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MULTINATIONALS ADMIT TAX SAVINGS FROM MOVING OPERATIONS OFFSHORE

Dear Colleague:

Congress is faced with the task of responding to the recent World Trade Organization ruling that our export-related tax benefits (the FSC/ETI benefits) violate our trade agreements. These provisions benefit our U.S. manufacturing sector. Therefore, I have consistently taken the position that any revenue raised from the repeal of the FSC/ETI provisions should be used to support domestic manufacturers.

For the last year, the Bush Administration and Ways and Means Committee Chairman Bill Thomas have consistently attempted to use that WTO ruling as a pretext for enacting additional tax benefits for the overseas operations of U.S. multinationals.

Last year, the President's budget recommended that all of the revenue from repeal of the current FSC/ETI benefits be used to expand tax benefits for the offshore operations of U.S. multinationals. Essentially, the Bush administration was recommending a tax increase on U.S. manufacturers in order to fund benefits for companies that have moved their manufacturing and other operations offshore.

The President's budget recommendation this year concerning FSC/ETI is not quite that explicit. However, the President, in his budget, continues to argue that our companies need more tax benefits for their offshore operations. When testifying before the Committee on Ways and Means, Treasury Secretary Snow made it clear that enacting these offshore tax benefits remains an important goal for the Administration.

The argument that our tax laws pose competitive disadvantages to our companies overseas always has had a dubious factual basis. There have been studies that indicate adoption of a territorial system (i.e., a tax exemption for income from active business operations overseas) would increase, not decrease, federal tax receipts. It is worth repeating that those studies indicate that our current law provides benefits overseas greater than a total exemption. The validity of those studies has been demonstrated by the fact that virtually all major U.S. multinationals oppose suggestions that the U.S. adopt a territorial tax system.

The argument in favor of the efforts to further liberalize our tax rules overseas has become even more difficult in light of a recent article in the Financial Times in which some major U.S. multinationals concede that they are reducing their tax rates "by investing more capital overseas." One major U.S. multinational has seen its effective rate on its financial service business drop from 27% in 1999 to 16% in 2003. That company acknowledges that much of the fall is due to the increased portion of its business operations that are conducted outside the United States.

The article makes it clear that many of the largest U.S. multinationals have seen significant drops in their average tax rate over the last several years and that moving assets and operations overseas "has played the biggest part in allowing them to bring down the average tax rate." The article quotes one corporate tax official, "You only have to look at the way we tighten our belts in the U.S. through layoffs," to understand what is happening.

It is worth noting that when a company reports its effective tax rate, it includes both U.S. and foreign income taxes. These companies are not shifting assets out of the United States into other developed countries with high corporate rates. They are shifting them into low-wage economies with low or no corporate taxes or into tax havens. A recent article in Tax Notes (a publication that focuses on Federal tax issues) by Martin Sullivan documents the extent to which U.S. multinationals are shifting income into tax havens. According to that article, approximately 30% of all the foreign profits of U.S. multinationals were reported by subsidiaries domiciled in four low-tax jurisdictions (Luxemburg, Bermuda, The Netherlands, and Ireland), even though those subsidiaries accounted for only 3% of the total employment overseas of U.S. companies.

During the Bush Administration, we have experienced more than two million domestic job losses. The job losses in the manufacturing sector have even been more severe, totaling 2.6 million during the Bush Administration. In December of 2003, domestic manufacturing employment fell to 14.5 million, its lowest level in 45 years.

Notwithstanding those job losses, the Bush Administration continues to push more tax incentives for companies to move their jobs offshore. It is time for all of us to vigorously oppose those efforts.

Sincerely,

Charlie

Charles B. Rangel
Ranking Democrat