Tax the profits of corporations' foreign subsidiaries: at least $114 billion over 10 years

The Idea: U.S. corporations with businesses located in foreign countries do not have to pay taxes on the profits earned by their foreign operations (subsidiaries) if the profits are held overseas. Requiring corporations to pay taxes on the profits of their foreign subsidiaries as they are earned would bring in at least $114 billion[13] in revenues over 10 years. It would ensure that profits of U.S. firms are taxed regardless of where they are earned and take away the incentive to keep profits offshore.

The Rationale: The U.S. has a worldwide tax system, which means U.S. companies generally must pay federal income taxes on all of their income, no matter where they earn it. However, a tax loophole allows U.S. multinationals to delay paying U.S. taxes on overseas profits, as long as they keep those profits offshore. Until these profits are "repatriated" to the U.S. parent company, the profits are taxed.

The ability to defer overseas subsidiary taxes provides an incentive for overseas investments, as lower foreign taxes could encourage U.S. companies to create jobs overseas rather than bringing the money back to the United States. The loophole also encourages companies to record profits offshore, even if most of their business is actually done in the U.S., in order to artificially lower their tax rate.

Some members of Congress have called for a "repatriation holiday," which would give companies holding back profits a period of time when they could bring them back to the U.S. and pay low or no taxes. In 2004, a holiday was given and $182 billion in offshore profits was "repatriated." However, as soon as the amnesty period was over, the firms went right back to holding profits offshore, as the following graph shows.

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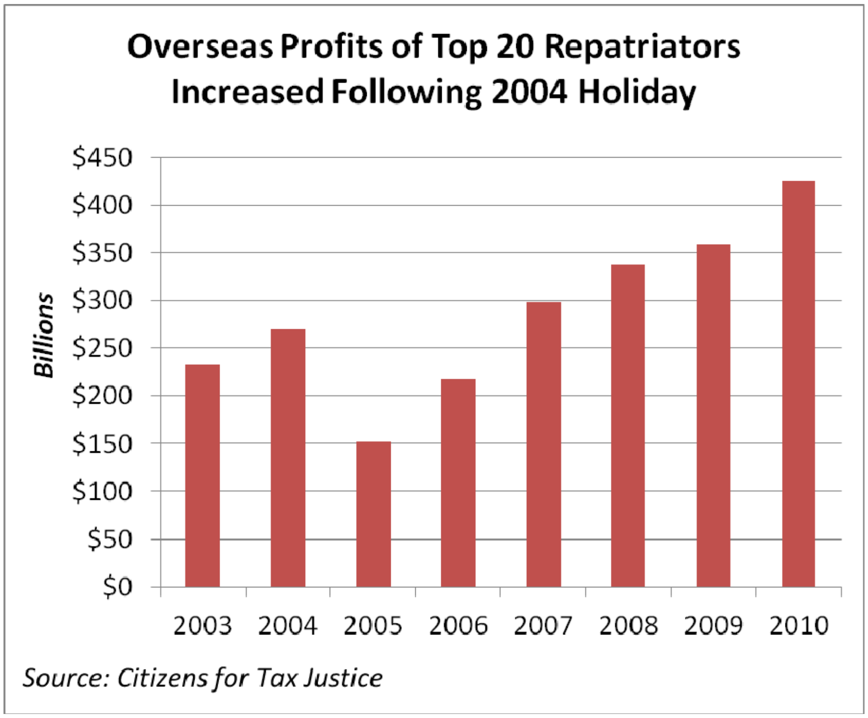

Tax holidays actually create a stronger incentive for holding profits offshore, as companies start warehousing profits overseas and waiting for another "holiday." The Institute for Tax and Economic Policy estimates that a tax holiday like the one in 2004 would cost the country $79 billion in lost revenue over a ten-year period.

A better solution is to repeal the rule allowing the deferral of taxes on overseas profits. Corporations would still receive a foreign tax credit, which lowers their U.S. taxes by the amount of taxes they pay to other countries. This would eliminate the potential for double taxation as well as the incentive to keep profits in other countries.

Support for the Idea: Recent surveys show this reform is very popular among small business owners who feel the existing loophole gives unfair advantages to large corporations. They want to see large transnational firms pay their fair share of taxes.

Legislation was introduced recently in Congress to tax the profits of corporations' foreign subsidiaries. Sen. John Rockefeller (D-WV) introduced the "International Tax Competitiveness Act of 2011," which would treat foreign corporations managed from within the United States as domestic corporations, thus preventing businesses from deferring the taxes of a foreign subsidiary. Related legislation in the Senate, by Sen.

Carl Levin (D-MI), would give the government stronger tools to combat off-shore tax havens and sanction foreign financial institutions that impede U.S. tax enforcement.

Of the plans reviewed for this revenue project, the following plans support eliminating the deferral of foreign subsidiary income: the Congressional Black Caucus' *The Responsible Path*, and the Congressional Progressive Caucus' *People's Budget*. Citizens for Tax Justice has also been pushing for this option.

[13] *Reducing the Deficit: Spending and Revenue Options*, CBO, pg. 186.