

**Barriers to Mobility:
The Lockout Effect of US Taxation of Worldwide Corporate Profits**

John R. Graham
Duke University

Michelle Hanlon
University of Michigan

Terry Shevlin
University of Washington

Draft: September 15, 2008

Abstract: Using data from a survey of tax executives, we examine the corporate response to the one-time dividends received deduction in the American Jobs Creation Act of 2004 (AJCA). We describe the firms' reported sources and uses of the cash repatriated under the Act. In addition, we examine non-tax costs incurred by firms to *avoid* bringing the cash home prior to the AJCA. We also contribute to current policy debates by examining whether firms would repatriate reinvested earnings again if a similar Act were to occur in the future and the likelihood that firms assess on there being another such Act. Overall, the evidence is consistent with a substantial lockout effect resulting from the current U.S. tax policy of taxing the worldwide profits of U.S. multinationals.

This paper was written for presentation at the conference entitled “Mobility and Tax Policy: Do Yesterday’s Taxes Fit Tomorrow’s Economy?” at the University of Tennessee. We have received helpful comments on earlier drafts of the paper from Ed Maydew and Ryan Wilson. We appreciate valuable research assistance from Nemit Shroff. Thanks to the following people for helpful comments on the development of survey questions: Jennifer Blouin, Merle Erickson, Ken Klassen, Peter Merrill, Lil Mills, Sonja Rego, Richard Sansing, Stephanie Sikes, Doug Shackelford, Joel Slemrod, and Ryan Wilson. We appreciate Jennifer Blouin and Linda Krull sharing their list of repatriating firms with us. We also appreciate the efforts of PricewaterhouseCoopers (especially Peter Merrill) and the Tax Executives Institute (especially Timothy McCormally) in asking firms to participate and in reviewing the survey document. Finally, we are grateful for the financial support of the Paton Accounting Fund at the University of Michigan and the Fuqua School of Business.

**Barriers to Mobility:
The Lockout Effect of US Taxation of Worldwide Corporate Profits**

INTRODUCTION

In a frictionless world, capital would flow freely across countries. Within multinational firms, capital would be allocated across divisions, regardless of the location of those divisions, to maximize marginal product and firm value. In reality, tax laws create barriers to capital mobility. Taxes also create incentives for firms to expend resources in an effort to evade or minimize capital taxes. In this paper, we investigate whether, how, and to what extent taxation distorts the mobility of capital within firms.

In particular, we survey tax executives to examine their firm's response to the one-time dividend received deduction in the American Jobs Creation Act of 2004 (AJCA). The AJCA granted a temporary dividends received deduction of 85 percent of the extraordinary dividend from foreign earnings repatriated back to the U.S., which effectively reduced the rate of tax on the repatriated dividends to 5.25 percent (15 percent*35 percent statutory tax rate; we provide more details about the Act below). This dramatic rate reduction was a temporary change in the tax price of dividend repatriation and thus provides an ideal setting to study the incentives firms face when deciding whether to repatriate earnings back to the U.S. and the effects of U.S. tax policy on capital mobility. Most estimates of the amount of dividends repatriated under the provisions of the AJCA exceed \$300 billion (Redmiles, 2007).

Hartman (1985) concludes that if the repatriation and U.S. taxation of foreign earnings is inevitable (and this is a crucial assumption) and tax rates are a known intertemporal constant, then U.S. repatriation taxes do not affect the decision of mature firms to either reinvest funds abroad or repatriate them home. The only factors that matter in Hartman's (1985) model are the

after-local-tax rate of return (r_f) and the home country, or domestic, after-tax rate of return (r_d). However, Hartman (1985) does not incorporate 1) cases where firms can use tax planning strategies to return the money at a low U.S. tax rate, 2) the effects of a temporary tax price change like the one-time DRD granted in the AJCA of 2004, or 3) any tax rate uncertainty.

Empirically, prior research suggests that firms retain a large share of their earnings abroad when faced with a high tax upon repatriation. For example, Hines and Hubbard (1990) analyze 1984 tax return data and report that a one percent decrease in the repatriation tax is associated with a four percent increase in dividend payments by foreign subsidiaries in a sample of U.S. multinationals. Further, Desai et al. (2001) using Bureau of Economic Analysis (BEA) data of dividend repatriations for foreign subsidiaries conclude that repatriations are sensitive to repatriation taxes (in contrast they find that repatriations from foreign branches which are not subject to the repatriation tax are not sensitive to the tax, mitigating concerns of time varying changes in repatriations due to other non-tax factors). They infer from their data that repatriation taxes reduce aggregate dividend payouts by 12.8 percent. In addition, Foley et al. (2007) hypothesize that the repatriation tax cost is a reason that firms hold significant amounts of cash, an empirical observation previously explained by the existence of transaction costs and precautionary motives. They report evidence consistent with their prediction—firms that face higher repatriation tax burdens hold higher levels of cash, hold the cash abroad, and hold the cash in affiliates that would trigger high tax costs when repatriating earnings.

Furthermore, there is anecdotal evidence that firms incur non-tax costs to avoid repatriation taxes, indicating these taxes are important. For example, in 1993 Apple Computer Inc. (now Apple Inc.) filed a \$500 million shelf offering. The company stated they were considering the debt offering to pay for new research and development facilities. Analysts at the time noted that

it was an unusual offering because Apple had more than \$1 billion in cash on hand and no long-term debt obligations. The investor relations spokesperson for Apple, Bill Slakey, responded that Apple was reluctant to draw on the cash reserves because much of the cash was outside the U.S. and repatriating those assets would produce a significant tax bill.¹ In this same article analysts discussed the difficulties of high technology firms obtaining debt, indicating the debt was costly, but apparently less costly to Apple than bringing cash home from overseas.

Potentially even more costly, a few years later Apple considered merging or selling itself to Sun-Microsystems because its “financial condition was worsening” and noted that its board may have “decided a merger is the best way to save the company, which is facing a cash crunch to pay future restructuring charges and an upcoming debt payment.” An analyst from Brown Brothers Harriman said that although Apple had \$1.1 billion in cash, most of it was in foreign subsidiaries. He stated “if they were to draw it out it would be subject to taxation. It’s liquid, but it’s like drawing money from a 401K (retirement plan) or something.”²

In contrast, there is evidence that firms tax-plan to bring the money back to the U.S. in ways that avoid the U.S. tax, and thus the repatriation tax should not result in a substantial lockout of foreign earnings (e.g., “triangular” strategies described below from Altshuler and Grubert, 2003). There is also much anecdotal evidence that firms avoid taxes in general (Drucker, 2008; GAO 2008).

We contribute to the literature by asking over 400 tax executives at firms with foreign source earnings about their firm’s response to the one-time DRD in the AJCA of 2004. Our survey approach allows us to examine issues that are difficult to examine using traditional archival or

¹ Taken from a Dow Jones News Service article entitled “Apple Edges Toward First Bond Offer with \$500 mln Shelf” by Thomas Weber. May 7, 1993.

² Taken from a Reuters News Wire article entitled “Apple Talks Stalled Again Over Price” by Therese Poletti. February 7, 1996.

theoretical methods. For example, we ask the tax executives to describe 1) the sources of funds repatriated (was it from cash?), 2) the uses of funds repatriated (were there projects in which they previously felt they could not invest because they felt the funds were locked out of the U.S.?), 3) the costs incurred to avoid repatriating earnings prior to the tax amnesty under the AJCA (were they borrowing instead of using earnings from foreign subsidiaries?), among other questions.

Data on these issues are difficult to obtain without the use of a survey. For example, most financial statement data are worldwide and not provided by geographic segments (under the current accounting rules). As a result, activities in the U.S. versus foreign jurisdictions cannot be easily discerned (e.g., did firms shift investment from foreign jurisdictions to the U.S.?). In addition, as we describe below, the AJCA did not require the specific tracing of funds nor that the spending of the funds be incremental spending on “permitted uses.” Thus, because cash is fungible, archival data cannot delineate between what the repatriated funds were used for and what the cash “freed up” by the repatriated funds was used for. We directly ask executives to distinguish between these two types of funds in our survey questions. Using archival data does have some benefits, however, such as the availability of a larger sample and the use of reported, audited financial statement data (or data collected elsewhere such as perhaps the BEA). Thus, we view our results as triangulating the data from the archival studies.

Our survey data indicate that on average over 60 percent of the repatriations came from cash holdings. This result is consistent with the observations in Foley et al. (2007) that large cash balances are held overseas to avoid the tax. When the tax rate was reduced significantly, the firms brought the cash back to the U.S. The reported uses of the cash brought back to the U.S. are wide ranging but generally consistent with uses explicitly permitted by Congress, e.g., U.S. capital investment, the hiring and training of U.S employees, and U.S. research and

development. In addition, firms report that the two most common uses for cash “freed up” by the repatriated cash were paying down domestic debt and repurchasing shares, as one would expect in an efficient market (additional cash does not create new investment opportunities). This result sheds light on the empirical finding (in Blouin and Krull (2008) for example) that firms used the repatriated cash for share repurchases, which the authors point out is not a “permitted use” of the funds. The more detailed data from the survey reveal that to a large extent the firms used the cash from the repatriations for permitted uses and used “freed up” cash to repurchase shares. This distinction is important given the writing in the AJCA and subsequent guidance from the Internal Revenue Service (described in detail below). Surprisingly, the third highest ranking use of freed up cash was additional U.S. capital investment (36 percent of the respondents). This result suggests that the current repatriation tax inhibits investment and that even alternative sources of financing, such as borrowing, must be too costly for some of these firms to undertake investment that they otherwise would undertake in the absence of the incremental repatriation tax (or a lower tax rate).

Finally, our survey data reveal that the most common reported action taken to avoid repatriation tax is the raising of capital via debt in the U.S., with nearly 44 percent of companies stating they had done this. In addition, nearly 20 percent of the respondents noted that their company had invested the foreign earnings in financial assets with a lower rate of return than they could have earned in the U.S. All of this evidence is consistent with a significant lockout effect from the U.S. tax policy that taxes the worldwide income of U.S. multinationals.

The paper proceeds as follows. The second section provides a brief discussion of taxation of foreign sourced earnings of U.S. multinationals. The third section discusses our survey approach and the sample. The fourth section presents descriptive data about the respondents, the results,

and our interpretation of these results in the context of the prior literature. The final section concludes.

TAXATION OF FOREIGN SOURCED EARNINGS OF U.S. MULTINATIONALS

Taxation of foreign earnings

The U.S. taxes income on a worldwide basis. This means that U.S. taxes are incurred on income earned in the U.S. as well as the income earned abroad. In order to avoid subjecting U.S. multinationals (and individuals) to double taxation, the U.S. allows a foreign tax credit against U.S. taxes for income taxes paid to foreign governments. These credits are limited, however, to the amount of U.S. tax liability on foreign income (before any foreign tax credit). Thus, in general, if a firm has an average foreign tax rate that exceeds the U.S. tax rate, then the firm will not owe any incremental U.S. tax upon repatriation (nor will it receive a rebate from the U.S. government). These firms are said to be in an excess credit position (or are said to have binding foreign tax credits). Conversely, if a firm has an average foreign tax rate that is less than the U.S. tax rate, the firm will receive full credit for the foreign tax paid (or deemed paid) and will have to pay U.S. tax in the amount of the differential between the foreign tax rate and the U.S. tax rate times the foreign earnings. These firms are said to be in a deficit credit position (or are said to have nonbinding foreign tax credits).

Another important feature of the U.S. tax system is what is known as deferral. A U.S. parent is taxed on its subsidiaries' foreign income only when it is repatriated back to the parent corporation.³ Until repatriation, earnings reinvested in foreign operations are allowed to grow U.S.-tax free. The earnings for the foreign subsidiaries are not consolidated and taxed currently

³ Deferral is only available for US taxes on earnings of foreign subsidiaries of U.S. parents; it is not available for the earnings of a foreign branch.

because the tax rules on consolidation are different for domestic and foreign subsidiaries. For tax purposes, consolidation onto a single return can be elected, but is not required, when direct or indirect ownership, of a *domestic* subsidiary is at least 80 percent in terms of voting power and value. Foreign subsidiaries generally cannot be included in the domestic tax consolidation, and thus neither are their earnings.^{4,5}

There are provisions, such as the Subpart F rules, which aim to discourage U.S. firms from taking full advantage of deferral. Under these rules, certain foreign income of foreign subsidiaries is not eligible for deferral and is subject to immediate taxation in the U.S. Subpart F income includes, among other items, passive income of the foreign subsidiary.

The American Jobs Creation Act of 2004

The American Jobs Creation Act was enacted into law on October 22, 2004. A portion of the Act was codified in Internal Revenue Code (IRC) Section 965. Subject to the limitations described below, IRC Section 965(a) provides that a corporation that is a U.S. shareholder of a controlled foreign corporation (CFC; essentially a foreign subsidiary of a US parent corporation) may elect, for one taxable year, an 85 percent dividends received deduction (DRD) with respect to certain cash dividends it receives from its CFCs.⁶ This deduction provision effectively

⁴ If the foreign subsidiary had income effectively connected with a U.S. trade or business then that income would be subject to U.S. tax, however the foreign subsidiary still would not be part of the tax consolidation with the U.S. parent.

⁵ Under the current accounting standards (APB 23), companies that have deferred US cash taxes by retaining overseas the foreign source earnings of foreign subsidiaries also do not have to record any related tax expense on their income statement for these taxes as long as the earnings are designated as permanently reinvested. This deferral of the income tax expense for financial accounting increases net income of the firm all else constant. See Graham, Hanlon, and Shevlin (2008) for a discussion and tests of the importance of financial accounting effects in location and repatriation decisions. In sum, their results indicate that the financial accounting effects contribute to the lockout of foreign earnings.

⁶ See IRS Notice 2005-10 for the definition of cash dividends (dividends defined in which IRC Sections qualify).

reduced the applicable U.S. rate on the repatriations from 35 percent to 5.25 percent (15 percent times 35 percent).

The DRD is subject to several limitations. First, the amount of dividends eligible for the deduction is limited to the greater of the following 1) \$500 million, 2) the amount shown on the taxpayer's applicable financial statement as being permanently reinvested outside of the U.S., or 3) if only the tax attributable to the permanently reinvested earnings is disclosed then the limitation is the amount of tax divided by 35 percent.⁷ Second, the dividends eligible are limited to the excess of the dividends received during the taxable year by the U.S. shareholder from CFCs over the annual average dividends during the "base period years". The base period are the three taxable years among the five most recent taxable years ending on or before June 30, 2003, determined by disregarding the year for which the total amount is highest and the year for which such total amount is lowest among the five years (Section 965(c)(2)). Third, the amount of dividends is reduced by any increase in related-party indebtedness of the CFC between October 3, 2004 and the close of the election year. Finally, the amount of the eligible dividend must be invested in the U.S. pursuant to a domestic reinvestment plan that is approved by the taxpayer's president, CEO, or comparable official before the payment of the dividend and that is subsequently approved by the board of directors or similar body. Companies could elect the application of the DRD for either their last taxable year which began before October 22, 2004 or the first taxable year which began during the one year period beginning on October 22, 2004.

The taxpayer was to prepare a written domestic reinvestment plan that describes the specific anticipated investments in the U.S. that the firm would make with the repatriated funds, the time period over which the investments would be made, and whether factors beyond the

⁷ The applicable financial statement is the most recently audited statement which is certified on or before June 30, 2003 as being prepared in accordance with GAAP, and if the taxpayer is required to file with the SEC did so file on or before June 30, 2003.

taxpayers control could affect its ability to make the contemplated investment. The plan was to provide sufficient detail to enable the taxpayer to show upon examination that the expenditures that subsequently occurred were of the kind that were in fact contemplated at the time of the adoption of the plan and the plan had to include the total dollar amount to be invested for each respective principal investment in the U.S.

The IRS provided lists of both permitted uses of the funds and disallowed uses of the funds that qualified for the DRD but stated that neither list was intended to be exhaustive. The items specifically permitted include 1) the funding of worker hiring, training and other compensation in the U.S., 2) infrastructure and capital investments in the U.S., 3) research and development in the U.S., 4) financial stabilization of the corporation for purposes of job retention and creation (including the repayment of debt—U.S. or foreign⁸, qualified pension plan funding, and other expenditures), 5) acquisitions of certain interests in business entities, 6) advertising and marketing expenditures in the U.S., and 7) purchases of intangible property in the U.S. The items specifically not permitted include 1) executive compensation, 2) intercompany distributions, obligations, and transactions, 3) dividends and other distributions with respect to stock, 4) stock redemptions, 5) portfolio investments in business entities, 6) debt instruments or other evidences of indebtedness, and 8) tax payments.

It is important to note that specific tracing or segregation of the funds was not required nor was the spending required to be incremental spending. In fact, Notice 2005-10 specifically states that “provided a sufficient amount of funds is properly invested in the United States pursuant to the domestic reinvestment plan...the fact that other non-permitted investments are made during

⁸ Temporary repayment of debt is not permissible but on the other hand the taxpayer is not required to demonstrate that there has been a net global reduction in indebtedness of the taxpayer’s corporate group in order for repayment to be a permissible use of funds. The overall facts and circumstances of each case will be considered upon examination.

the period covered by such plan generally will not affect the eligibility of the dividend under section 965” (section 4.05)

By examining firms’ behaviors in response to the one-time DRD, we can make some inferences with regard to whether and to what extent the U.S. policy of taxing worldwide income impedes capital mobility.

SURVEY APPROACH AND SAMPLE

We developed the survey instrument with the support of Tax Executives Institute, PriceWaterhouseCoopers (PwC), and the Coalition for the Analysis and Study of Territorial Taxation. We solicited feedback from members of each of the above groups as well as from academic researchers. We had two companies beta test the online survey and we made revisions based on their suggestions.

Survey Sciences Group (SSG), a survey research consulting firm, assisted with the final survey design and programmed an online version of the survey. SSG also professionally formatted a paper version of the survey to be distributed with the final reminder. The final survey contained 64 questions, most with subparts. The paper version of the survey was 12 pages long. The survey contained many branching questions and as a result many firms were directed to answer only a portion of the questions.⁹

An initial email invitation was sent on August 9, 2007 to the highest ranking tax executive that is a member of Tax Executives Institute (TEI) at 2,794 firms (thus, only one invitation was sent to each company); three of these were returned as undeliverable. We also sent a letter via two-day express mail to fifteen companies for which we did not

⁹ The online survey is available at www.ssgresearch.com/taxsurvey and the paper version is available upon request from the authors.

have email addresses. Thus, a total of 2,806 companies were sent invitations to complete the survey.

SSG sent three email reminders throughout August and September. We then sent a paper version of the survey (along with a letter with instructions about how to complete the survey online) during the last week of September and the first week of October. We closed the online survey on November 9, 2007.

A total of 804 firms entered the online version of the survey or sent back a paper version. Sixty of these firms entered no more than one or two responses and thus we delete them from our usable sample leaving 744 complete responses. The response rate for our survey is 26.5 percent (744/2,806), much higher than most prior survey studies. For example, Graham, Harvey, and Rajgopal (2005) obtain a response rate of 10.4 percent, Trahan and Gitman (1995) report a response rate of 12 percent in a survey mailed to 700 executives, and Graham and Harvey (2001) obtain a 9 percent response rate and Brav et al. (2005) have a 16 percent response rate. Slemrod and Venkatesh (2002) survey tax preparers and corporate taxpayers about compliance costs and obtain a 12 percent response rate from the tax professionals and 9 percent from the taxpayer corporations. One study that obtains a similar response rate to ours is Slemrod and Blumenthal (1996), which surveys large corporate taxpayers about compliance costs and obtain a response rate of 21.8 percent (365/1,672). We believe that our relatively high response rate is attributable to the support of Tax Executives Institute.¹⁰

¹⁰ In addition, the respondents seem to have a genuine interest in the topics. For example, one company wrote “Appreciate the survey. Interestingly, the survey touches on those tax management areas most important to our company at the moment...” Another commented “I rarely fill out surveys, but was impressed by your questions. The U.S. system for taxing foreign dividends is terrible in so many ways and doesn't even raise revenue.” Another respondent wrote simply, “Good survey!”

Because we are interested in U.S. companies' decisions with respect to taxes, we eliminate forty firms that indicate they are an S-corporation or state that they did not file a Form 1120 (under the assumption these companies are also not C-corporations but rather some type of pass-through entity). We restrict the sample further by eliminating observations which are subsidiaries of foreign parents (105 firms) or which state in their comments that their foreign operations were insignificant and thus they were not sure how to respond to the foreign earnings questions (4 firms). Finally, because we are interested in corporate decisions with respect to the repatriation of foreign earnings, we delete 184 observations where the respondent states that the firm had no foreign earnings during the last 10 years. This leaves us with a final sample of 411 firms. The sample size varies across questions due to branching or incomplete responses for that particular question.¹¹

DESCRIPTIVE DATA, RESEARCH QUESTIONS, AND RESULTS

Descriptive statistics

Our survey was divided into four parts. The first part of the survey asked general descriptive questions about the companies.¹² These data are summarized in Table 1 Panel A. In terms of ownership, 80.5 percent of the respondents are publicly traded on the NYSE, NASDAQ or AMEX, while 19 percent are privately held, and 0.5 percent are 'other' such as over-the-counter stocks. Our respondent firms represent a variety of industries, with roughly 39 percent being from manufacturing, 14 percent classified as holding companies, 7 percent from

¹² The second part of the survey asked questions about general location and reinvestment and repatriation decisions. The third part focused on the AJCA of 2004 and the repatriation decisions in response to that Act, the subject of the current paper. The final part of the survey asked general questions about tax aggressiveness, tax rates, and tax planning. The data in the second and last part of the survey are analyzed in separate papers.

professional, scientific, and technical services, and nearly 6 percent from wholesale trade (industries classifications are derived from the companies' responses about their principal business activity code on Form 1120). In all, 18 different industry classifications are represented. Nearly 10 percent of the respondents did not enter an industry code.

In terms of size, 23 percent of our sample has assets of \$500 million or less, 16.7 percent has assets that range from \$500 million to \$1 billion, 33.8 percent have assets between \$1 billion and \$5 billion, 8.6 percent have assets ranging from \$5 billion to \$10 billion, and nearly 18 percent have assets in excess of \$10 billion. Thus, our firms are on average larger than the typical firm on Compustat (e.g., 76 percent of our sample firms fall in the upper two quintiles of Compustat firms ranked by assets). Indeed, our sample contains many household names and some of the largest firms in the economy.

It is difficult using publicly available archival data to obtain information on the location of a firm's assets. In our sample, 38 percent of the companies indicate they have 10 percent or less of their assets in foreign locations. Slightly more than 11 percent of the firms have more than half of their assets in foreign locations.

The responses for our sample firms show that 95 percent of the firms file a consolidated Form 1120. The number of entities included in the consolidated filings vary greatly, with nearly 36 percent of respondents including fewer than ten entities. On the high end, 8.8 percent of respondents report that their firm includes more than 100 entities in their consolidated return. Because these data have not been collected previously we have no benchmark against which to compare them.

We next ask how many Forms 1120 were filed by the company (where "company" means the entity that files a consolidated 10-K or financial accounting statement). Roughly 59 percent

of the firms file one Form 1120. Slightly more than 29 percent file between two and ten Form 1120s and 9 percent file between 11 and 50 1120s. The multiple filings reflect the fact that the consolidation rules are different for tax purposes than for book purposes. For tax purposes, the consolidated filing is an election available only when ownership exceeds 80 percent. Financial accounting, however, requires consolidation when ownership exceeds 50 percent. Our question asked about the tax filings for the financial accounting group. It is therefore not surprising that there are multiple 1120s filed for the accounting group due to the differing consolidation rules.

In addition to the data on number of Form 1120s filed, we gather data regarding how many Form 5471s (Information Returns of U.S. Persons with Respect to Certain Foreign Corporations required to be filed when the US company has a greater than 10 percent ownership share of a foreign corporation) are filed by our sample firms. Six percent of the sample did not file a Form 5471. The majority of the sample, almost 75 percent, report that they file between 2 and 50 Form 5471s and 8 percent of the respondents filed more than 100 of the forms. These data reveal that the majority of the firms in the sample have at least a 10 percent ownership of at least one (and in most cases more than one) foreign corporation.

Thus, many of our sample firms are relatively large, file consolidated 1120s and/or multiple form 1120s, and have ownership interests in foreign subsidiaries. Our sample is therefore not composed of simple firms but rather is more representative of a broad cross-section ranging from simple to very complex in terms of tax structure and filings.

Finally, in our sample, almost 53 percent of the companies say that they generally have had excess foreign tax credits (i.e., foreign tax credit carryforwards) over the last five years. These data provide some idea as to whether the company operates in generally low-tax or high-tax foreign jurisdictions as well as the foreign tax credit position which may influence their

repatriation decisions. That fifty-three percent of our respondents have excess credits, somewhat calls into question the extent and availability of cross-crediting strategies. This observation was mentioned by one of our test companies when we asked the executive how prevalent cross-crediting is. He said a lot of firms have excess credits so he was not sure how available cross-crediting is in practice or to what extent it is used.

In Panel B of Table 1, we report additional descriptive data. The data reveal that 195 firms indicate they have a U.S. net operating loss (NOL) carryforward and the average (median) U.S. NOL over all sample firms (including those that have a zero NOL) is \$111 million (\$0) as of the latest fiscal year end. In terms of foreign NOL carryforwards, 228 firms report having a foreign NOL that on average (at the median) is \$58 million (\$0). More firms report having a state NOL (268 firms) and these NOLs have an average (median) of \$129 million (\$10).

Research questions and results

What was the source of the repatriated cash?

Foley et al. (2007) argue that companies maintain large cash balances because of the repatriation tax—the earnings are locked out of the U.S, or “trapped” overseas. Consistent with Foley et al. (2007) our data, presented in Figure 1, indicate that across our sample firms, the average percentage of the funds repatriated under AJCA that came from cash holdings was slightly more than 60 percent. In addition, the average percentage of funds repatriated under AJCA that came from the liquidation of financial assets was slightly more than 10 percent. Thus, the average amount of repatriated funds obtained from cash or near cash sources held overseas is nearly 75 percent. The fact that the repatriated funds were already in liquid form, but not

repatriated until the tax burden was reduced, is consistent with a lockout effect of U.S. tax policy and an impediment to capital mobility.

Anecdotal evidence suggests some firms borrowed money to repatriate to the U.S. For example, Merck in their 2005 annual report state that “Loans payable also includes \$1.6 billion of commercial paper issued by a foreign subsidiary under a \$3.0 billion commercial paper borrowing facility established in October 2005 to provide funding for a portion of the Company’s AJCA repatriation.” Similarly, our data indicate that the average percentage of funds reported to have come from borrowed money in the foreign subsidiary is approximately 24 percent; an average of approximately 20 percent was borrowed from unrelated parties, 3 percent from related parties, and about 1 percent from the U.S. parent company. This borrowing suggests that some of the foreign earnings were reinvested in a non-liquid activity. If this non-liquid activity generally consists of operations, then the earnings are not what we would call “locked-out,” i.e., the company was apparently not just holding trapped funds in cash or passive activities but it really did have overseas investments in which to use the funds. However, some of the data below suggests that perhaps these investments were not as profitable as alternative investments in the U.S. absent the tax.

Thus, the most common source of funds was cash or the liquidation of a financial asset (an average of nearly 75 percent of the funds repatriated). The second most common source was the borrowing of funds (an average of 24 percent of the funds repatriated). All other sources such as the infusion of equity by the parent or selling investments (e.g., property, plant and equipment) in the foreign subsidiary are trivial in comparison and sum to only an average of 1 percent of the funds repatriated.

How were the repatriated funds spent?

As described above, companies were required to have a dividend reinvestment plan (DRP) in place detailing their reinvestment of the repatriated funds in the U.S. While the government described permitted and unpermitted uses of the funds, they were careful not to require tracing of the funds. Several papers have investigated the use of funds using archival publicly available data. For example, Blouin and Krull (2008) examine firms that repatriated dividends and their spending activities following the repatriation. The authors conclude that firms used the cash to repurchase shares and that there was not an increase in capital investment. However, archival data are limited in their ability to discern the ultimate outcome of where investment occurs. For example, public financial statements do not reveal actions such as a company shifting investment that otherwise would have occurred overseas but because of the repatriation, occurred in the U.S. Furthermore, an increase in repurchases is not technically against the terms of the Act as stated in IRS Notice 2005-10 which explicitly states that “provided a sufficient amount of funds is properly invested in the United States pursuant to the domestic reinvestment plan...the fact that other non-permitted investments are made during the period covered by such plan generally will not affect the eligibility of the dividend under section 965” (section 4.05). Thus, a company can use the repatriated funds for investment and growth in the U.S., and use the freed up funds that otherwise would have been used for investment to repurchase shares.¹³ Using a survey approach enables us to directly ask questions designed to provide a deeper understanding of the actions companies took in response to the Act with respect to how the repatriated funds were spent.

¹³ See Brennan (2007) for an excellent discussion of theory of what firms should have done with the cash if trying to maximize shareholder value. In brief, more cash in the U.S. does not mean more investment opportunities in the U.S. Thus, the options which maximize shareholder value the most is to pay down debt or return the capital to shareholders in the form of a repurchase or dividend.

Figure 2 presents the responses to our use of funds questions and reveals the percentage of the repatriated funds that were used for specific causes as of the end of the year 2006. Our survey responses reveal that on average 24 percent of the repatriated dividends by our sample firms were used for U.S. capital investment. Our respondents, on average, used 23 percent of the repatriated cash for the hiring and training of U.S. employees, an average of 14.7 percent of the funds on U.S. research and development, and an average of 12.4 percent was used to pay down domestic debt. An average of ten percent of the funds was used for items we did not specifically delineate in the survey but which were typed in and described by the respondents. The most common of the additional descriptions of uses include 1) U.S. advertising and marketing, 2) U.S. non-executive compensation, 3) qualified plan benefit contributions. On average, the respondents report that seven percent of the funds repatriated was used for acquisitions and an average of 4.6 percent was still held in cash at the end of 2006. In contrast to Blouin and Krull (2008) and Clemons and Kinney (2008) (but consistent with Brennan (2007)), we do not find an overwhelming indication that firms used the cash to repurchase shares. In fact, on average, only 3.4 percent of the funds were used to repurchase shares and only 0.3 percent on average was used to pay dividends. Thus, the survey respondents indicate that for the most part the funds were used for the purposes explicitly stated as permitted.

As mentioned above, the spending in the DRP did not have to be incremental expenditures -- firms could substitute the repatriated cash for investment and use the cash they would have otherwise spent on investment on, for example, repurchases.¹⁴ As a result, the archival data could reveal an increase in repurchases and no increase in capital spending without there being any type of violation of the AJCA. In an attempt to reconcile survey results with some of the

¹⁴ Thus the actions can be much like the state lottery systems in the U.S. The funds from the lotteries are used on education but they are not incremental to what the government budget would be if there were no lottery. The lottery funds are to some extent substituted for non-lottery state funds.

recent literature that argues the repatriated funds were used for repurchases, we ask our firms how they spent the funds “freed up” by the repatriated cash. We ask this question in a simple yes-no format – “...did the availability of the repatriated funds for the purposes indicated above [Figure 2 purposes] free up other cash for any of the following?” Thus, the tabulated responses are not the average percentage of the funds repatriated across our sample firms but the percentage of firms that responded yes for each action. The most common yes response from 47.4 percent of the firms was that they used the funds to pay down domestic debt. Consistent with the empirical data (e.g., Blouin and Krull (2008)), the second most common response was that 40.4 percent of the firms used freed up cash to repurchase shares. In addition, 17.5 percent of our respondents say they paid dividends to shareholders with the freed up funds. Thus, the firms used the repatriated funds for the permitted purposes but then apparently had excess cash (relative to that needed to fund positive net present value investments) in the U.S., which they returned to shareholders. This is consistent with efficient use of the funds per financial theory.

A large number of firms responded that they used the freed up cash for U.S. investment, consistent with the lockout of these funds under pre-AJCA U.S. tax policy. For example, 36.8 percent of the firms responded that they used some of the freed up cash for U.S. capital investment, 25.5 percent of the firms used some of the cash for hiring and training of U.S. employees, 24.6 percent of the firms used some of the cash for U.S. research and development and 21.9 percent of the firms used some of the cash for the acquisition of another firm or assets. Thus, the firms appear to have had expected positive net present value investments in the U.S. that otherwise they would have had to raise capital to fund or not do at all, consistent with the foreign earnings being locked-out of the U.S.

In the results discussed so far (Figures 2 and 3) there is not much evidence of ‘round-tripping’ occurring. Some have suspected firms brought the money back to the U.S. and then sent it back overseas. Our responses indicate that this was rare – at least in the form we asked: very little capital or debt infusions were returned from the U.S. parent to the foreign subsidiaries.¹⁵ Thus, the funds appear to have remained in the U.S., presumably the ultimate goal of the Act.

Geographic segment data are extremely limited (after SFAS 131 in 1997) thus, archival data consist only of worldwide capital expenditures for most firms. Thus, whether firms shifted investment – decreasing foreign capital expenditures and increasing U.S. capital expenditures - is difficult to examine using archival data. To address this issue, we asked the firms the following question “as a result of the repatriation, did your company shift investment (or does your company plan to shift investment) to the U.S. that otherwise would have been done in a foreign location?” Our data on this question (untabulated) reveal that out of 113 respondents, 24 percent answered that yes they did shift investment to the U.S. from a foreign location. This result is further evidence of a lockout effect from the U.S. tax policy to tax worldwide earnings of U.S. corporations. Once the tax rate is effectively reduced, firms alter their investment location decisions bringing the cash to the U.S. and investing domestically.

Non-tax costs firms are willing to incur to avoid the repatriation tax

Another indicator of whether firms view overseas earnings as trapped is whether they incur non-tax costs instead of bringing the earnings back to the U.S. and paying the tax. These non-tax

¹⁵ There are other forms of ‘round-tripping’ we did not have space to ask about, however. For example, changing transfer prices prior to the repatriation so otherwise domestic sourced earnings were labeled foreign sourced and immediately brought back to the U.S. under the AJCA. See Bradley (2008) for a discussion and tests of this possibility.

costs represent a distortion in firm behavior as a result of a tax. In our survey, we directly ask “Because of the U.S. tax policy to tax foreign earnings, has your company taken any of the following actions to finance U.S. operations in order to avoid repatriating the foreign earnings (in years where the Section 965 election was not available)?” By far the most common response given by 43.6 percent of the respondents, is that their companies had raised capital via debt in the U.S. instead of bringing the cash needed back to the U.S. from a foreign subsidiary (see Figure 4). This result is consistent with the data in Figures 2 and 3 that show firms used repatriated funds and funds freed up from repatriations to pay down debt.

When asked whether the firm had invested in financial assets with a lower rate of return than U.S. investments, nearly 20 percent said yes they had accepted a lower pre-tax rate of return in order to avoid the tax. This evidence is directly consistent with tax law constraining investment to be suboptimal. The remaining choices received few positive responses, however, we find the fact that 9 percent of the respondents indicate that they had considered selling the entire company, some divisions, or some assets rather than repatriating funds is astonishing given the gravity of such an action (consistent with the press story about Apple in the introduction). Nearly 5 percent of our firms said that they decreased or did not increase a dividend to shareholders because they could not bring the cash back to the U.S. from foreign subsidiaries, and 3 percent responded that they decided not to invest in a profitable project in the U.S. (presumably the cost of raising capital was high as well).

A review of the ‘other’ responses (i.e., those filled in by respondents) reveals one company raised capital via a stock issuance, one company inverted to avoid the repatriation tax¹⁶, two companies used foreign subsidiaries (rather than the U.S. parent) to acquire a target company,

¹⁶ A corporate inversion is where the company relocates the place of legal incorporation to another location, generally a tax haven country, in order to avoid (or minimize) the U.S. corporate income tax. For studies on corporate inversions see Desai and Hines (2002), and Cloyd et al. (2003).

and two companies managed their transfer pricing arrangements. While we have no way to credibly quantify the costs of these activities, the degree to which these options are costly for the firms and their shareholders represent a lower bound to the cost of bringing the foreign earnings back to the U.S. and incurring the repatriation tax upon doing so.

Do firms pay tax on repatriated earnings anyway?

Altshuler and Grubert (2003) propose that many firms avoid the repatriation tax via the parent borrowing against foreign passive assets or through the use of related affiliates to effectively achieve tax free repatriations.¹⁷ The authors argue that a multinational corporation can engage in a variety of strategies that effectively repatriate foreign earnings without incurring the home country tax. The evidence above with respect to firm borrowings and the repayment of debt provides some evidence consistent with their hypothesis (i.e., that firms borrowed and avoided the tax). While this borrowing strategy avoids the U.S. tax on repatriation it is not costless as evidenced by many firms unwinding the positions and paying a 5.25 percent tax on the repatriations.

We further examine the general issue of whether firms repatriate earnings and whether they pay tax on these repatriations by asking our respondent firms what their cash effective tax rate is on non-965 repatriations.¹⁸ The data in Figure 5 reveal that out of the 406 firms that answered this question, 42 percent of the respondents do not normally repatriate earnings, 11 percent of the

¹⁷ For example, the low-tax subsidiary could lend to or invest in a related high-tax foreign affiliate, the high-tax affiliate then can repatriate all of its earnings back to the U.S. while then using the funds from the low-tax affiliate to fund operations. Another strategy is for a low-tax affiliate to be capitalized by an equity injection from an upper-tier subsidiary facing a higher local tax rate. Then any dividends paid from the low-tax affiliate to the high-tax affiliate would receive the blended higher rate for foreign tax credit computations. The authors refer to these as “triangular” strategies.

¹⁸ Note that we asked them to divide by the cash dividends received in the U.S. and not the dividend grossed-up by the foreign taxes paid. We wanted a measure of cash taxes paid on actual cash received here in the U.S. but this results in a rate that is generally overstated to the rate computed as U.S. tax paid on the grossed-up dividend.

firms pay a 0 percent tax rate, and roughly 12 percent respond that their average cash rate is between 0 and 5 percent. Thus, 65 percent of the sample either do not repatriate or pay a cash tax rate of less than 5 percent. That leaves 35 percent of our respondents that normally pay a rate greater than 5 percent; indeed approximately 12 percent report that they pay a cash rate greater than 30 percent on their non-965 repatriations.

Fourteen percent of our sample firms that repatriated earnings under the Act (N=114) report that they halted some form of tax planning intended to mitigate the tax burden on repatriated earnings in order to take advantage of the one-time DRD in the AJCA of 2004. This is intriguing given the Altshuler and Grubert (2003) evidence that firms tax plan around the repatriation tax.¹⁹ Further, it is possible that our response of 14 percent is an understatement because firms that tax plan to avoid the repatriation tax may not have repatriated anything under the Act, in which case they would not be in our respondent sample for this particular question (because only firms that took advantage of the Act were directed to answer this question).²⁰

On the other hand, the large cash balances on balance sheets (Foley et al. (2007) and the amount of funds repatriated in response to the AJCA are prima facie evidence that the U.S. repatriation tax is locking-out earnings and that many firms have no less costly (less than the 5.25 percent tax rate on the repatriations under the Act) method of repatriating the funds.

¹⁹ Firms could have also done additional tax planning to maximize tax benefits under the Act. For example, Merck states in its 2005 report to shareholders that "...the Company repatriated \$15.9 billion during 2005. The Company recorded an income tax charge of \$766.5 million in Taxes on Income in 2005 related to this repatriation, \$185 million of which was paid in 2005 and \$582 million which will be paid in the first quarter of 2006. This charge was partially offset by a \$100 million benefit associated with a decision to implement certain tax planning strategies." The additional expense for financial accounting results because Merck repatriated earnings designated as permanently reinvested and thus no tax expense was previously charged for the earnings on their income statement (see footnote 5 above). When the earnings are repatriated and the tax is owed, albeit at a relatively low rate, the related expense must be recorded for financial accounting purposes.

²⁰ Indeed, in Graham, Hanlon, and Shevlin (2008), 23 percent of the sample respondents stated that they did not take full advantage of the AJCA because they could repatriate foreign earnings at a rate less than 5.25 percent. However, in the cross-tabulation of the data in Graham, et al. (2008), many of the firms in the 23 percent were firms in excess foreign tax credit position, which may explain a large portion of the low tax repatriations – these firms pay a high foreign tax rate and thus owe little or no U.S. tax upon repatriation even in the absence of the AJCA.

Furthermore, discussions with the executives reveal that many do view the earnings as trapped. In the beta testing stage of the survey, we asked the executives if there were other important questions we should ask in the survey. One executive started laughing and said “Yes, ask how in the hell are you going to get these earnings back without another AJCA?”²¹

Tax policy implications of the AJCA

Clausing (2007) argues that one effect of the dividend received deduction in the AJCA of 2004 is that it may “send the signal that the U.S. government may grant such holidays in the future, or perhaps even move toward exempting foreign dividends from U.S. taxation.” She points out that the one-time DRD shares many features of a tax amnesty which is expected to reduce future compliance (see for example Alm, McKee and Beck (1990)). The worry is that firms anticipate that a similar amnesty will occur in the future and thus change their behavior going forward, in anticipation of that future amnesty.

We asked our sample firms (N=287) to assess the probability that there would be another one-time DRD (or similar rate reduction). Roughly 29 percent responded that their firm assessed a zero percent probability on another rate reduction in the foreseeable future (see Figure 6). In addition, 65 percent of the firms responded that they assessed the probability to be greater than zero but less than or equal to 50 percent. Thus, few firms believe there is greater than a fifty-fifty chance of there being another one-time DRD (only 5 percent assessed a probability of greater than 50 percent). Of the 286 firms that responded to the follow up question, 93 percent indicate that they have not reduced repatriations in expectation of another rate reduction (2 percent

²¹ The comment mentioned earlier in the manuscript from a different executive about the lack of availability of cross-crediting strategies also is indicative of locked-out earnings.

respond that they have reduced repatriations, and a little more than 4 percent respond that they are not sure). Thus, most firms appear to believe that this was a one-time rate reduction.

Importantly for our investigation of whether there is a lockout effect, the data in Table 2 show that 65 percent of our sample firms (N=286) respond that they would take advantage of another such provision if enacted, and the 166 firms that answered the follow-up question said they would repatriate an average of nearly 60 percent of the permanently reinvested earnings they currently have overseas. These results reveal that these firms would have greater mobility of capital if the U.S. tax on repatriated earnings were lower or not in effect. In addition, the highest level of consensus that we received on any question on the entire survey occurred when 77 percent of the respondent firms (N=296) indicated that yes, their company believes that the U.S. policy to tax worldwide income harms their companies relative to non-U.S. competitors.

DISCUSSION OF POTENTIAL RESPONSE BIAS

Although we obtain a high response rate relative to most prior surveys, we still have potential issues with response bias as in all surveys because our response rate is substantially less than 100 percent. In considering whether the non-respondents are different from respondents we examine firm characteristics of our publicly traded respondent firm to all of Compustat and find that in general our sample firms (publicly held) are larger, with higher effective tax rates, are slightly more highly leveraged, and have approximately the same book-to-market and price-earnings ratios as the average Compustat firm. Thus, it is not the case that only small, simple firms answered our survey. In addition, as our descriptive data reveal, our firms range from simple to complex and are varied in terms of industry, size, and type of ownership. Furthermore, our sample repatriating firms (N=105 for which we received data about the *amount* repatriated)

repatriated \$142.30 billion of qualifying dividends which constitutes 46 percent of the total qualifying repatriations documented in Redmiles (2007) – and her sample consisted of 851 tax returns. Therefore, our sample constitutes a substantial fraction of the total amount repatriated under the AJCA.

Another concern could be that only firms that complied with the explicitly listed “permitted uses” of funds would respond to the survey. In an attempt to investigate this possibility, we examine whether our respondent sample differed in terms of “unexpected repatriations” as defined in Blouin and Krull (2008). We compare our respondent firm repurchases over the years 2004-2007 to the average repurchase level of the firms in the Blouin and Krull (2006) study.²² If our firms have a significantly lower average level of repurchases than the Blouin and Krull (2006) sample then there may be some concern about response bias. However, in both the univariate and multivariate tests that Blouin and Krull (2006) conduct (in their paper they tested repatriating firms versus non-repatriating firms) we find that our sample firms actually repurchase a higher average amount of shares relative to the amounts for the entire sample of repatriating firms in their paper.

While we cannot completely eliminate all concerns about response bias because we do not know why the non-responding firms did not respond, we find no evidence of obvious bias in the expected manner discussed above.

CONCLUSION

We survey tax executives about their firms’ decisions surrounding the AJCA of 2004 in order to gain a deeper understanding of whether U.S. tax on foreign earnings creates barriers to

²² We appreciate Jennifer Blouin and Linda Krull supplying us with their sample firm names so that we could conduct this test.

capital mobility. In contrast to a world where capital flows freely across countries, we find evidence consistent with the U.S. tax on repatriated earnings being a significant barrier to mobility.

Our data are consistent with Foley et al. (2007), who hypothesize that earnings are retained overseas due, at least in part, to the U.S. tax due upon repatriation. Indeed, many of our sample firms have taken costly actions to avoid the tax, such as raising capital via debt and investing in foreign assets with a lower pre-tax rate of return than alternative investments in the U.S. These costs indicate that earnings are locked-out of the U.S. as a result of the U.S. tax policy to tax worldwide earnings.

When a temporary tax amnesty for repatriated earnings was enacted as part of the AJCA of 2004, a substantial amount of money was brought back to the U.S. In addition, our survey data suggest that most of the funds were obtained from cash or near cash sources, further evidence that these funds were previously locked-out. Our data suggests that much of the funds were used for capital reinvestment, training and hiring of employees, U.S. research and development, and the payment of domestic debt. We also asked firms whether the use of repatriated funds for the above purposes freed up other cash for other purposes. The tax managers responded that 47 percent of their companies used some of the freed up cash to pay down domestic debt and 40 percent of the firms used some of the funds to repurchase shares. This result offers some explanation and reconciliation of the prior literature which suggests firms used the repatriated funds to repurchase shares.

References

- Alm, James, Michael McKee, and William Beck. "Amazing Grace: Tax Amnesties and Compliance." *National Tax Journal* 43 No. 1 (March 1990): 23-37.
- Altshuler, Rosanne and Harry Grubert. 2003. "Repatriation Taxes, Repatriation Strategies and Multinational Financial Policy." *Journal of Public Economics* 87: 73-107.
- Blouin, Jennifer and Linda Krull. 2008. "Bringing it Home: A Study of the Incentives Surrounding the Repatriation of Foreign Earnings Under the American Jobs Creation Act of 2004." Working paper, University of Pennsylvania.
- Bradley, Sebastian. 2008. "Dividend Repatriation and Transfer Pricing Strategies in Response to the American Jobs Creation Act of 2004." Working paper, University of Michigan.
- Brav, Alon, John R. Graham, Campbell Harvey and Roni Michaely. 2005. "Payout Policy in the 21st Century." *Journal of Financial Economics* 77: 483-527.
- Brennan, Thomas. 2006. "Coming Home: Cash-Flow and Market Response to Repatriation." Working paper, Drexel University School of Law.
- Clausing, K. A. 2005. "Tax Holidays (and Other Escapes) in the American Jobs Creation Act." *National Tax Journal* 58 (3): 331-346.
- Clemons, Roy and Michael R. Kinney. 2008. "The Who, Why, and What of the One-Time Tax Holiday for Repatriations Provided by the American Jobs Creation Act of 2004." Working paper, Texas A&M University.
- Cloyd, B., L. Mills and C. Weaver. 2003 "Firm Valuation Effects of the Expatriation of U.S. Corporations to Tax Haven Countries." *The Journal of the American Taxation Association*, Supplement.
- Desai, Mihir A., C.Fritz Foley, and James R. Hines Jr. 2001. "Repatriation Taxes and Dividend Distortions." *National Tax Journal* 54 (4): 829-851.
- Desai, Mihir A. and James R. Hines Jr. 2002. "Expectations and Expatriations: Tracing the Causes and Consequences of Corporate Inversions." *National Tax Journal* 55(3): 409-441.
- Drucker, J. 2008 "Corporate Tax Reporting Draws GAO Scrutiny." *The Wall Street Journal*, A2 August 13.
- Foley, C. Fritz, Jay C. Hartzell, Sheridan Titman, and Gary Twite. 2007 "Why do Firms Hold so Much Cash? A Tax-Based Explanation" *Journal of Financial Economics* 86: 579-607.

Graham, John R., and Campbell Harvey. 2001. "The Theory and Practice of Corporate Finance: Evidence from the Field." *Journal of Financial Economics* 60: 187-243.

Graham, John R., Campbell Harvey and Shiva Rajgopal. 2005. "The Economic Implications of Corporate Financial Reporting." *Journal of Accounting and Economics* 40: 3-73.

Graham, John R., Michelle Hanlon, and Terry Shevlin. 2008. "The Effect of Financial Accounting on the Location, Reinvestment, and Repatriation Decisions of Multinational Companies." Working paper, Duke University, University of Michigan, and University of Washington.

Grubert, Harry and John Mutti. 2001. "Taxing International Business Income. Dividend Exemption versus the Current System." American Enterprise Institute.

Hartman, D., 1985. "Tax Policy and Foreign Direct Investment." *Journal of Public Economics*. 26 (1):107-121.

Hines, James R. Jr. and R. Glenn Hubbard. 1990. "Coming Home to America: Dividend Repatriations by U.S. Multinationals." In Razin, A., Slemrod, J. (Eds), *Taxation in the Global Economy*, University of Chicago Press, Chicago, IL pp. 161-200.

Redmiles, Melissa. 2007. "The One-Time Dividend Received Deduction." Working paper, IRS Statistics of Income.

Trahan, Emery A. and Lawrence J. Gitman. 1995. "Bridging the Theory-Practice Gap in Corporate Finance. A Survey of Chief Financial Officers." *Quarterly Review of Economics and Finance* 35 (Spring): 73-87.

Table 1 Descriptive Statistics

Panel A: General descriptive statistics

	Percent		Percent
Ownership (N=411)			
Public - NYSE	52.3	File a consolidated Form 1120 (N=407)	
Public - Nasdaq/Amex	28.2	Yes	95.1
Private	19.0	No	4.9
Other (e.g., OTC)	0.5	Entities included in 1120 group (N=387)	
Industry (N=411)			
Agriculture, Forestry, Fishing, and Hunting	0.00	1	0.26
Mining	1.95	2 - 10	35.66
Utilities	0.73	11 - 50	46.25
Construction	0.73	51 - 100	9.04
Manufacturing	38.93	> 100	8.79
Wholesale Trade	5.84	Number of Forms 1120 filed (N=403)	
Retail Trade	3.65	Zero	0.00
Transportation and Warehousing	1.95	1	59.31
Information	4.14	2 - 10	29.28
Finance and Insurance	3.16	11 - 50	8.93
Real Estate, Rental and Leasing	2.92	51 - 100	0.50
Professional, Scientific, and Technical Services	7.06	101 - 1,000	1.74
Management of Companies (Holding Companies)	13.87	> 1,000	0.25
Admin., Support, Waste Mgt. and Remediation Services	1.70	Number of Forms 5471 filed (N=411)	
Educational Services	0.49	Zero	6.08
Health Care and Social Assistance	0.49	1	5.60
Arts, Entertainment, and Recreation	0.97	2 - 10	31.39
Accommodation and Food Services	0.73	11 - 50	37.47
Other services	0.97	51 - 100	11.44
No code reported	9.73	> 100	8.03
Assets (N=396)			
<\$500 million	23.0	Generally have excess foreign tax credits? (N=408)	
\$500 - \$999 million	16.7	Yes	52.9
\$1 - \$4.9 billion	33.8	No	47.1
\$5 - 10 billion	8.6		
> \$10 billion	17.9		
Percent of Assets in Foreign Location (N=395)			
0%	7.34		
0-10%	30.63		
11%-20%	14.68		
21%-30%	13.92		
31%-40%	12.15		
41%-50%	9.87		
51%-60%	3.29		
61%-70%	3.54		
71%-80%	2.28		
81%-90%	1.01		
91%-100%	1.27		

Notes: These data were obtained through survey questions. Form 1120 is the U.S. Corporate Income Tax form. Form 5471 is an informational return filed in the U.S. about the activities of a foreign controlled corporation owned more than 10 percent by a U.S. person (the definition of which includes a U.S. corporation).

Table 1 (continued)
Descriptive Statistics

Panel B: Net Operating Losses

Survey responses to the question: As of your latest fiscal year-end, your company had tax net operating loss carryforwards in the following jurisdictions of approximately:
(all dollar amounts below are in millions of dollars)

All respondents

	Mean	Stdev	25th	50th	75th	Maximum	N
U.S. NOLs	111	344	0	0	53	3,400	385
Foreign NOLs	58	204	0	2	29	2,300	370
State NOLs	129	427	0	10	80	5,900	374

Responses conditional on the firm having an NOL

	Mean	Std	25th	50th	75th	Maximum	N
U.S. NOLs	219	459	10	50	197	3,400	195
Foreign NOLs	94	253	5	20	62	2,300	228
State NOLs	180	495	8	30	120	5,900	268

Table 2
Questions about a Future AJCA

Panel A:

Would your company take advantage of another IRC Section 965 (that is, another one-time DRD)?

	Yes	No
286 companies responded	64.7%	35.3%

Panel B:

Survey responses to the question: If the answer to question C-11 [the question in Panel A] is yes, approximately what percentage of permanently reinvested earnings would your company repatriate in qualified dividends based on the expected unremitted foreign earnings as of the end of tax year 2007?

	Mean	Std Dev	25%	Median	75%
166 companies responded	58.5%	33.9%	25%	50%	100%

Figure 1

Sources of Repatriated Cash

N=112

Survey responses to question: How were the funds obtained that were repatriated (specifically consider only the qualifying dividends under Section 965)?

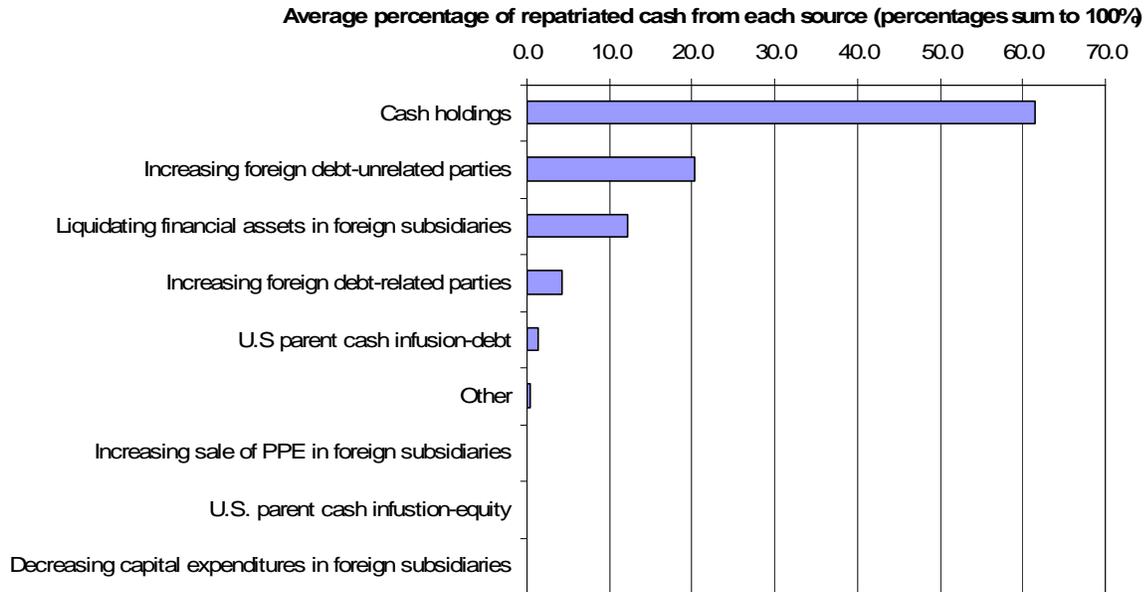


Figure 2
Uses of Repatriated Cash
(N=111)

Survey responses to question: At the end of the tax year 2006, what have been the uses of the cash dividends repatriated to the U.S. (specifically consider only the qualifying dividends under Section 965)?

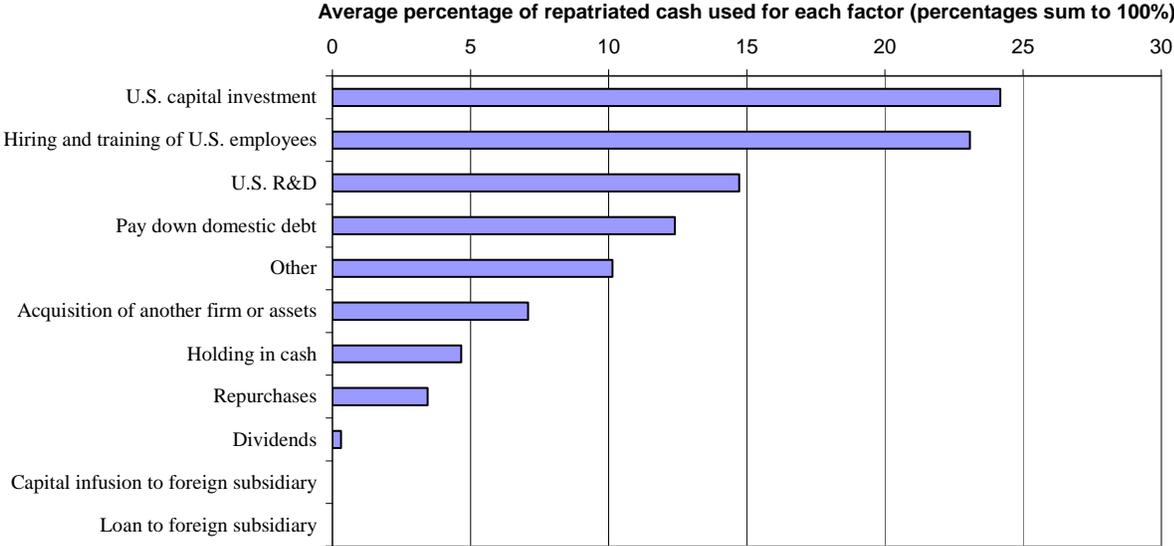


Figure 3
Uses of Cash “Freed Up” by the Cash Repatriated
(N=111)

Survey responses to the question: Recognizing the fungibility of cash, did the availability of the repatriated funds for the purposes indicated above free up other cash for any of the following?

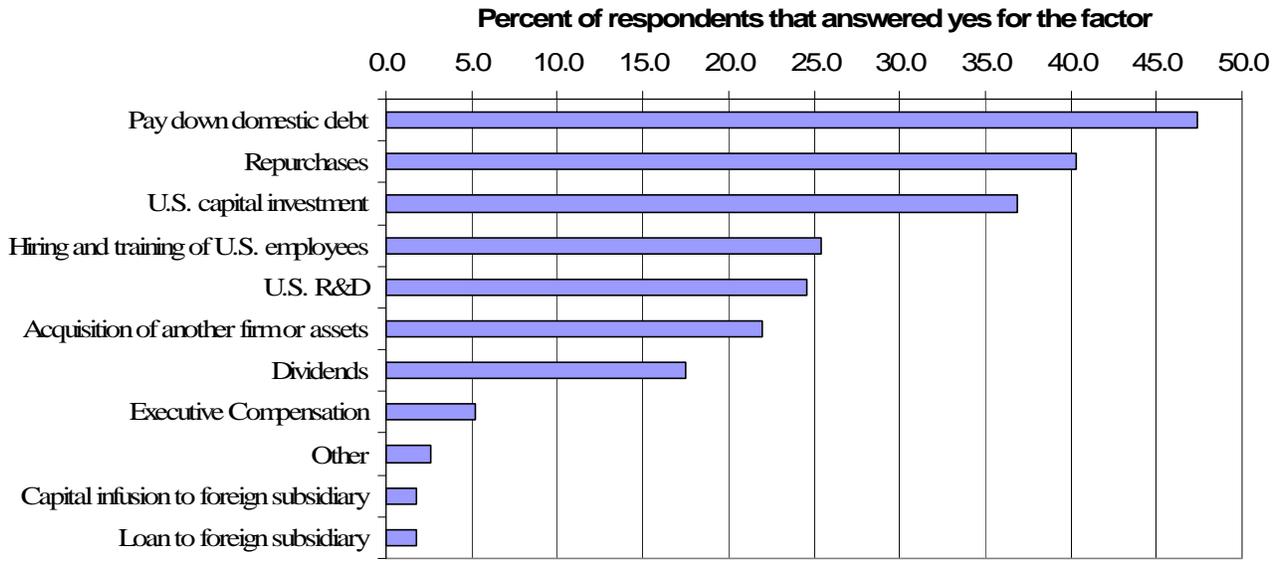


Figure 4
Actions Taken to Avoid the Repatriation Tax

Survey responses to the question: Because of the U.S. tax policy to tax foreign earnings, has your company taken any of the following actions to finance U.S. operations in order to avoid repatriating the foreign earnings (in years where the Section 965 election was not available)?

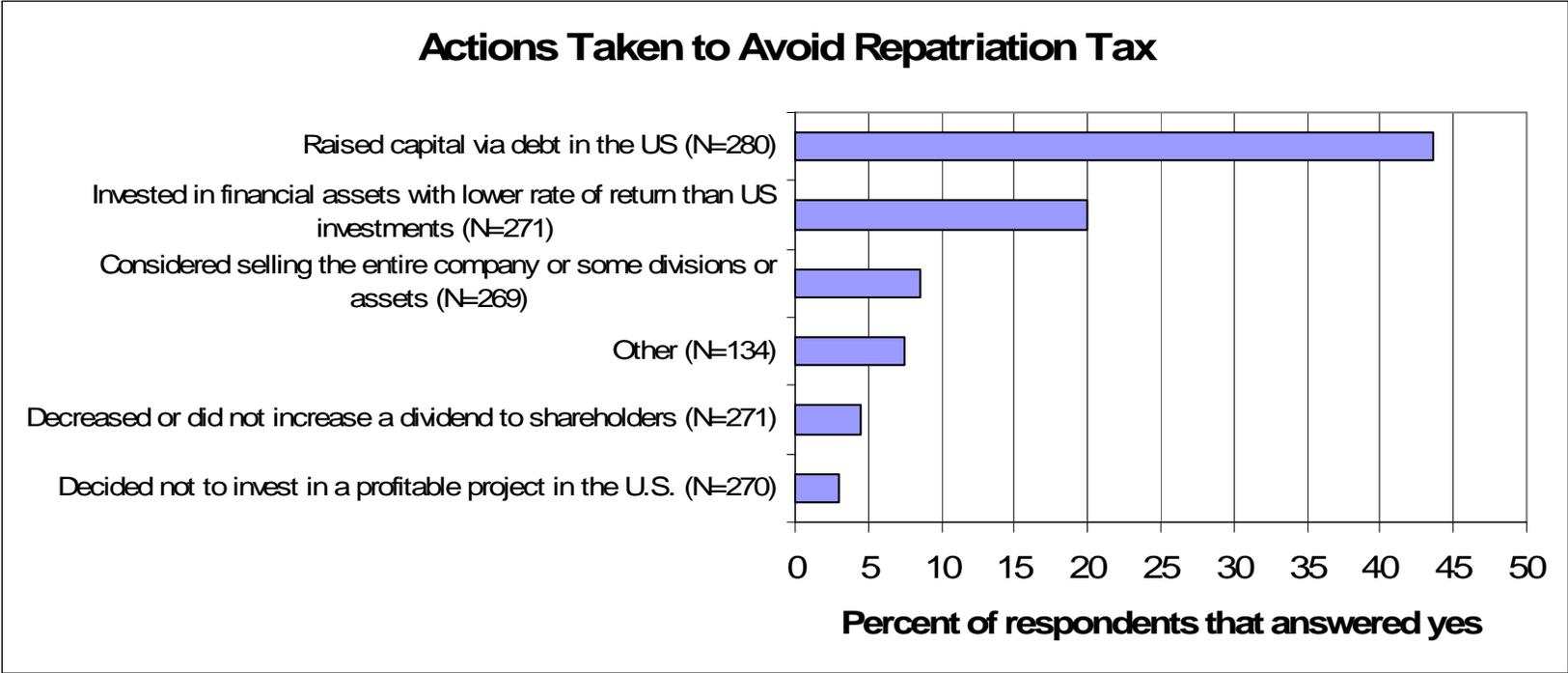


Figure 5
Cash Tax Rate on Non-965 Repatriations

Survey responses to the question: If your company repatriates foreign earnings in the form of dividends, approximately what is the average cash tax rate that your company pays to the U.S. on those dividend repatriations? (for this question only do not consider the repatriations made under the Section 965 election). By average cash tax rate we mean the amount of U.S. tax paid after foreign tax credits divided by cash dividends received in the U.S.

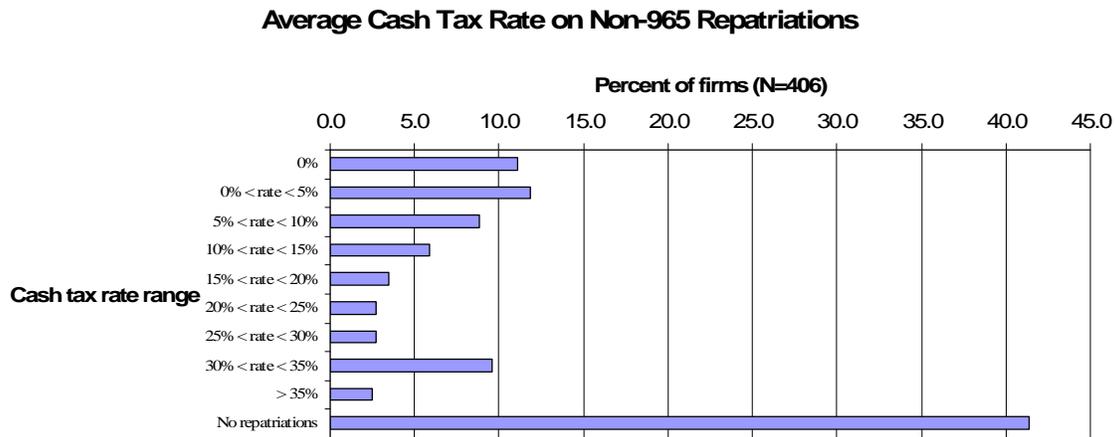
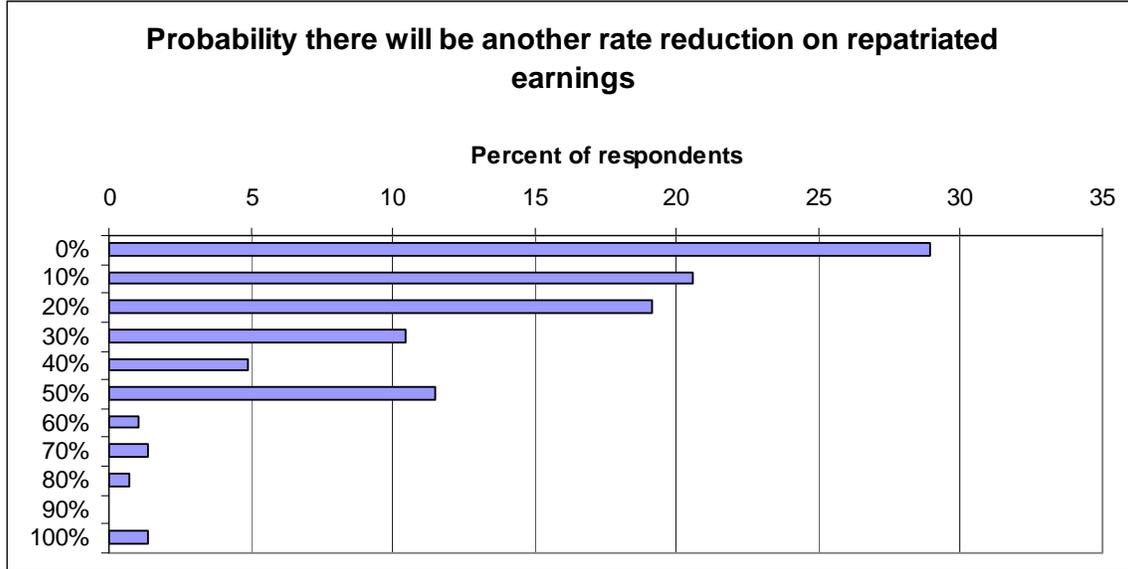


Figure 6
Probability of Another 'One-Time' DRD

Panel A:

Survey responses to the question: Approximately what probability does your company assess on the likelihood that sometime during the foreseeable future there will be another tax rate reduction on repatriated foreign earnings (similar to the one-time DRD under Section 965). (Check one probability.) (N=287)



Panel B:

Survey responses to the question: Following AJCA of 2004, has your company reduced its repatriations from foreign subsidiaries because your company expects a future rate reduction for repatriated earnings? (N=286)

