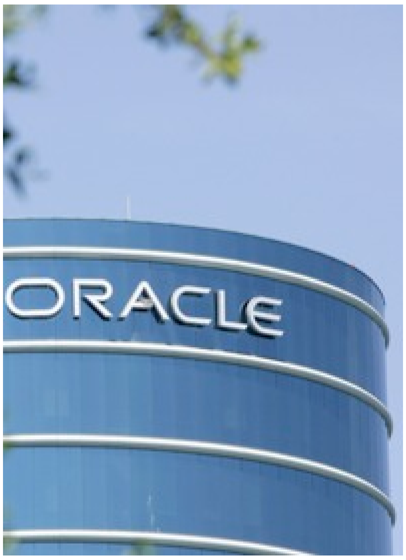
Trillion-dollar Tax Holiday Sought by Multinationals



Hers is only one of many large multinational corporations with large profits (estimated at $1 trillion) languishing abroad, owing to to the 35 percent corporate tax that would be levied if those funds were brought back to the United States. Others backing the proposal are Cisco, Apple, Duke Energy, and Pfizer. It's an effort that began last fall when it became clear that there would likely be serious efforts in the new 112th Congress to grow the economy and slow down the growth of deficit spending.

This isn't the first time such an idea has been considered. In 2004, a multinational "tax holiday" was enacted, and 843 corporations repatriated some $362 billion in profits from their foreign operations, generating nearly $20 billion in revenues for the Treasury. The opportunity was especially attractive because the tax rate was reduced from the usual 35 percent rate to just 5.25 percent if the companies acted within a year of passage of the act.

Naturally, Congress was interested in making sure that such repatriation would in fact go to creating new jobs, and so wrote legislation to go along with the tax break requiring those companies taking advantage of the break to invest in "hiring and training U.S.-based workers, investing in infrastructure located in the United States, research and development, and marketing performed in the United States." The legislation specifically barred any repatriated earnings from being spent on executive compensation, shareholder dividends, or stock buy-backs.

Naturally, once the funds were deposited in the United States, and the tax liabilities paid, the companies determined the best use of those funds. To the chagrin of those trying to direct the activities of the multinationals into areas where they would "do the most good," the multinationals instead put most of the money into the pockets of its shareholders (the owners of the companies). According to the National Bureau of Economic Research, for every dollar "repatriated" under the tax holiday, between 60 and 92 cents was paid out in dividends to the companies' shareholders.

This outraged the statists and planners who were looking for a way to use other peoples' money to accomplish their purposes. Because the same sort of dividends would likely be paid out this time around, they are opposing the current efforts for another tax holiday. In a study from the Center on Budget and Policy Priorities, it was claimed that the 2004 tax holiday "failed as a stimulus" and that if another tax holiday was allowed, "the firms would likely retain the repatriated earnings … rather than spend them on domestic investment or hiring." In a classic example of the error in logic known as "post hoc, ergo propter hoc" (after this, therefore because of this), CBPP "found that many firms laid off workers even as they reaped substantial benefits from the tax holiday and [instead] passed them on to shareholders."

> Pfizer, for example, which took advantage of the [holiday] and repatriated the largest amount (around $37 billion), started a number of layoffs in its U.S. workforce (around 3,500 jobs) and closed U.S. factories in 2005.
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> Other companies that took advantage of the holiday but laid off workers shortly thereafter included Ford Motor Company (which repatriated about $850 million under the holiday but then began laying off about 10,000 workers in 2005), Merck (which repatriated $15.9 billion but announced layoffs of 7,000 workers in 2005), Motorola, Proctor and Gamble, PepsiCo, and Honeywell International.

Oracle President Catz properly dismissed such attempted connections between repatriation of funds under the tax holiday and company layoffs. She said that many of those firings were due to mergers, and added, "It also rained for a full month [after the money came back] but repatriation didn't make it rain, either."

The conclusion from CBPP was revealing in its bias and lack of understanding about how markets are supposed to work: "In short, the evidence suggests that the [2004] repatriation tax holiday failed in its objective to encourage firms to increase their U.S. investment and hiring. Instead, these firms — predominately large multinational corporations — effectively passed the earnings repatriated under the holiday to their shareholders."

Imagine that. A company, owned by shareholders, hires expert managers to try to make profits offering products and services to its customers. When such a company succeeds, it invests some, much, or most of those profits back into new facilities and workers in order to take advantage of its opportunities. The owners of the company wait patiently on the sidelines for a return on their investment.

Along comes a government that so highly taxes those profits that the company decides not to return them to the company, but keeps them in a lower-tax country, awaiting, hopefully, other better opportunities to invest them.

When an opportunity arrives in the form of a tax holiday, the managers of the company decide to take advantage of it, and then return a portion of those profits that have been languishing offshore, perhaps for years, to its rightful owners: the shareholders!

Unfortunately, Catz and her other supporters of a tax holiday are going to find this a very long row to hoe. Supporters of government intervention and anti-capitalist ideologies have great sway in today's world. It's likely that the National Federation of Independent Business (NFIB) will complain that such a holiday is just another "payoff" for big business, failing to recognize the every one of its small business owners would most certainly like to be big someday, and have problems like that. No doubt the U.S. Chamber of Commerce will have its say in the matter, and liberal majorities in the Senate and the President will likely keep this from happening.

But the issue of a tax holiday raises other interesting questions. What if the corporate tax rate was permanently reduced to zero? After all, who pays those corporate taxes anyway — ultimately it's the consumer. Corporations are merely tax funnels. And imagine how the economic decisions would be impacted if a company could make its plans without having to consider the onerous, eternal, and ever-changing rules of the IRS. Think of how productive a company might become if substantially more of its time, effort, and capital were invested in developing and improving products for its customers. Given what is known of how the free market works when it is left alone, wouldn’t investment in capital increase, demand for skilled workers increase, and standards of living for all the citizens increase?

Perhaps a tax holiday — permanent and for everyone — isn’t such a bad idea after all.

Photo: AP Images