THE COMMERCIAL APPEAL

Date: Saturday, September 07, 2013
Location: MEMPHIS, TN
Circulation (DMA): 97,431 (44)
Type (Frequency): Newspaper (D)
Page: 7
Section: Main
Keyword: Matt Gardner

GUEST COLUMN

Most of us want corporate loopholes shut

By Matt Gardner
Special to Viewpoint

Democratic Sen. Max Baucus and Republican Rep. Dave Camp, the chairmen of the tax committees in the U.S. Senate and House, will visit FedEx headquarters in Memphis on Monday to discuss tax reform, an effort they are leading in Congress. It's an apt, if awkward, location for such a conversation.

The venue is apt because FedEx's taxpaying behavior is emblematic of the challenges facing anyone seeking to fix the United States' corporate tax system; it's awkward because FedEx is a heavy feeder on tax breaks enthusiastically supported over many years by bipartisan majorities in Congress.

FedEx's founder and CEO, Frederick W. Smith, holds a view of our corporate tax code that many other CEOs share, and has said we should "reduce our corporate tax rate to a worldwide competitive level of 25 percent and we have to go to what's called a territorial tax system."

What Smith does not mention, though, is that FedEx, like many other corporations that are household names, has paid hardly anything in federal corporate income taxes in recent years. Yes, the statutory corporate income tax rate is 35 percent. But the effective corporate income tax rate — the percentage of profits corporations actually pay in income taxes after accounting for various breaks and loopholes — is much lower for companies like FedEx.

For example, my organization, the Institute on Taxation and Economic Policy, found that between 2008 and 2010, FedEx paid an effective federal income tax rate of just 0.9 percent on over $4.2 billion in U.S. profits. With two more years of tax filings now publicly available, we know that over the past five years, FedEx paid an average effective federal income tax rate of just 4.2 percent.

How does FedEx drive down its effective income tax rate? The most significant way is with "accelerated depreciation" tax breaks, which allow companies to write off the cost of the machinery and equipment they purchase much faster than it actually wears out. Congress and President Barack Obama, rather than paring back these wasteful subsidies, have cheerfully expanded them in recent years.

Curtailing depreciation tax breaks should be on the short list of any common-sense tax reform agenda.

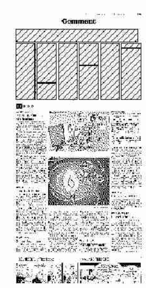
Smith, along with a growing army of corporate lobbyists, also calls for a "territorial" tax system. This is a euphemism for proposals to exempt the offshore profits of American corporations from U.S. taxes.

American corporations already get several breaks for their offshore profits. They receive a credit against their U.S. taxes for any foreign taxes they pay, which is how we ensure they avoid double taxation. But on top of that, they also get to "defer" paying any U.S. taxes that would be due on those offshore profits until they bring them back to the U.S.

And that last break has led corporations to accumulate a great deal of profits offshore. Sometimes these profits really are earned by a corporation's offshore business, but sometimes these are, in fact, U.S. profits that are "offshore" on paper only as an accounting gimmick to avoid U.S. taxes.

FedEx's latest annual report discloses that it now holds $1.3 billion in "permanently reinvested earnings," income that the company has moved "offshore" and says it does not plan to bring back; $300 million of this went abroad in just the past year. FedEx would likely benefit handsomely from a "territorial" system that essentially calls off U.S. taxes on offshore profits.

FedEx also demonstrates how the U.S. corporate income tax does not appear to make our companies less "competitive," despite the insistence of legions of CEOs that it does. Between 2008 and 2010, FedEx paid an effective income tax rate of 45 percent in the foreign countries where it does business. That's about 50 times higher than the 0.9 percent rate they faced in the U.S. In fact, of the Fortune 500 corporations that were consistently profitable and that had significant offshore profits during that same period, we found that two-thirds



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actually paid higher taxes in the foreign countries where they do business than they paid in the U.S.

Baucus and Camp have taken their tax reform tour to other large corporations that also have lower taxes at the top of their agendas. But poll after poll shows that's not what the American public wants. It turns out that large majorities of us want corporate tax loopholes closed and those extra dollars invested in the U.S. economy — in bridges, highways, ports, power grids, communications and other infrastructure — investments that make companies like FedEx profitable in the first place.

Matt Gardner is executive director of the Institute on Taxation and Economic Policy in Washington.