2011

Corporate America Untaxed

Tax Avoidance on the Rise

SAMUEL KANG General Counsel and TUAN NGO Legal Associate | The Greenlining Institute

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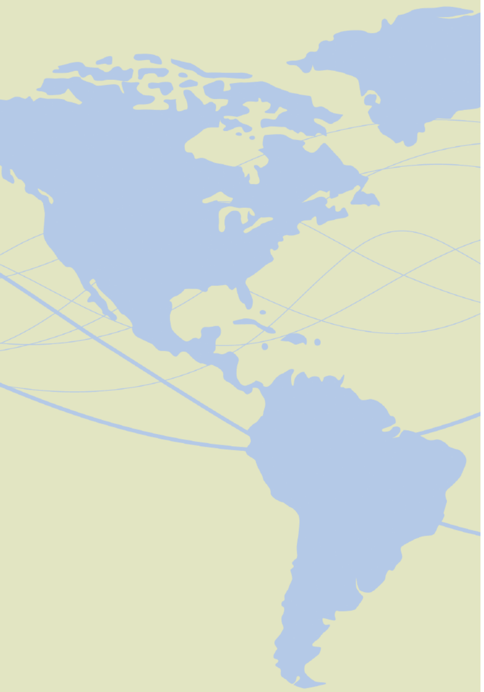

About the Greenlining Institute

The Greenlining Institute is a national policy, research, organizing, and leadership institute working for racial and economic justice. We ensure that grassroots leaders are participating in major policy debates by building diverse coalitions that work together to advance solutions to our nation's most pressing problems. Greenlining builds public awareness of issues facing communities of color, increases civic participation, and advocates for public and private policies that create opportunities for people and families to make the American Dream a reality.

About Greenlining's Consumer Protection Program and Our Legal Team

Led by General Counsel Samuel Kang, Greenlining uses in house legal experts to ensure that there is equity in the state's energy, telecom, and cable industries. Greenlining's legal team is one of the few active racial justice advocates at the California Public Utilities Commission, the Federal Communications Commission, and other regulatory bodies.

They work closely with grassroots leaders to ensure that the needs and solutions of communities of color are represented in the halls of these commissions. Greenlining plays a critical role in ensuring that California's regulated companies remain leaders on issues of diversity and economic equity. In addition, our legal team builds bridges between grassroots leaders and corporate CEOs to ensure that positive dialogue leads to win win solutions.

About the Authors

Samuel S. Kang, General Counsel
Sam's primary responsibility is to craft strategies that maximize the organization's cooperative opportunities, or in the alternative, compel adversarial compliance. He has led several successful campaigns impacting state and national policy. Sam engages directly with the heads of federal and state regulatory agencies, corporate executives, and community leaders. He also provides strategic guidance to members of the California legislature and U.S. Congress. Sam has been interviewed and quoted in dozens of media outlets across the country including the Los Angeles Times, San Francisco Chronicle, Sacramento Bee, Philadelphia Inquirer, and CBS. Prior to Greenlining, Sam worked at several NGOs on issues ranging from Iraqi sanctions enforcement to economic development in New York's West Harlem neighborhood. He was previously a Coro Fellow and recognized as one of the top young Korean American leaders in the United States.

Tuan Ngo, Legal Associate
Tuan is from Santa Ana, California and currently attends the University of California, Hastings, where he will receive his J.D. in 2013. Tuan earned his B.A. in Diplomacy and World Affairs from Occidental College and has worked for the Tides Foundation in San Francisco. He was a 2007-08 Coro Fellow. In 2003, Tuan founded a Leprosy English Camp that benefited over 100 youth whose family members were affected by leprosy in the Surin province of Thailand. He is also an advocate stateside as Chair of the Queer-Straight Alliance and the Asian Pacific Island Association. Tuan is also a board member of the Vietnamese American Bar Association of Northern California.

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Executive Summary

- In 2010, U.S. corporations avoided approximately $60 billion in U.S. corporate income taxes by using a variety of devices and gimmicks to shift profits to foreign subsidiaries, while the Fortune 100 companies received some $89.6 billion in federal contracts.

- Since the Government Accountability Office reviewed this issue in 2008, top companies have added 44 new subsidiaries in countries identified by the GAO as tax havens.

- The lost revenue would be more than enough to fund the entire budgets of the Environmental Protection Agency and the Departments of Energy and Labor ***combined.***

- One recent study found that eight of the top 12 companies effectively paid no federal income taxes from 2008 through 2010. In 2010, General Electric paid no federal income tax.

- The official U.S. corporate tax rate of 35 percent largely exists in name only. The U.S. collects less in corporate taxes as a share of GDP than 24 out of 26 industrialized countries.

- The share of the federal budget funded by corporate income taxes has dropped dramatically since the 1940s, from 28.8 percent of the budget to 10.3 percent.

- Of the 77 Fortune 100 companies with subsidiaries in tax haven countries, 69 had federal contracts. The largest in terms of dollar amounts was General Dynamics, with nearly $15 billion in federal contracts and 14 subsidiaries in tax haven or financial privacy jurisdictions.

- The pharmaceutical and tech sectors loom particularly large, including Merck, Pfizer, General Electric, Dell and Google. G.E., paying essentially no federal tax, had over $3 billion in federal contracts.

- Google's "Double Irish Dutch Sandwich" illustrates the convoluted mechanisms used to hide profits overseas. Many other strategies are also used.

Methodology

This study paralleled the methodology of the GAO Report in 2008, "Large U.S. Corporations and Federal Contractors with Subsidiaries in Jurisdictions Listed as Tax Havens or Financial Privacy Jurisdiction," including the definitions of tax havens. We updated the corporations covered to match the 2011 Fortune 100 list. This report does not attempt to determine whether corporations or contractors engaged in transactions with subsidiaries specifically to reduce taxes. The existence of subsidiaries in jurisdictions listed as tax havens does not prove that a corporation or contractor established that subsidiary for the purpose of reducing its tax burden. Research and literature review, however, do suggest a strong relationship.

Introduction

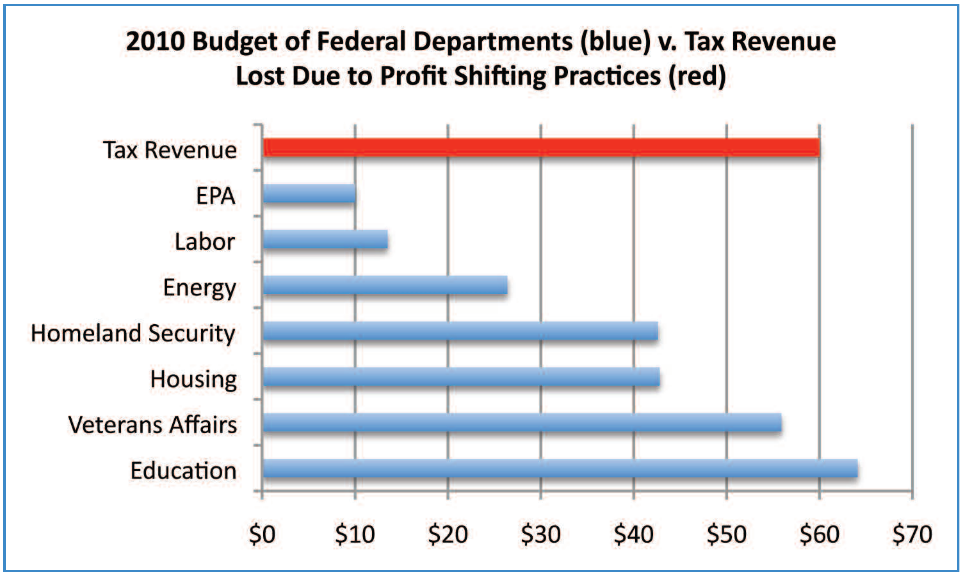
"Tax issues associated with the transfer of intangibles outside the United States have been a high risk compliance concern for us and have seen a significant increase in recent years. Taxpayers, especially in the high technology and pharmaceutical industries, are shifting profits offshore."

Mark Everson, *IRS Commissioner,* June 13, 2006

With efforts to cut the federal budget deficit dominating Washington headlines, the use by major corporations of legal gimmicks and devices to avoid federal taxes is getting increased attention. In 2010 the Fortune 100 American corporations reported $6.7 trillion in worldwide revenue and received $89.6 billion worth of taxpayer-funded federal contracts, while U.S. companies avoided $60 billion in taxes by shuttling profits offshore. This comes at a time when a variety of programs critical to American families are potentially on the chopping block, including Medicare, Social Security, food safety, mass transit, public elementary and secondary education, workplace safety, and law enforcement. These cuts threaten millions of Americans who saw their wealth dwindle even before the 2008 market meltdown.[1]

Much has been made of the 35 percent U.S. corporate income tax rate, but by moving profits offshore, many of America's largest companies pay an effective tax rate that is far lower – zero in some cases. The $60 billion in corporate income tax revenue lost annually to the offshoring of profits would be ***more than enough to fund the annual budgets of the Environmental Protection Agency and the Departments of Labor and Energy combined.*** Alternatively, it would be enough to pay 1.2 million public school teachers for a year or cover public college tuition for more than 8.5 million students.

Because the economic world has changed drastically in the last three years, this report updates and extends a 2008 report conducted by the Government Accountability Office (GAO) that ranked the Fortune 100 corporations by the number of foreign subsidiaries in tax haven countries and by the amount they earned from taxpayer-funded contracts awarded by the federal government.[2] With trillions of dollars in cuts to vital programs under consideration, it is time to ask: ***Are large corporations paying their fair share of taxes?***



Corporate Profits: The Untaxed Americans

While many Americans struggled, the Fortune 100 companies last year posted $6.7 trillion in worldwide revenue. But many will avoid paying anything close to the 35 percent statutory corporate income tax rate by employing complicated tricks to move profits offshore. Some multinationals will pay nothing, including General Electric, which did not pay any federal income tax in 2010.[3] And GE is not an exception. A study by economist Robert McIntyre reported that of the top twelve U.S. corporations, eight effectively paid nothing to the U.S. government in taxes from 2008 through 2010, while these twelve companies reported a collective $171 billion in pretax U.S. profits.[4]

Despite having the second highest corporate income tax rate in the world, the U.S. collects less in corporate taxes as a share of its GDP than all but two of the 26 developed countries, Chile and Mexico.[5] Countries with higher corporate tax collection as a percentage of GDP include Germany, the United Kingdom, and South Korea. A report by the GAO found that the average U.S. effective tax rate on domestic income of large corporations in 2004 was an estimated 25.2 percent.[6] The figure could now be as low as 18.4 percent according to a study by economist Robert McIntyre.[7]

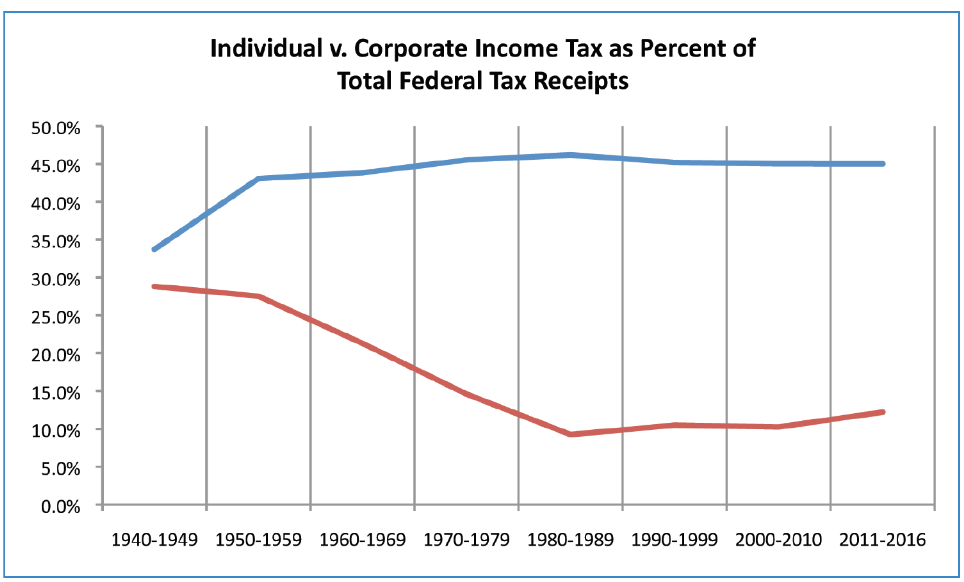
> "The issue of corporations paying no tax or little tax in the United States, when the majority of their operations are here, is problematic. The problem is that this is sort of the level of micro that people don't look at."[8]
>
> **Mark Skoda, *Chairman and founder of the Memphis Tea Party***

Trickle-Up Economics

America's weak economic recovery has benefitted some more than others. Since the recovery began in June 2009, "corporate profits captured 88 percent of the growth [while] aggregate wages and salaries accounted for only slightly more than 1 percent of growth."[9]

While receiving a tiny share of recent economic growth, individual taxpayers are contributing a far larger share of the federal budget than corporations: 42 percent of the 2010 federal budget, as compared to corporate America's nine percent. In dollar amounts, individuals paid $915 billion, six times corporations' $138 billion.[10]

Meanwhile, taxpayers contribute greatly to rising corporate profits. In 2010, American taxpayers – firefighters, teachers, nurses, plumbers, doctors – invested $89.6 billion in government contracts awarded to the Fortune 100 companies, including many that are avoiding U.S. taxes by shifting profits overseas.



Individual v. Corporate Income Tax as Percent of Total Federal Tax Receipts

Year	Individual income tax rate as % of total revenue	Corporate income tax rate as % of total revenue
1940-1949	33.7%	28.8%
1950-1959	43.1%	27.5%
1960-1969	43.9%	21.3%
1970-1979	45.5%	14.6%
1980-1989	46.2%	9.3%
1990-1999	45.2%	10.5%
2000-2010	45.1%	10.3%

Source: Data provided by The White House's Office of Management and Budget. www.whitehouse.gov/omb/budget/historicals. The data does not include percentages for social insurance and retirement receipts, excise taxes, and "other" taxes, which together with individual income and corporate income tax would add up to 100 percent.

Results

FOREIGN SUBSIDIARIES BY THE NUMBERS

Seventy-seven of the 100 largest corporations in terms of 2010 revenue reported having subsidiaries in jurisdictions listed as tax havens or financial privacy jurisdictions ("tax havens"), as defined and listed in the GAO 2008 report.[11] Sixty-nine of the 77 had federal contracts, with values ranging from $12,000 to $15 billion, in fiscal year 2010.

Eighty-five of the 100 largest corporations had foreign subsidiaries and 12 did not (3 companies did not have foreign subsidiaries information available). The 85 corporations had a total of 9,563 foreign subsidiaries (281 more than 2008) and of these, 2,365 are located in tax haven jurisdictions (44 more than 2008).

Fifty-two corporations added at least one subsidiary in tax haven countries and twenty-one companies reduced their subsidiaries in tax haven countries by at least one between 2008 and 2010. Each company added on average 2.9 foreign subsidiaries and 0.5 in a tax haven country between 2008 and 2010. The outlier is CitiGroup, which decreased their number of foreign subsidiaries by 1,129 between 2008 and 2011. Of these, 404 are identified as tax havens. If CitiGroup is removed from the data set, the averages change significantly. On average, each company added 14.7 foreign subsidiaries between 2008 and 2011; each company, on average, added 4.7 in tax havens.

(NOTE: Companies only have to list "significant subsidiaries" (defined by specific criteria) in their SEC 10-K filings and may omit any subsidiary which, considered in the aggregate, does not constitute a significant subsidiary. Therefore, the actual number of subsidiaries or foreign branches may be significantly higher than the figures listed here. At least one of the Google subsidiaries described in the "Profit Shifting 101" section below does not qualify as "significant" by federal standards.)

Summary Changes in Significant Foreign Subsidiaries and Significant Subsidiaries in Tax Haven Countries (2008-2010)

	Significant Foreign Subsidiaries		Significant Foreign Subsidiaries in Tax Havens	
	Foreign subsidiaries (2010)	Change in foreign subsidiaries (2008-2010)	Subsidiaries in tax havens (2010)	Change in subsidiaries in tax havens (2008-2010)
Sum Total of Significant Subsidiaries	**9563**	+279	**2365**	+44
Average # of Significant Subsidiaries	**98.6**	+2.9	**24.4**	+0.5
Median # of Significant Subsidiaries	**27**	0	**7**	1

Five of the 77 corporations that had subsidiaries in tax haven jurisdictions had more than 100 subsidiaries in such jurisdictions. The number of subsidiaries in jurisdictions listed as tax havens or financial privacy jurisdiction ranged from one for four corporations to a high of 341 for one corporation. Eighteen corporations had 50% or more of their foreign subsidiaries in jurisdictions listed as tax havens or financial privacy jurisdictions.

The Top Corporations with the Highest Numbers of Significant Subsidiaries in Tax Haven Countries

Corporation	# of significant subsidiaries in tax havens	Change in # of significant subsidiaries in tax havens (2008-2010)	Revenue	Federal contract obligations
Bank of America	341	226	$134,194,000,000	$8,217,232
Morgan Stanley	297	24	$39,320,000,000	$15,718,864
News Corp.	127	-25	$32,778,000,000	$3,064,717
PepsiCo	114	44	$57,838,000,000	$217,345,182
Pfizer	106	26	$67,809,000,000	$993,344,145
Merck	97	53	$45,987,000,000	$992,878,809
J.P. Morgan Chase	81	31	$115,475,000,000	$73,252,830
Oracle	78	1	$26,820,000,000	$239,094,305
Abbott Laboratories	71	35	$35,167,000,000	$73,593,104
Kraft Foods	70	34	$49,542,000,000	$373,035,722
Marathon Oil	61	-15	$68,413,000,000	$3,932,716
Dow Chemical	54	19	$53,674,000,000	$10,743,692
Wells Fargo	49	31	$93,249,000,000	$5,027,389
Procter & Gamble	42	-41	$79,689,000,000	$174,411,000
Boeing	40	2	$64,306,000,000	$174,402,717
Cisco Systems	39	1	$40,040,000,000	$8,660,186
Johnson & Johnson	39	1	$61,587,000,000	$120,417,358
Caterpillar	38	-11	$42,588,000,000	$699,812
Prudential Financial	38	11	$38,414,000,000	$199,812,476
Goldman Sachs	37	8	$45,967,000,000	$79,346
Total	**1819**	**455**	**$1,192,857,000,000 [$1.2 trillion]**	**$3,687,731,602 [$3.7 billion]**

In 2010 seven jurisdictions listed as tax havens had more than 100 corporate subsidiaries, ranging from 179 in Switzerland to 580 in the Cayman Islands. Two corporations, Morgan Stanley and Bank of America, owned a total of 373 out of the 580 subsidiaries in the Cayman Islands. In 2008, eight jurisdictions had more than 100 corporate subsidiaries, ranging from 123 to 569. For the jurisdiction with 569 subsidiaries, 372 were owned by four corporations.

The high number of corporate subsidiaries concentrated in seven tax haven jurisdictions line up with the IRS data revealing that most of the dividends that came back to the U.S. during the 2004 one-time tax holiday (which allowed corporations to bring offshore earnings back to the U.S. at 5.25 percent) came from extremely low-tax countries, including the Netherlands, Switzerland, Bermuda, and Ireland.[12]

Top 7 Tax Haven Jurisdictions Where Corporations Have Subsidiaries as of 2010

Jurisdictions listed as tax havens	# of significant corporate subsidiaries
Cayman Islands	580
Ireland	287
Luxembourg	245
Hong Kong	206
Singapore	185
Bermuda	184
Switzerland	179
Total	**1866**

Locations of Dividends Repatriated During 2004 Tax Holiday: Countries Accounting for at Least 1% of Dividends (These Countries accounted for 87% of the total amount of money repatriated)

Netherlands	28.80%
Switzerland	10.40%
Bermuda	10.20%
Ireland	8.20%
Luxembourg	7.50%
Canada	5.90%
Cayman Islands	5.90%
United Kingdom	5.10%
Hong Kong	1.70%
Singapore	1.70%
Malaysia	1.20%

Source: Internal Revenue Service, cited in Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion."

CONTRACTORS BY THE NUMBERS

Sixty-nine corporations that reported receiving federal contracts in fiscal year 2010 also had subsidiaries in jurisdictions listed as tax havens or financial privacy jurisdictions. These 69 corporations received a total $45.4 billion in federal contracts (close to half of the $89.6 billion that all Fortune 100 corporation received) and together had 2,292 subsidiaries in jurisdictions listed as tax havens or financial privacy jurisdictions. The contract amounts range from a low of $12,000 to a high of $15 billion. These 69 corporations reported over $4.7 trillion in revenue in fiscal year 2010 before tax. Fifty-seven of the 69 corporations with both federal contracts and tax haven subsidiaries received more than $1 million in federal contracts in 2010.

Tax Avoiders with Federal Contracts (2010)

Corporation	Federal contract obligations for fiscal year 2010*	Federal contract obligations for fiscal year 2007**	# of significant foreign subsidiaries	# of significant subsidiaries in tax havens
General Dynamics	$15,045,973,553	$14,771,780,475	64	14
United Technologies	$7,655,549,679	$5,909,541,140	73	11
McKesson	$4,601,029,713	$3,716,550,693	2	2
General Electric	$3,072,873,259	$3,136,076,490	57	14
Honeywell Int'l	$2,554,725,867	$1,406,022,372	27	5
Hewlett-Packard	$1,818,560,724	$2,888,122,686	92	17
IBM	$1,650,362,395	$1,557,715,071	85	14
Dell	$1,447,149,023	$1,078,042,002	188	35
Pfizer	$993,344,145	$575,802,321	438	106
Merck	$992,878,809	$1,402,363,446	478	97
Oracle	$239,094,305	$169,940,870	328	78
Dow Chemical	$10,743,692	$4,288,310	451	54
Cisco Systems	$8,660,186	$8,498,124	224	39
Apple	$3,508,651	$2,222,746	2	2
Google	$121,867	$150,695	2	2
Goldman Sachs	$79,346	$274,957	52	37
Total	**$40,094,655,214 [$40.1 billion]**	**$36,627,392,398 [$36.6 billion]**	**2563**	**527**

Source: Federal contract obligations can be found at USA Spending, www.usaspending.gov

*The assistance prime awardee data includes agency submissions as of 07/20/2011 and the contracts prime awardee data includes procurement data downloaded from FPDS as of 07/18/2011. Current figures are underestimates, as not all data has been reported.

**Federal contract obligations for fiscal year 2007 reported in GAO Report have been updated as of July 21, 2011.

ANALYSIS OF THE TOP THREE SECTORS

Financial Services Sector: This sector has a total of 2,054 foreign subsidiaries, 873 of which are in tax haven countries. The sector posted $720.9 billion in total revenue and received $244.6 million in taxpayer funded contracts in 2010.

Pharmaceuticals & Chemicals Sector: This sector has a total 1,958 foreign subsidiaries, 393 of which are in tax haven countries. The sector posted $693 billion in total revenue and received over $9.3 billion in taxpayer funded contracts in 2010.

Technology Sector: This sector has a total 1,092 foreign subsidiaries, 242 of which are in tax haven countries. The sector posted $775 billion in total revenue and received over $8.3 billion in taxpayer funded contracts in 2010.

Financial Services Sector (2010)

Corporation	# of significant subsidiaries in tax havens	# of significant foreign subsidiaries	Revenue	Federal contract obligations
Bank of America Corp.	341	745	$134,194,000,000	$8,217,232
Morgan Stanley	297	597	$39,320,000,000	$15,718,864
J.P. Morgan Chase & Co.	81	217	$115,475,000,000	$73,252,830
Wells Fargo	49	97	$93,249,000,000	$5,027,389
Goldman Sachs Group	37	52	$45,967,000,000	$79,346
American International Group	25	99	$104,417,000,000	$34,618,009
Citigroup	23	111	$111,055,000,000	$107,286,602
American Express	15	113	$30,242,000,000	$417,245
INTL FCStone	5	23	$46,940,300,000	$0
Total	**873**	**2054**	**$720,859,300,000**	**$244,617,517**
			[$720.9 billion]	**[$244.6 million]**

Pharmaceuticals & Chemicals Sector (2010)

Corporation	# of significant subsidiaries in tax havens	# of significant foreign subsidiaries	Revenue	Federal contract obligations
Pfizer	106	438	$67,809,000,000	$993,344,145
Merck	97	478	$45,987,000,000	$992,878,809
Abbott Laboratories	71	289	$35,166,700,000	$73,593,104
Dow Chemical	54	451	$53,674,000,000	$10,743,692
Johnson & Johnson	39	182	$61,587,000,000	$120,417,358
DuPont	12	51	$32,733,000,000	$5,089,245
Cardinal Health	11	41	$98,601,900,000	$890,593,486
McKesson	2	2	$108,702,000,000	$4,601,029,713
Medco Health Solutions	1	24	$65,968,300,000	$664,425
AmerisourceBergen	0	0	$77,954,000,000	$1,330,710,283
Express Scripts	0	2	$44,989,700,000	$321,656,947
Total	**393**	**1958**	**$693,172,600,000**	**$9,340,721,207**
			[$693 billion]	**[$9.3 billion]**

Technology Sector (2010)

Corporation	# of significant subsidiaries in tax havens	# of significant foreign subsidiaries	Revenue	Federal contract obligations
Oracle	78	328	$26,820,000,000	$239,094,305
Cisco Systems	39	224	$40,040,000,000	$8,660,186
Dell	35	188	$61,494,000,000	$1,447,149,023
Ingram Micro	27	87	$34,589,000,000	$0
Hewlett-Packard	17	92	$126,033,000,000	$1,818,560,724
General Electric	14	57	$151,628,000,000	$3,072,873,259
IBM	14	85	$99,870,000,000	$1,650,362,395
Intel	8	20	$43,623,000,000	$2,738,740
Microsoft	4	5	$62,484,000,000	$105,175,653
Apple	2	2	$65,225,000,000	$3,508,651
Amazon.com	2	2	$34,204,000,000	$329,285
Google	2	2	$29,321,000,000	$121,867
Total	**242**	**1092**	**$775,331,000,000**	**$8,348,574,088**
			[$775.3 billion]	**[$8.3 billion]**

Profiting Shifting Favors the Pharmaceutical and Technology Sectors

The current corporate tax system makes it easier for pharmaceutical and technology companies to shift intellectual property and manufacturing to low-tax countries, as compared to industries where customers and the provision of services are largely domestic.[13] As a result, domestic-to-foreign profit shifting has accelerated in recent years among American pharmaceutical and high-tech firms, which have seen their effective tax rates decline drastically.

In a study of nine large U.S. drug companies, economist Martin Sullivan found that in 1999 these corporations' foreign profits accounted for 39.2 percent of worldwide profits, but by 2005 their foreign profits jumped to 69.9 percent.[14] Profit shifting to low and no-tax countries helped these corporations cut their effective tax rate down to 23 percent by 2003 from 27.2 percent in 1999.[15] Collectively, these drug companies had total pretax profits of $42.6 billion in 2005. If 23 percent of which were repatriated back to the United States and taxed at an average rate of 30 percent, the treasury would take in an additional $2.9 billion in just one year from only nine companies.[16]

Who Wins and Loses Under Current Tax System (as of 2006)[17]

Pharmaceuticals & Technology Companies	Effective Tax Rate	Other Companies	Effective Tax Rate
Cisco Systems	19.80%	CVS Caremark	38.80%
General Electric	3.60%	Disney	36.50%
Hewlett Packard	20%	Home Depot	35.40%
Johnson & Johnson	22%	Target	37.20%
Merck	12.50%	United Health Group	35.40%
Pfizer	17.10%	Wal-Mart	33.60%

Source: Martin A. Sullivan, "Drug Firms Move Profits to Save Billons," Tax Notes, August 7, 2006

CORPORATIONS AVOIDING TAXES WHILE RECEIVING TAXPAYER FUNDED CONTRACTS

Fortune 100 corporations reported $6.7 trillion in total worldwide revenue in 2010. Seventeen companies (see table below) had $163 billion in profits; yet they paid an average effective tax rate of 17.9 percent (average effective tax rate between 2008 through 2010 is 18.4 percent), much lower than the 35 percent statutory rate. At the same time, these corporations received $3.1 billion in taxpayer funded contracts. As of December 30, 2010, these companies earned a total of $463.9 billion from foreign subsidiaries overseas (offshore cash). Foreign profits eclipsed U.S. profits, making up 53% of worldwide income ($86.3 billion).[18]

Taxes, Profits, and Undistributed (i.e. not returned to the U.S.) Foreign Earnings (Amounts are for 2010 and in millions unless otherwise noted)

Corporation	Undistributed earnings of profits from foreign subsidiaries	US Profit Before Taxes	Foreign Profit Before Taxes	Worldwide Profit Before Taxes	Average World ETR (2008-2010)
General Electric	$94,000	$5,078	$9,130	$14,208	0.5%
Pfizer	$48,200	-$2,477	$11,899	$9,422	16.4%
Merck	$40,400	$1,154	$499	$1,653	25.2%
Cisco Systems	$31,600	$1,102	$8,313	$9,415	19.8%
IBM	$31,100	$9,140	$10,583	$19,723	25.7%
Apple	$30,800	$5,540	$1,300	$18,540	29.3%
Microsoft	$29,500	$9,575	$15,438	$25,013	25.8%
Abbott Laboratories	$26,800	-$275	$5,988	$5,713	19.4%
Hewlett-Packard	$21,900	$4,027	$6,947	$10,974	19.8%
Oracle	$21,000	$4,282	$3,961	$8,243	27.9%
Bank of America*	$17,900			-$1,323	-33.2%
Goldman Sachs *	$17,700			$8,354	22.8%
Google	$17,500	$4,948	$5,848	$10,796	19.6%
Dell	$12,300			$2,024	25.9%
Intel	$11,800	$13,926	$2,119	$16,045	27.7%
Dow Chemical	$9,800	-$821	$3,623	$2,802	15.8%
Amazon.com	$1,600	$886	$611	$1,497	24.3%
Total	**$463,900**	**$56,085**	**$86,259**	**$163,099**	**18.4%**

*Did not separate profits by U.S. and foreign profits

Profit Shifting 101:
How to Make Profits Invisible to the IRS

> "A very significant part of this accumulation of profits offshore is the artificial shifting of profits using transfer pricing [and] there's been a significant increase in its aggressiveness over the past decade."[19]
>
> **Martin Sullivan, *Tax economist, former employee of the Treasury Department & Arthur Andersen LLP***

Using techniques to move profits to tax haven countries, U.S. companies amassed at least $1 trillion in foreign profits that are not taxed in the U.S. and will cost the U.S. government $199 billion in revenue from 2011 through 2015. This section illustrates how multinationals amass large profits that go untaxed in the United States, using Google Inc.'s "Double Irish Dutch Sandwich" structure as an example of an easily-replicable structure similar to what many U.S. multinationals are using, including Pfizer and Facebook.[20]

PROFIT SHIFTING: TRANSFER PRICING & EARNINGS STRIPPING

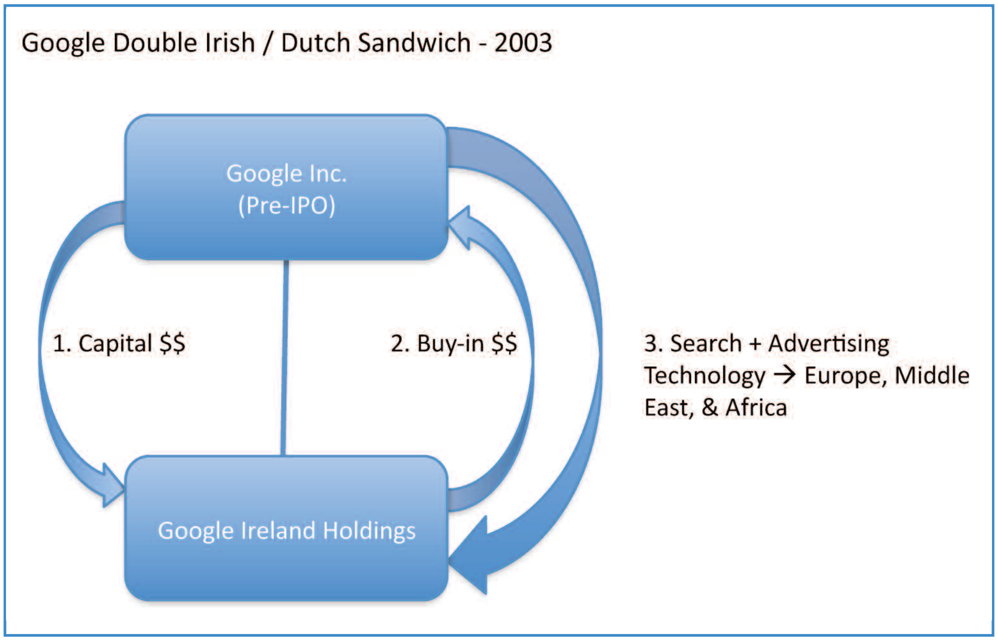
Transfer pricing describes the process by which subsidiaries of multinational corporations "deal with each other for the purpose of determining the income of each of the [entities]."[21] Using transfer pricing, companies like Google can lower their taxes by shifting profits from the U.S. to countries that have lower tax rates. The transaction is a paper transaction between Google, located in Mountain View, California, and its subsidiaries in Ireland, allowing Google to allocate expenses and profits among different countries. For instance, when Google Inc. licenses its patents to offshore subsidiaries in a low-tax country like Ireland, profits from sales overseas are recognized by the Irish subsidiary, not the U.S. parent.

STEP 1: Creating the Foreign Subsidiary

In 2003, a few months before its initial public offering, Google Inc. created a wholly-owned Irish subsidiary, Google Ireland Holdings ("Ireland Holdings"), for which it had provided start-up capital. Ireland Holdings can conduct business independent of the parent company and take business risks that the parent company is not liable for. Google commenced its Irish operations in 2003 with five employees.[22]

STEP 2: "Arms-Length Exchange" Contract: A Sweetheart Deal[23]

Ireland Holdings then entered into an agreement with Google Inc. to acquire the rights to Google's search and advertising technologies and other intangible property, using the capital provided by Google Inc. The license given to Ireland Holdings allowed it to do business in Europe, the Middle East and Africa. Ireland Holdings purchased the rights to the technologies for an undisclosed "buy-in" payment. The buy-in payment was agreed to by the Internal Revenue Service through a program called an Advanced Pricing Agreement. Because transfer pricing is a process internal to a company, multinationals can easily manipulate pricing to minimize tax liability. The new Google structure can be represented as follows:



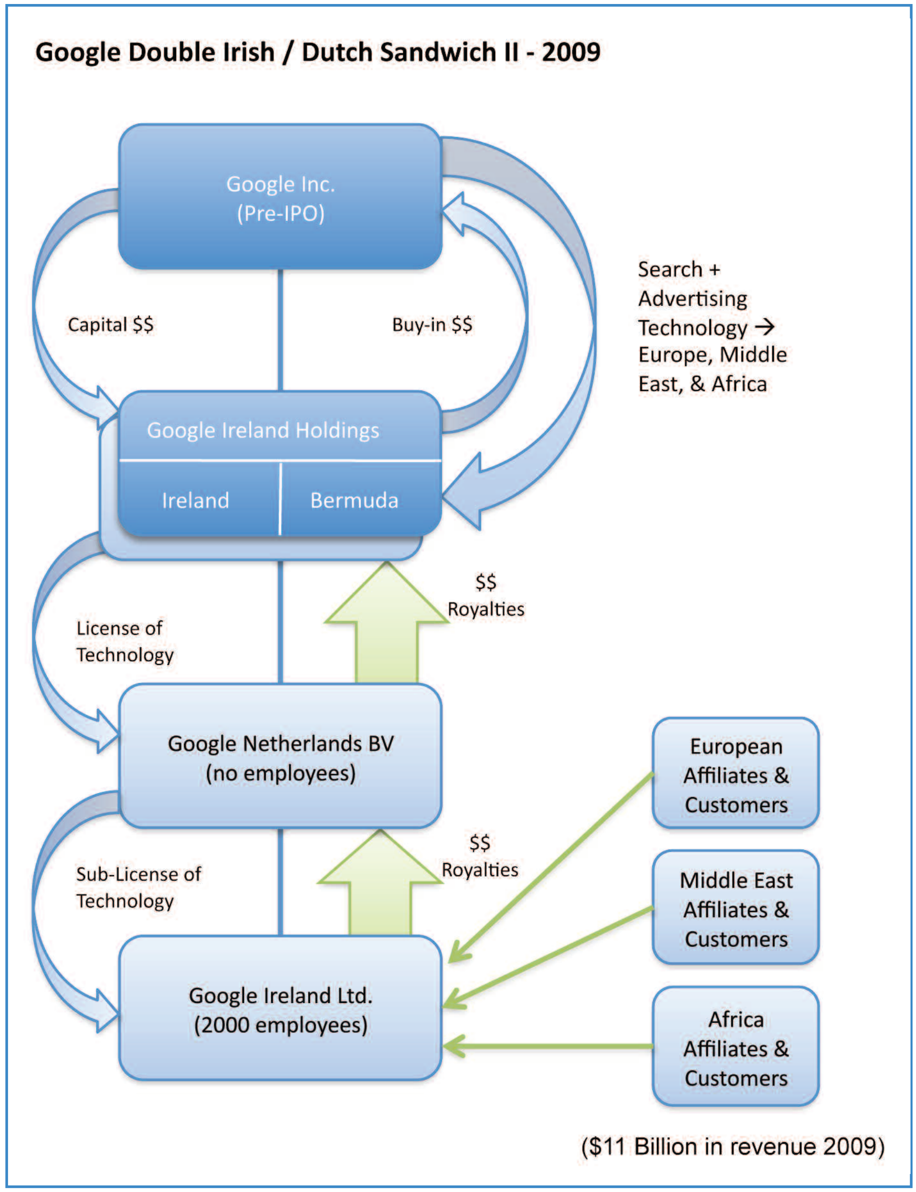
Source: Edward D. Kleinbard, "Stateless Income."

STEP 3: The Check-the-Box Rule, or How to Make a Company Disappear

Google's structure transformed again within a few years. First, Irish law allows Google to treat Ireland Holdings as a Bermuda resident for tax purposes even though it was incorporated in Ireland so long as the management and control of the entity is in Bermuda. The corporate income tax rate in Bermuda is zero percent and Ireland's is 12.5 percent. In a sense, Ireland Holdings became a dual resident company: It remained an Irish corporation because that is its place of incorporation. But for Irish tax purposes, Ireland Holdings became a resident of Bermuda by reporting that its management is in Bermuda. This made Ireland Holdings exempt from Irish taxes.

Also, Ireland Holdings created a Dutch subsidiary, Google Netherlands BV ("Netherlands BV"), which in turn created a third-tier subsidiary, Google Ireland Limited ("Ireland Limited.") in Ireland. Ireland Holdings licensed its patent rights to Netherlands BV, which in turn licensed those rights to Ireland Limited. Ireland Limited then began collecting billions of dollars in advertising revenues from the use of these technologies.

For U.S. tax purposes, Google has an Irish incorporated subsidiary with Bermuda tax residency with branches in the Netherlands and Ireland. The Irish branch conducts substantially all of Google's business in Europe, the Middle East and Africa. However, Ireland Holdings earnings are essentially tax free because Ireland Holdings is treated as a tax resident of Bermuda.



Source: Edward D. Kleinbard, "Stateless Income."

Since 1997, the Treasury has allowed corporations to treat a subsidiary as a separate corporation or to "disregard" it as a separate entity for U.S. tax purposes simply by checking a box on the tax form – commonly referred to as the "check the box"[25] rule. Thanks to this rule, multinationals saved billions in taxes.[26]

Both Netherlands BV and Ireland Limited had "checked the box," and therefore each was treated as a disregarded entity or "tax nothing" for U.S. purposes. But both were treated as corporations for all non-U.S. tax purposes. Thus, a company can disappear "for purposes of U.S. law while remaining relevant for purposes of all other fiscal systems, thereby facilitating a host of tax system arbitrage opportunities."[27]

STEP 4: Earnings Stripping in Action: Moving Money to a Tax Haven

Income earned in high-tax countries in Europe, the Middle East, and Africa flows directly to Ireland Limited without being taxed in those countries through a simple device: While Google salespeople are scattered in high-tax countries to meet and bring in clients, all final transactions occur in Ireland. Salespeople in these affiliates do not sign any paperwork to complete the sale. In effect, income is stripped from local affiliates and moved to Ireland Limited, where it is subject to a 12.5 percent corporate income tax.

STEP 5: Taking Deductions: Wiping Out Profits

While Ireland Limited is subject to a 12.5 percent tax on its net income, it pays very little in taxes. Companies are able to deduct from revenue the price they pay for goods and services they purchase in the course of business, including royalties paid to license intangibles from an affiliate. But because this transfer is an internal process, it is easily manipulated to increase the tax deduction.[28]

Ireland Holdings deducts from its income large royalty payments made to Netherlands BV for the use of Google intangibles originally transferred in 2003. Using this process, a company can claim the royalty fees wiped out much or all of its profits, reducing its annual tax liability.[29] Netherlands BV, then, also makes royalty payments almost as large to Ireland Holdings, thereby claiming large deductions. Netherlands BV pays taxes in the Netherlands on the spread between the royalties received and the royalties paid.

STEP 6: A Detour Through Amsterdam

Why does Netherlands BV exist when Ireland Limited could direct profits to Ireland Holdings? Royalties paid directly from an Irish company to a Bermuda subsidiary (that is, from Ireland Limited to Ireland Holdings) would be subject to a withholding tax imposed by Ireland on payout of royalties. But this tax does not apply if the royalties payments are between companies located in European Union member states, "even one that is an affiliate [and] serves no purpose but [to eliminate] Irish withholding tax."[30] Google BV exists to avoid triggering an Irish withholding tax. The royalty payments from Ireland Limited in Dublin take a detour to the Netherlands to avoid triggering an Irish withholding tax.

STEP 7: Profits Disappear in the Bermuda Triangle

Meanwhile, from a U.S. tax point of view, Ireland Limited and Google BV do not exist at all thanks to the "check-the-Box" rule. The United States only sees a Bermuda company – where most of its net income comes to rest – with operations located in Ireland. The result is a near-zero U.S. tax rate on income derived from customers in Europe, the Middle East and Africa.

STEP 8: Calculating Foreign Tax Savings

Ireland Limited today employs about 2,000 employees at its office in central Dublin. This subsidiary reported about 88 percent of Google's overseas sales, yet recorded "a pre-tax profit of less than one percent of sales in 2008, [largely due to] the $5.4 billion in royalties it paid, indirectly, to the Bermuda managed company."[31] By taking a detour to the Netherlands, Ireland Limited in Dublin avoided triggering Irish withholding tax. In Amsterdam, "Google Holding BV paid out 99.8 percent of the $5.4 billion it received from Dublin to the unit managed in Bermuda. The Dutch company has no employees."[32]

STEP 9: Foreign Profits Eclipse Domestic Earnings

Google's profits from its foreign subsidiaries eclipse its domestic earnings. From 2008 through 2010, Google consistently reported more foreign than domestic earnings. Substantially all of the income from foreign operations was earned by an Irish subsidiary.

	Domestic Earnings	Foreign Earnings
2008	$2,059 million	$3,794 million
2009	$3,579 million	$4,802 million
2010	$4,948 million	$5,848 million

This arrangement is known as a "Double Irish" structure because of the use of two Irish firms, with "Dutch Sandwich" coming from "the insertion of Google BV as a sort of tax filler between the two Irish firms."[33] Nothing in this structure is unique to Google. Indeed, structures like the Double Irish Dutch Sandwich have been reported to be in wide use in the technology and pharmaceutical industries.[34]

Evidence of Profit Shifting

Evidence shows that extensive profits are made by subsidiaries in countries where there is no logical reason for the firms to be there – except to reduce taxes.

Economist Martin Sullivan found that the average effective tax rate of U.S. multinational subsidiaries in five low-tax countries was below 10 percent. Although these small countries have economies equal to only 2 percent of the world's non-U.S. GDP, they together account for 21 percent of foreign profits of U.S. multinationals. These data strongly suggest that U.S. multinationals are aggressively shifting profits to tax havens and thereby significantly reducing taxes properly owed to the United States and other industrialized countries.[35]

Evidence of transfer pricing is strong. From 1999 through 2007, foreign profits of U.S. multinationals increased by 163 percent, while over the same period, traditional indicators of economic activity have increased on average by only 97 percent. This excessive growth of foreign profits represents an annual revenue loss of at least $28 billion, according to a study by economist Martin Sullivan.[36]

Other Methods of Avoiding U.S. Taxes[37]

> "If multinationals cannot be prevented from shifting profits to low-tax jurisdictions, then it becomes impossible to maintain the domestic corporate tax rates. If that bleeding can't be stanched, we might as well abandon the income tax."
> **Reuven S. Avi-Yonah, *Director of the International Tax Program at the University of Michigan Law School in Ann Arbor*[38]**

Method 1: THE DEFERRAL PRIVILEGE: The Building Blocks of it All

The current U.S. tax system, which allows corporations to defer profits and take foreign tax credits (discussed below), encourages corporations to shift profits offshore or disguise U.S. profits as foreign profits.

One benefit of creating a subsidiary in a no or low tax country is the special treatment of profits earned overseas. U.S. corporations are not taxed on income earned by foreign subsidiaries until they distribute that income back to the U.S. parent company.[39] Technically, corporations only defer paying U.S. income taxes on these profits, but these deferrals often begin to look permanent.

The deferral lasts until companies repatriate the earnings to the U.S. Google, for example, has deferred U.S. taxes on about $17.5 billion as of December 31, 2010.

In practice, however, corporations rarely repatriate significant portions, thus avoiding the taxes indefinitely.[40] Apple, for example, made $65 billion in pretax earnings in 2010 and of that amount, $13 billion was earned overseas. But instead of paying the total tax due on foreign profits (which would have been $4.5 billion), it deferred almost all of it.[41] As of September 25, 2010, Apple has $30.8 billion in deferred foreign income. Of that amount, Apple intends to invest $12.3 billion in operations outside the U.S. indefinitely. U.S. companies had amassed at least $1 trillion in foreign profits not taxed in the U.S. due to deferral as of the end of 2009. That cumulative total, based on filings by 135 companies, increased 70 percent over three years, from $590 billion in 2006.[42] Deferral of taxes on income of foreign subsidiaries will cost the U.S. $199 billion from 2011 through 2015.[43]

Companies wanting to bring their offshore profits back to the U.S. are lobbying Congress to institute a one-time tax holiday much like the one passed in 2004.[44] Leading this growing coalition of American's largest multinational corporations is Chief Executive Officer John Chambers of Cisco Systems Inc., along with other large technology and pharmaceutical firms. Cisco since 2005 has cut its income taxes by $7 billion by booking roughly half of its worldwide profits through a subsidiary located at the foot of the Swiss Alps that employs about 100 people.[45] Indeed, of the 843 companies that took advantage of the 2004 tax holiday, 52 percent of the benefits went to just 15 of the largest American multinational corporations, which were firms tending to have intangibles either in technology or brand names.[46] Pharmaceutical and medicine companies accounted for 32 percent of the total money brought back to the U.S., or $99 billion. Computer industry and electronic equipment industry accounted for $58 billion or 18% of the total. These two industries accounted for half of the repatriations.[47]

Corporation	Undistributed earnings of profits from foreign subsidiaries (millions)
General Electric	$94,000
Pfizer	$48,200
Merck	$40,400
Cisco Systems	$31,600
IBM	$31,100
Apple	$30,800
Microsoft	$29,500
Abbott Laboratories	$26,800
Hewlett-Packard	$21,900
Oracle	$21,000
Bank of America	$17,900
Goldman Sachs	$17,700
Google	$17,500
Dell	$12,300
Intel	$11,800
Dow Chemical	$9,800
Amazon.com	$1,600
Total	**$463,900**

Source: Figures gathered from the companies' 2010 SEC 10-K filings.

METHOD 2: DEDUCTIONS: Tax Subsidy for Foreign Profits

Even though corporations can defer profits earned offshore until they bring them back to the U.S., some of the expenses a corporation incurs to earn offshore profits are deductible against their U.S. taxable income immediately. Allowing immediate deductions of these expenses is "a tax subsidy for moving operations offshore [and] makes corporations even more tempted to devise schemes to make it appear that their U.S. income is being earned offshore."[48]

The details of these schemes have been documented by the Congressional Research Service and Citizens for Tax Justice.[49]

METHOD 3: THE FOREIGN TAX CREDITS PRIVILEGE: The Crediting Game

Another benefit of creating a foreign subsidiary is that foreign taxes are credited against repatriated income, so the corporation only pays the U.S. government the difference between the foreign rate and the U.S. rate.[50] Corporations can escape paying taxes to the U.S. government on income received from a foreign subsidiary by using excess foreign taxes paid in one country to offset U.S. tax that would be due. This is known as cross crediting. Since corporations can determine when to repatriate income, they often arrange to offset U.S. taxes on income earned in low-tax jurisdictions with foreign credits earned from high-tax jurisdictions, thus maximizing the use of the foreign tax credit.[51] This method has been curtailed in recent years through changes in tax regulations.

METHOD 4: INVERSE EARNINGS STRIPPING: Lowering U.S. Taxes, Increasing Overseas Profit

Much like when Google sold its intangibles to Ireland Holdings in 2003, a subsidiary in Bermuda could theoretically invent an intellectual property which it sells or licenses to Google Inc. in Mountain View. Instead of deflating the price, Google Bermuda could sell it to Google Inc. at an inflated price, allowing the U.S. parent company to claim large deductible expenses that reduce their U.S. taxable income. Meanwhile, the profits from the sale to Bermuda Holdings are not taxed because Bermuda does not have a corporate income tax. This method has been curtailed in recent years through changes in tax regulations.

METHOD 5: DEBT FINANCING: Lending to Itself

A company may also shift profit from a high-tax jurisdiction to a low-tax one by borrowing more in a high-tax jurisdiction and less in the low-tax one.[52] A U.S. corporation, for example, may create a foreign subsidiary in a low-tax jurisdiction where the U.S. parent would lend borrowed money to its subsidiary. A report by the Department of Treasury shows evidence that "U.S. multinationals allocate more interest to high-tax jurisdictions, but it is more difficult to assess earnings stripping by foreign parents of U.S. subsidiaries because the entire firm's accounts are not available."[53] A study by Altshuler and Grubert found that half of income shifting was due to transfer pricing of intangibles and most of the remainder was due to the shifting of debt.[54]

Conclusion

The evidence suggests that major U.S, corporations are avoiding tens of billions of dollars in U.S. corporate income taxes through a variety of devices and gimmicks which allow them to hide profits overseas, often artificially assigning these profits to countries with little or no corporate income tax. At a time in which growing concern over the federal deficit is leading to consideration of severe cuts in vital programs, it is urgent that Congress and the administration address and correct the loopholes that allow this large-scale tax avoidance.

References

[1] From 2001 through 2007, median household incomes experienced a steady decline while wages stagnated. The costs of health care and education continued to rise dramatically. The 2007 recession further eroded the wealth of middle-class Americans, destroying $20 trillion in wealth and nearly 9 million jobs. As a result, income for the median American household dropped by more than 4 percent from 2007 to 2009, the largest two-year decline in 35 years.

[2] See GAO, "Large U.S. Corporations and Federal Contractors with Subsidiaries in Jurisdictions Listed as Tax Havens or Financial Privacy Jurisdiction," December 2008.

[3] Robert McIntyre, "12 Corporations Pay Effective Tax Rate of Negative 1.5%," Citizens for Tax Justice, June 2011

[4] Robert McIntyre, "12 Corporations Pay Effective Tax Rate of Negative 1.5%," Citizens for Tax Justice, June 2011 (Citizens for Tax Justice released a preview of its forthcoming major study of Fortune 500 companies and the taxes they paid over 2008-10. This preview analysis looked at 12 corporations, including American Electric Power, Boeing, DuPont, Exxon Mobile, FedEx, General Electric, Honeywell International, IBM, United Technologies, Verizon Communications, Wells Fargo, and Yahoo).

[5] Citizens for Tax Justice, "U.S. is One of the Least Taxed Developed Countries," June 2011.

[6] GAO, "U.S. Multinationals Corporations: Effective Tax Rates Are Correlated with Where Income is Reported." GAO-08-950, August 2008 ("The average U.S. effective tax rate on foreign source income of these large corporations was around 4 percent. Bermuda, Ireland, Singapore, Switzerland, the UK Caribbean Islands, and China had relatively low rates among countries that hosted significant shares of U.S. business activity (measured by sales, value added, employment, compensation, physical assets, and net income). U.S. business increased in absolute terms both domestically and abroad from 1989 through 2004. Nevertheless, as of 2004, over 60 percentof activity (by all six measures) of U.S. multinational corporations remained located in the U.S. The UK, Canada, and Germany are the leading foreign locations of U.S. business by all measures except income.")

[7] Citizens for Tax Justice, "Statement of Robert S. McIntyre Before the Senate Budget Committee Regarding Business Tax Subsidies Administered by the Internal Revenue Service," March 9, 2011.

[8] Jesse Drucker, "U.S. Companies Dodge $60 Billion in Taxes With Global Odyssey," Bloomberg, May 13, 2010.

[9] Center for Labor Market Studies, "Their Impacts on Workers, Profits, and Stock Value," Northwestern University, May 2011 (According to the study, between the second quarter of 2009, when the recovery began, and the fourth quarter of 2010, national income rose by $528 billion, with $464 billion of that growth going to pretax corporate profits, while just $7 billion went to aggregate wages and salaries, after accounting for inflation.)

[10] Office of Management and Budget, www.whitehouse.gov/omb/budget/Historicals

[11] See a list of tax haven countries in the appendix. See footnote 55 for how the GAO compiled the list.

[12] Internal Revenue Service, cited in Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion," Sept. 2010, p. 19

[13] Testimony of Martin A. Sullivan before the Committee on Ways and Means of the U.S. House of Representative, January 20, 2011.

[14] Martin A. Sullivan, "Drug Firms Move Profits to Save Billons," Tax Notes, August 7, 2006 (the figure represents data from nine of the largest drug companies by 2005 revenue, including Pfizer, Johnson & Johnson, Abbott Laboratories, Merck, Bristol-Myers Squibb, Wyeth, Eli Lilly, Amgen, and Schering Plough. In estimating the amount of foreign and domestic income, first "worldwide income was estimated by dividing reported total tax liability by the worldwide effective tax rate. Second, domestic and foreign shares (which were reported in percentage) were multiplied by estimated worldwide income to arrive at the dollar amounts of domestic and foreign income.").

[15] Martin A. Sullivan, "Drug Firms Move Profits to Save Billons," ("Average excluded a few reported effective tax rates that are aberrations due to large one-time financial events or large losses that severely distort tax rates. Figures are adjusted to remove the effects of the repatriation provisions of the American Job Creation Act of 2004.").

[16] Martin A. Sullivan, "Drug Firms Move Profits to Save Billons," Tax Notes, August 7, 2006 (Drug prices are generally considered to be higher in the United States than in other countries, so a good argument could be made that domestic profits should be even larger and that the annual revenue loss from inappropriate transfer pricing is greater than $2.9 billion.).

[17] Testimony of Marin A. Sullivan Before the Committee on Ways and Means of U.S. House of Representatives, January 20, 2011.

[18] In Edward D. Kleinbard's research, "Stateless Income," he cites several papers examining the concentration of corporate income in a handful of relatively small foreign economies (Ireland, Singapore, Switzerland, Bermuda, and the Cayman Islands) whose only common feature is their low tax rates. See Edward D. Kleinbard, "Stateless Income," University of Southern California Law School, USC Center in Law, Economics and Organization Research Paper No. C11-1 & USC Legal Studies Research Paper No. 11-6, March 21, 2011; Martin Sullivan, "U.S. Multinationals Shifting Profits Out of the United States," Tax Notes, March 10, 2008; Martin Sullivan, "A Challenge to Conventional Tax Wisdom", 44 Tax Notes International 841, December 11, 2006 ("30 percent of the pre-tax profits of foreign affiliates of U.S. firms were located in very low-tax countries, a figure greatly disproportionate to employment or physical capital there"); Altshuler & Grubert, "The Three Parties in the Race to the Bottom: Host Governments, Home Governments and Multinational Companies", 7 Fla. Tax Rev. 153, 170, 182 (2005) (finding that from 1997 to 2002 "there was almost 100 percent growth in the income of foreign affiliates of U.S. parent companies in seven major low-tax countries (Bermuda, Cayman Islands, Ireland, Singapore, the Netherlands, Luxembourg, and Switzerland), and that this income represented roughly 40 percent of worldwide income from equity investments").

[19] Jesse Drucker, "U.S. Companies Dodge $60 Billion in Taxes With Global Odyssey," May 13, 2010.

[20] For a full description of Google's model, see Edward D. Kleinbard, "Stateless Income," University of Southern California Law School, USC Center in Law, Economics and Organization Research Paper No. C11-1 & USC Legal Studies Research Paper No. 11-6, March 21, 2011.
[21] Edward D. Kleinbard, "Stateless Income," University of Southern California Law School, USC Center in Law, Economics and Organization Research Paper No. C11-1 & USC Legal Studies Research Paper No. 11-6, March 21, 2011.
[22] Edward D. Kleinbard, "Stateless Income."
[23] An arm's length transaction is a transaction between two related or affiliated parties that is conducted as if they were unrelated, so that there is no question of a conflict of interest.
See Glossary of International Tax Terms at http://www.taxfoundation.org/news/show/152.html.
[24] Citizens for Tax Justice, "Revenue-Positive Reform of the Corporate Income Tax Income Tax," Jan 2011.
[25] GAO, *Effective Tax Rates Are Correlated With Where Income is Reported,* August 2008, p. 14.
[26] Rosanne Altshuler and Harry Grubert, "Governments, and Multinational Corporations in the Race to the Bottom," *Tax Notes International,* February 2006, p. 459-474.
[27] Rosanne Altshuler and Harry Grubert, "Governments, and Multinational Corporations in the Race to the Bottom," *Tax Notes International,* February 2006, p. 459-474.
[28] Citizens for Tax Justice, "Revenue-Positive Reform of the Corporate Income Tax Income Tax," Jan 2011.
[29] Citizens for Tax Justice, "Revenue-Positive Reform of Corporation Income Tax," Jan. 2011
[30] The Netherlands does not impose withholding tax on the outbound royalties paid to Ireland Holdings, and contents itself with collecting a small tax (essentially a fee for the use of its tax system) on the modest "spread" between the royalties Google BV receives and those it pays on to Ireland Holdings. (It is normal in Dutch tax practice to negotiate this sort of spread in advance with the Dutch tax authorities.)
[31] Jesse Drucker, "Google 2.4% Rate Shows How $60 Billion Lost to Tax Loopholes," *Bloomberg,* Oct. 2010.
[32] http://www.businessweek.com/technology/google-tax-cut/google-terminal.html
[33] Edward D. Kleinbard, "Stateless Income," *University of Southern California Law School,* USC Center in Law, Economics and Organization Research Paper No. C11-1 & USC Legal Studies Research Paper No. 11-6, March 21, 2011.
[34] See Jesse Drucker, "U.S. Companies Dodge $60 Billion in Taxes With Global Odyssey," May 13, 2010; Ron Claiborne, "U.S. Firms Dodge Billions in Taxes by Moving Profits Overseas," ABC World News, May 13, 2010; Jesse Drucker, "Google 2.4% Rate Shows How $60 Billion Lost to Tax Loopholes," Bloomberg, Oct. 2010.
[35] Testimony of Martin Sullivan before the Committee on Ways and Means of U.S. House of Representatives, January 20, 2011. For evidence of profit shifting, see Government Accountability Office, *U.S. Multinational Corporations: Effective Tax Rates are Correlated with Where Income is Reported,* GAO-08-950, August 2008 (finding that countries with no or low-tax such as Bermuda, Ireland, UK Caribbean Islands (Cayman Islands, British Virgin Islands, Turks, Caicos), Singapore, and Switzerland have higher shares of pretax profits of U.S. multinationals than value added, tangible assets, sales, compensation, or employees); Martin Sullivan, "U.S. Citizens Hide Hundreds of Billions in the Caymans," Tax Notes, May 24, 2004, p. 96 (Sullivan reports that the return on assets for 1998 averaged 8.4% for U.S. manufacturing subsidiaries, but with returns of 23.8% in Ireland, 17.9% in Switzerland, and 16.6% in the Cayman Islands); Martin Sullivan, "Extraordinary Profitability in Low-Tax Countries," Tax Notes, August 25, 2008, p. 724-727 (he noted that of the 10 countries that accounted for the most foreign multinational profits, the five countries with the highest manufacturing returns for 2004 (the Netherlands, Bermuda, Ireland, Switzerland, and China) all had effective tax rates below 12%, while the five countries with lower returns (Canada, Japan, Mexico, Australia, and the United Kingdom) had effective tax rates in excess of 23%.)
[36] Testimony of Martin Sullivan Before the Committee on Ways and Means of U.S. House of Representatives, January 20, 2011.
[37] This report does not cover all profit shifting and earning stripping employ by corporations. For a more thorough discussion of these and other methods, see Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion," p. 10. This report will not discuss Contract Manufacturing.
[38] Jesse Drucker, "U.S. Companies Dodge $60 Billion in Taxes With Global Odyssey," May 13, 2010.
[39] The U.S. tax system, under an anti-abuse rule referred to as Subpart F, bars corporations from deferring corporate profits in the form of rent, royalties, interests, dividends, and other types of "passive" income. These "passive" income sources are taxed immediately, because otherwise corporations may easily manipulate them for tax avoidance purposes. Serious loopholes, however exist. Many U.S. corporations may and do manipulate foreign tax credits to defer taxes on these types of offshore income. Also, in 1997, Congress enacted an exception in subpart F called "active financing," allowing corporations to defer certain insurance and banking income and income from manufacturers' financing of sales of their products. This exception has been extended several times. For more information, see: Citizens for Tax Justice, "Congress Should End 'Deferral' Rather than Adopt a 'Territorial' Tax System," March 2011; Jane G. Gravelle, "Tax Havens: International Tax Avoidance and Evasion," Congressional Research Service, Sept. 2010, p. 6.
[40] Jesse Drucker, "Google 2.4% Rate Shows How $60 Billion Lost to Tax Loopholes," *Bloomberg,* Oct. 2010.
[41] Jesse Drucker, "Google 2.4% Rate Shows How $60 Billion Lost to Tax Loopholes," *Bloomberg,* Oct. 2010.
[42] Jesse Drucker, "U.S. Companies Dodge $60 Billion in Taxes With Global Odyssey," May 13, 2010.
[43] Jesse Drucker, "U.S. Companies Dodge $60 Billion in Taxes With Global Odyssey," May 13, 2010.
[44] In 2004, corporations successfully lobbied the Bush administration to allow corporations to repatriate their offshore cash holding back to the U.S. at a tax rate of 5.25 percent.
[45] Jesse Drucker, "Cisco leads push for U.S. tax holiday," June 29, 2011.

www.royalgazette.com/article/20110629/Business02/70699927. The coalition of corporations leading lobbying efforts includes Adobe, Apple, CA Technologies, Duke Energy, Google, Microsoft, Pfizer, Qualcomm.
See also David Kocienewski, "Companies Push for Tax Breaks on Foreign Cash," The New York Times, June 10, 2011.

[46] Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion," Sept. 2010, p. 18-19.

[47] Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion," Sept. 2010, p. 18-19.
See also Rodney P. Mock and Andreas Simon, "Permanently Reinvested Earnings: Priceless," Tax Notes, November 17, 2008 (Their study found that firms with low tax burdens repatriated the most during the 2004 tax holiday. Because pharmaceutical and computer industries predominately have foreign subsidiaries in extremely low-tax jurisdictions, it is likely that a significant portion of their earnings were repatriated from countries such as the Netherlands, Switzerland, Bermuda, and Ireland).

[48] Citizens for Tax Justice, "Revenue-Positive Reform of Corporation Income Tax," Jan. 2011.

[49] Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion." Citizens for Tax Justice, "Revenue-Positive Reform of Corporation Income Tax," Jan. 2011.

[50] Citizens for Tax Justice, "Congress Should End 'Deferral' Rather than Adopt a 'Territorial' Tax System," March 2011.
See also Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion," p. 12 (The types of income that is considered foreign sources and thus can be shielded with foreign tax credits include "income from U.S. exports which is U.S. source income, because a tax provision (referred to as title passage rule) allows half of export income to be allocated to the country in which the title passes. Others include royalty income from active business and interest income).

[51] Congressional Research Service, "Tax Havens," p. 11. See also GAO Report on Effective Tax Rate (Report shows that between cross crediting and deferral, U.S. multinationals paid little U.S. tax on foreign income.)

[52] See Congressional Research Service, "Tax Havens: International Tax Avoidance and Evasion," Sept. 2010, p. 6.

[53] U.S. Department of Treasury, Report on Congress on Earnings Stripping, Transfer Pricing and U.S. Income Tax Treaties, Nov. 2007.

[54] Harry Grubert, "Intangible Income, Intercompany Transactions, Income Shifting, and the Choice of Location," *National Tax Journal,* Vo. 56, March 2003, Part 2

[55] In its 2008 study, the Government Accountability Office (GAO) identified jurisdictions that are considered tax havens or financial privacy jurisdiction, including OCED's list of committed jurisdiction and uncooperative tax havens, the National Bureau of Economic Research (NBER) working paper, which included a list of tax havens that was based on research summarized in Hines and Rice's article (James R. Hines, Jr. and Eric M. Rice, "Fiscal Paradise: Foreign Tax Havens and American Business," *The Quarterly Journal of Economics,* vol. 109, no. 1 (1994): 149-182). GAO, "Large U.S. Corporations and Federal Contractors with Subsidiaries in Jurisdictions Listed as Tax Havens or Financial Privacy Jurisdictions," GAO-09-157, Dec. 2008.

[56] Ibid. "A U.S. District Court order granting leave for IRS to serve a 'John Doe' summons, which included a list of jurisdictions that are recognized as offshore tax haven or financial privacy jurisdictions by industry analysts and are actively promoted as such by promoters of offshore schemes."

[57] NBER's list included the Channel Islands. Jersey and Guernsey are part of the Channel Islands. The two other sources we used to identify tax havens listed Jersey and Guernsey as two separate tax havens and did not include the Channel Islands on their lists of tax havens. To be consistent, we are including Jersey and Guernsey as tax havens on the bureau's list rather than the Channel Islands.

Appendix

List of Tax Haven Countries

The table below is a list of countries listed as tax havens or financial privacy jurisdiction in a recent report by GAO.[55]

Jurisdiction	Organization of Economic Co-operation and Development List (OECD)	National Bureau of Economic Research (NBER)	US District Court order granting leave for IRS to serve a "John Doe" summons [56]
Andorra	Yes	Yes	No
Anguilla	Yes	Yes	Yes
Antigua and Barbuda	Yes	Yes	Yes
Aruba	Yes	No	Yes
Bahamas	Yes	Yes	Yes
Bahrain	Yes	Yes	No
Barbados	No	Yes	Yes
Belize	Yes	Yes	Yes
Bermuda	Yes	Yes	Yes
British Virgin Islands	Yes	Yes	Yes
Cayman Islands	Yes	Yes	Yes
Cook Islands	Yes	Yes	Yes
Costa Rica	No	No	Yes
Cyprus	Yes	Yes	Yes
Dominica	Yes	Yes	Yes
Gibraltar	Yes	Yes	Yes
Grenada	Yes	Yes	Yes
Guernsey[57]	Yes	Yes	Yes
Hong Kong	No	Yes	Yes
Ireland	No	Yes	No
Isle of Man	Yes	Yes	Yes
Jersey	Yes	Yes	Yes
Jordan	No	Yes	No
Latvia	No	No	Yes
Lebanon	No	Yes	No
Liberia	Yes	Yes	No
Liechtenstein	Yes	Yes	Yes
Luxembourg	No	Yes	Yes
Macao	No	Yes	No
Maldives	No	Yes	No
Malta	Yes	Yes	Yes
Marshall Islands	Yes	Yes	No
Mauritius	Yes	No	No
Monaco	Yes	Yes	No
Montserrat	Yes	Yes	No
Nauru	Yes	No	Yes
Netherlands Antilles	Yes	Yes	Yes
Niue	Yes	No	No
Panama	Yes	Yes	Yes
Samoa	Yes	No	Yes
San Marino	Yes	No	No
Seychelles	Yes	No	No
Singapore	No	Yes	Yes
St. Kitts and Nevis	Yes	Yes	Yes
St. Lucia	Yes	Yes	Yes
St. Vincent and the Grenadines	Yes	Yes	Yes
Switzerland	No	Yes	Yes
Turks and Caicos Islands	Yes	Yes	Yes
U.S. Virgin Islands	Yes	No	No
Vanuatu	Yes	Yes	Yes

For a **List of the Largest U.S. Corporations, their Numbers of Foreign Subsidiaries and the Amount of Their Federal Contracts,** go to:

http://www.greenlining.org/resources/pdfs/100LargestCorporations.pdf

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