Wall Street Journal (December 2-3, 2017

For Multinationals, the Tax Bill's Good Likely Outweighs the Bad

Beyond a new corporate tax rate, the House and Senate versions have major repercussions for U.S. companies with overseas operations

By Theo Francis

Multinational corporations have a lot to like in both the House and Senate tax-overhaul proposals. Depending on a company's structure and operations, there could be a lot to worry about as well.

Companies with bigger U.S. operations, big capital budgets and less debt stand to benefit more, tax experts say. Those that have spent years shifting intellectual property and profits overseas are likely to see less benefit.

"For the majority of the economy, I think companies will net out better," said Stefanie Miller, senior tax analyst with Height Securities LLC.

Here are five broad provisions likely to make a significant impact on large multinationals.

Lower corporate rate: Both the House and Senate proposals cut the top corporate tax rate to 20% from 35%, a particular boon for companies with predominantly U.S. income and high effective tax rates, including banks and retailers. Companies are likely to benefit less if they already generate much of their profits in low-tax countries—whether through local operations or, as in the case of some technology and pharmaceutical firms, after years of aggressive tax-management.

To pay for the cut, Congress would eliminate a variety of tax breaks, including one aimed at domestic manufacturers that tends to reduce effective tax rates by about 3 percentage points for firms that can claim it, Ms. Miller estimates. Industrial firms aren't thrilled, but the overall rate reduction would more than offset the loss, she said.

The bill proposes limiting tax deductions for interest payments and the use of net operating losses to offset taxable income, which could be a problem for firms with high debt levels or significant accumulated losses.

But for most companies, these limits likely aren't severe enough to change the overall tax benefit firms ultimately receive; rather, they affect when companies can claim the benefits, according to J. Richard Harvey, a Villanova University law professor and former U.S. Treasury official. "Public companies are generally not that concerned about timing items," Mr. Harvey said.

Repatriated profits: U.S. companies have accumulated more than $2 trillion in overseas profits that, under the current system, would incur a hefty tax bill if returned to U.S. shores. Both House and Senate proposals would impose a one-time levy on the fruits of those profits—whether assets are repatriated or not—at 14% on liquid assets under the House proposal and 10% under the Senate's. The payoff for companies: Future foreign profits would go largely untaxed by Uncle Sam, under what is called a territorial tax system.

Among the biggest beneficiaries of the proposal: pharmaceutical companies, which have accumulated billions of dollars in overseas profits in low-tax countries, meaning they could incur big tax bills under current law if the proceeds are brought to the U.S. Amgen Inc., for example, has kept about $39 billion in cash overseas, while Pfizer Inc. has $22 billion and Merck & Co. has $20 billion, according to Credit Suisse analysts. Once freed up for U.S. use, most of those profits will likely be used for either acquisitions or buybacks, the analysts predict.

Intellectual property: Much of the profits tied up offshore were generated with intellectual property that had been shifted to low-tax jurisdictions. The Senate bill offers incentives to move that intellectual property back to U.S. parent firms: no tax on the transfer for three years, and then a lower 12.5% tax rate on future income it generates, rising to 15.6% in 2025.

That would make moving intellectual property back to the U.S. more cost-effective. Still, for some companies, keeping even lower tax rates in foreign jurisdictions could prove worthwhile. And low-tax jurisdictions could seek to counter the move by offering bigger incentives to stay, or even by imposing penalties on outbound transfers, said Robert Willens, a Columbia Business School professor who runs his own tax-and-accounting services firm.

Global minimum tax: If lower rates and a territorial system are the carrots, the House and Senate bills also include sticks—provisions intended to discourage tax-law arbitrage by large companies. One such measure, in both bills, would impose a global minimum tax of 10% on most companies. House and Senate details differ, but in essence, companies paying less than 10% tax on profits in foreign jurisdictions—dubbed "global intangible low-tax income," or GILTI—would have to make up the difference to the IRS. That would narrow the advantage for firms operating in low-tax countries like Ireland, Luxembourg or various island tax havens.

Base erosion measures: Another suite of measures seeks to rein in payments among U.S. companies and their foreign units that policy makers see as eroding the U.S. tax base. The House bill would impose a 20% tax on some payments from U.S. firms to foreign affiliates, sparking worries among U.S. manufacturers that they could be penalized for importing parts for use in products assembled in the U.S. The Senate's more intricate approach essentially imposes a 12.5% tax on income attributed to foreign units that exceeds a measure of expected return, called the "base erosion and anti-abuse tax," or BEAT. Similarly, if a disproportionate amount of a multinational firm's debt is incurred by U.S. units, the company would be barred from deducting more of its interest payments.

"The base erosion elements of the bill are something people haven't really thought about a whole lot," Mr. Willens said. "It definitely offsets a lot of the benefits."