Discussion of “Watch What I Do, Not What I Say: The Unintended Consequences of the HIA”

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Overview

- A discussant’s nightmare!
- Unintended consequences?
- Provide a picture of those taking advantage of the holiday
- Policy implications?
- Open research questions

Unintended consequences

- Money is fungible!
  - Are Members of Congress naïve?
  - Experiment demonstrated that firms were not financially constrained when it comes to domestic investment (even though they claimed they were)
  - Difficult to use tax policy toward MNCs to influence their domestic investment

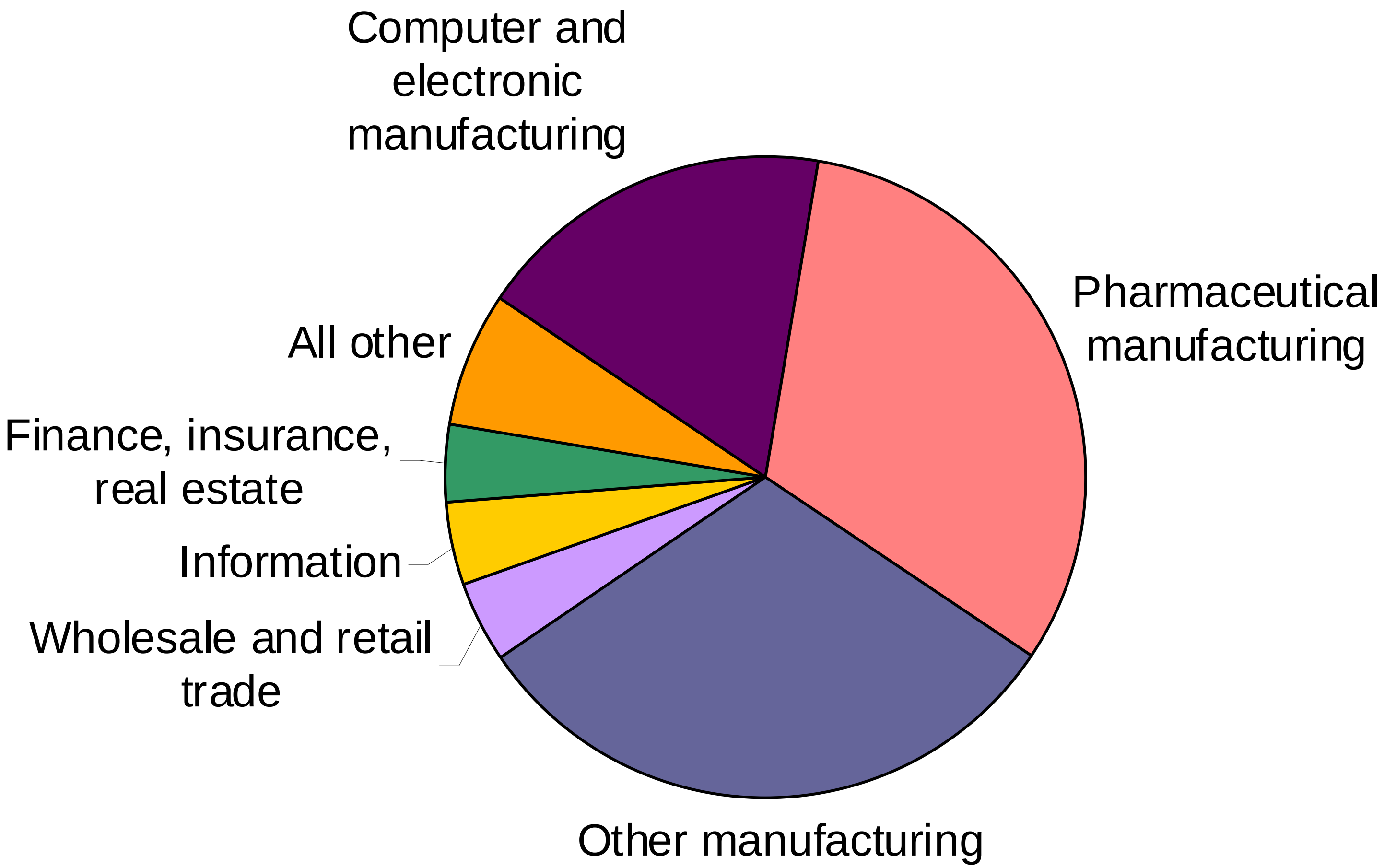
Unintended consequences

- Given money is fungible, what should we have expected?
  - Any difference in use of dividends in 2005 than in any other year with transitory low tax rate on dividend repatriations?
  - Aside: Surprised the authors didn't find significant effect on debt buybacks and executive compensation

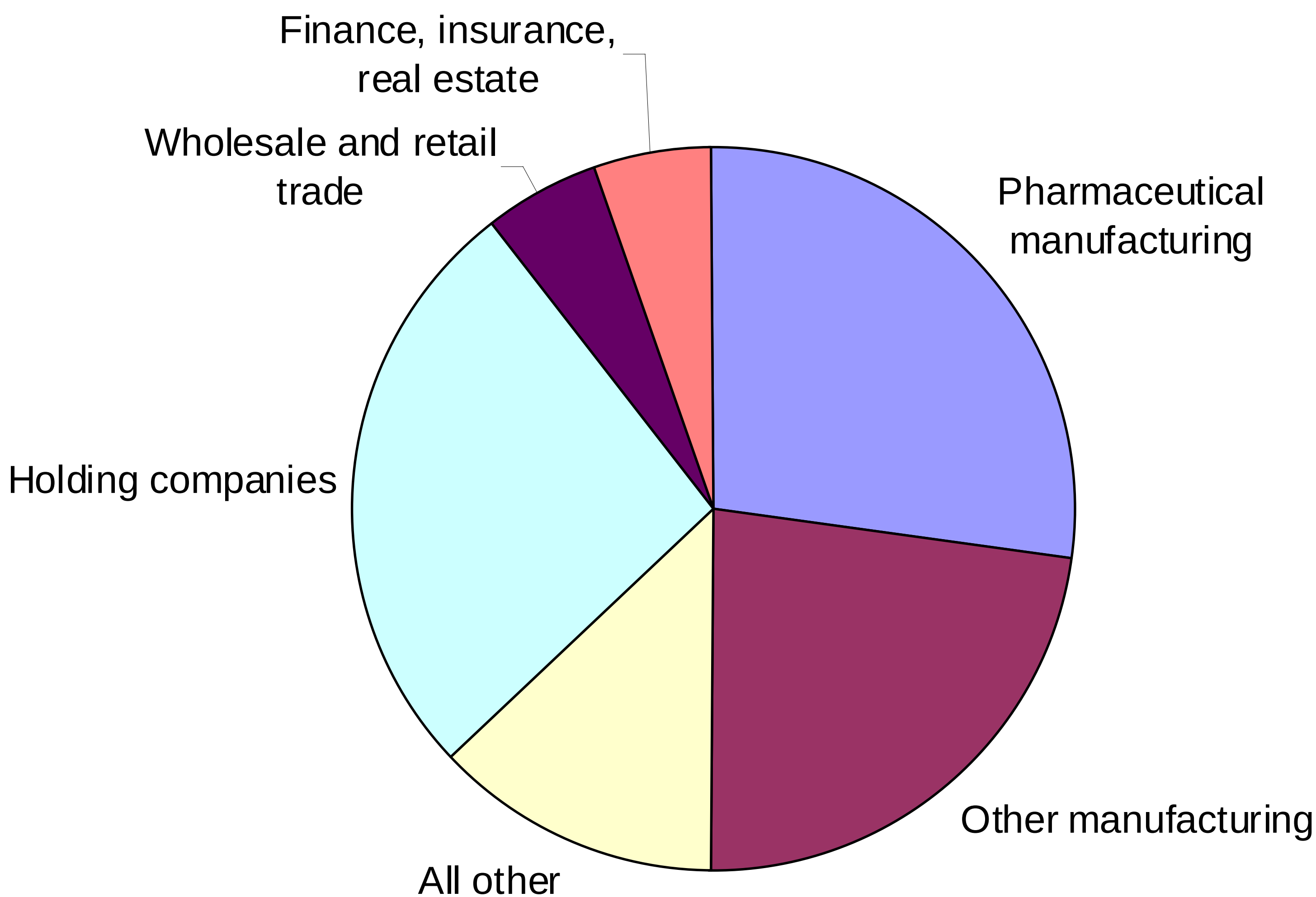
Who took advantage of the holiday?

- A small number of mostly large corporations (Redmiles 2008, data from tax returns)
  - Some 843 corporations (of a total of 9,700 corporations with foreign subsidiaries)
  - 29 pharmaceutical corporations repatriated roughly 32% of all qualifying dividends
  - 15 computer manufacturing corporations repatriated roughly 11%
  - 34 semiconductor firms repatriated about 4%
  - These 78 firms accounted for almost half of all qualifying dividends!

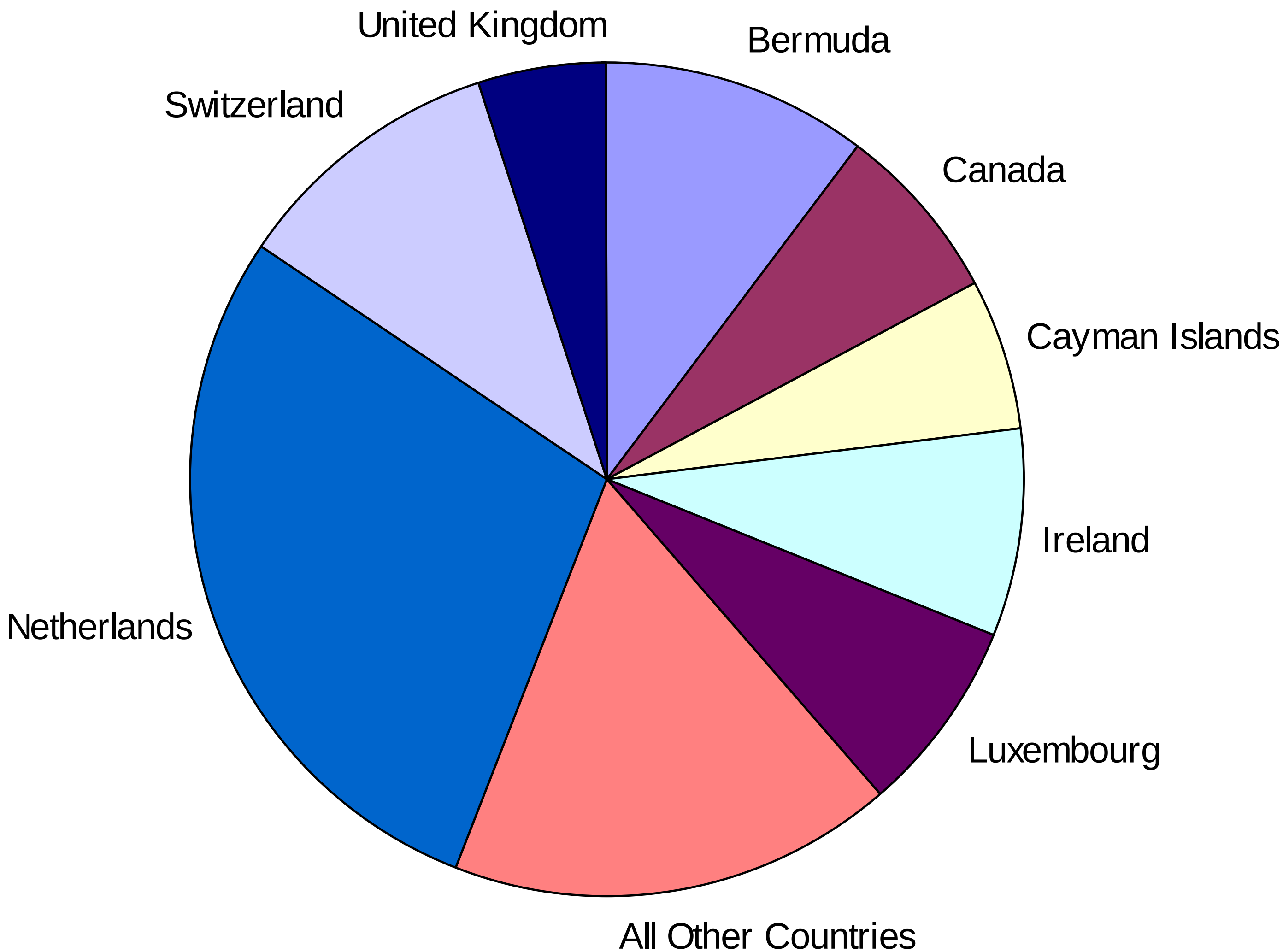
Repatriations by industry of parent



Repatriations by industry of subsidiary



Repatriations by country of subsidiary



Back to the paper…

- Provide similar information from the BEA data
- Questions: Does BEA data identify qualifying dividends?
- Authors do perform sensitivity analysis
  - If just look at manufacturing or pharma, any result on executive compensation or debt buy downs?

Instruments for dividends

- Why use only dummy variables?
- Instrument #1: Foreign tax burdens
  - Why not use parent's average repatriation tax instead of an indicator of whether tax is greater than the median? What was the median?
- Instrument #2: Tax haven / holding company
  - What percentage of firms did *not* have an affiliate in a tax haven or a holding company affiliate?
- Suggestion for another instrument
  - Measure of cash held abroad interacted with 2005 dummy (more on this later)

Policy implications?

- Burden of repatriation tax is important since it bears on the comparison of different systems of taxation of cross border investment
  - In particular, bears on comparison between exemption systems (no repatriation tax) and worldwide systems like the current U.S. system
  - An important question is whether deferral under the current system is as good as exemption

Policy implications?

- Some (including myself) have suggested that under current system firms have alternatives to repatriations
  - Can borrow against passive assets held abroad. Earnings in low-tax country can support domestic investment without bearing the U.S. corporate tax. (But interest rate may ↑ with stock of debt)
  - Can use “triangular strategies”. Low-tax affiliate invests in high-tax affiliate which becomes vehicle for tax free repatriation.
  - Another strategy uses tiers of subsidiaries to “blend” repatriation tax rates
- Repatriation tax can be avoided
  - Would predict that no one uses the holiday!

Policy implications?

- Results of paper suggest that these alternatives to repatriation, in fact, are not costless

  ... but do they give us information about excess burden of the repatriation tax?

- As authors state, results show that firms can’t eliminate the burden of repatriation taxes

- Grubert (July 2009) lays out a model in which there is no conceptual link between holiday repatriations and the burden of the tax

Open research questions

- Tax holidays
  - Does finding a big temporary response to a tax holiday say anything about the welfare cost of the tax in question?
  - What are the welfare implications of tax holidays?

- Did the tax holiday discourage repatriations post holiday?

Great paper

- The type of research that makes a difference in DC!
- Tax holiday has been proposed and dismissed but will certainly be proposed again
- Demonstrates the difficulty of using tax policy towards multinationals to increase domestic investment