analogous objectives to section 965, Mexico issued a presidential decree, published in the official gazette on March 26, 2009, to encourage repatriation of funds by Mexican entities and individuals to Mexico. Under the decree, qualifying funds that are remitted to Mexico through December 31 will benefit from a 7 percent tax rate for legal entities and a 4 percent tax rate for individuals.

dividends, the proposal likely would increase U.S. tax revenue as a result of the increase in the amount of foreign earnings that would be repatriated. Finally, the proposal could require that a certain amount of the repatriated earnings be designated for national priorities (such as job creation) and could include other requirements to further promote the effectiveness of the provision and the growth of the U.S. economy.⁹

A 2009 study conducted by George Schink and Laura Tyson shows some of the benefits of a repatriation provision. The Schink-Tyson study evaluated the potential impact of a temporary repatriation proposal modeled after section 965 for purposes of stimulating the U.S. economy. The proposal would permit U.S. companies to repatriate incremental foreign earnings and pay a 5.25 percent maximum tax on the incremental repatriated earnings during 2009 and 2010.¹⁰ It also included a requirement that the funds be used for a list of permitted uses and required that a certain amount of those funds be used for national priorities.

The Schink-Tyson study concluded that: (1) the proposal would attract an estimated \$565 billion of additional repatriated earnings to the United States that would otherwise remain overseas (and contrasted that with the stimulus bill the House passed in January that calls for government spending of \$545 billion); (2) those incremental earnings would be available to support the domestic activities of U.S. companies and would have a substantial effect in 2009 and 2010, years of great vulnerability for the U.S. economy; (3) the additional funds would mean 425,000 more jobs during the 2009-2012 period, resulting from the creation of new jobs and the retention of existing jobs that would have been lost if those additional funds

⁹Some recent bills have addressed the criticism from opponents of section 965 as enacted by proposing modifications to section 965.

¹⁰George Schink and Laura Tyson, "A Temporary Reduction in Taxes on Repatriated Profits for the Purpose of Economic Stimulus and Investment in National Priorities: An Economic Assessment," LECG LLC, Jan. 30, 2009. The rate reduction in the proposal was accomplished by excluding 85 percent of the incremental repatriated earnings from taxation. The remaining 15 percent would be taxed at the 35 percent tax rate adjusted downward to reflect foreign taxes already paid on those earnings. The "incremental" repatriation would be defined as repatriations in excess of "normal" repatriations over the last six years. The proposal elaborates on this definition.

were not available¹¹; and (4) the proposal would increase rather than reduce federal government revenue.¹²

The proposal included a requirement that at least 5 percent of the incremental repatriated earnings be committed to investment in national priority areas, including renewable energy projects, energy efficiency projects, healthcare initiatives, and broadband development. The Schink-Tyson study concluded that if, as expected, the temporary tax relief were to attract \$565 billion of incremental repatriated earnings, the commitment would generate an additional \$28 billion of investment in those areas.¹³ ■

¹¹See Allen Sinai, "Macroeconomic Effects of Reducing the Effective Tax Rate on Repatriated Foreign Subsidiary Earnings in a Credit- and Liquidity-Constrained Environment," Decision Economics Inc., New York, Jan. 30, 2009.

¹²For a discussion of the increased revenue, see p. 14 of Schink and Tyson, *supra* note 10.

¹³See pp. 3-4 of Sinai, *supra* note 11.