

Putting Profits Over Patriotism

some american corporations are helping to fight the war on terrorism by storming the beaches — of bermuda

by Robert S. McIntyre

In a recent article in *The New York Times*, David Cay Johnston details how some sleazy American companies are reincorporating in Bermuda and other countries to avoid taxes. Insurance companies led the way a few years ago, and when Congress failed to take action, other patriotically challenged corporations followed suit.

The ploy entails little more than some creative paperwork. In late 2000, for example, computer-hard-drive maker Seagate Technology turned itself into a Cayman Islands “shell company” called “New SAC,” whose operations, Seagate notes in its 2000 annual report, “are substantially identical to the operations of Seagate Technology before the transactions.”

In fact, these freshly minted offshore companies don’t do anything at all in their new “home” countries. The chief financial officer for New Jersey-based Ingersoll-Rand, which expects to cut its U.S. taxes by \$40 million a year by pretending to move to Bermuda, cheerfully admitted to the *Times* that Ingersoll won’t even set up an office in Bermuda. “We just pay a service operation” to accept mail, he said.

Stanley Works, the well-known Connecticut toolmaker, expects to cut its taxes from \$110 million a year to \$80 million by reincorporating in Bermuda. New Hampshire-based Tyco International says it saved more than \$400 million last year by

doing the same. Others with existing or planned mail drops in Bermuda include: the infamous Global Crossing; New Jersey manufacturer Foster Wheeler; the Texas oil-well-services giant Nabors Industries; and Cooper Industries of Texas, which anticipates cutting its taxes by 40 percent. The big accounting firms — motto: “we have no scruples” — are aggressively promoting the new scheme. In a message to its clients, an Ernst & Young partner conceded that it might look unpatriotic, but

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Why would setting up a mail drop on a sunny island allow an American company to avoid taxes?

United States corporate income tax laws do have restrictions against companies using tax havens

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like Bermuda. But our anti-tax-haven rules generally apply only to companies incorporated in America. As newly-borne “foreign corporations,” companies claim to be suddenly exempt from the anti-tax-haven rules; they argue they must pay taxes only on whatever profits they deign to characterize as American. Not surprisingly, that’s a lot less than what they really earn here.

The tax-shelter promoters would like everyone to believe this is all so very, very complicated that nothing can be done about it. But that’s just blowing smoke. We don’t have to let a mail drop in Bermuda turn an American corporation into a foreign corporation. Instead, Congress should simply follow the lead of countries such as Germany, Japan and the United Kingdom, and treat any ostensibly “foreign” corporation whose shares are mostly owned by Americans as, well, American.

Beyond that, we ought to scrap an antiquated rule that lets American companies indefinitely “defer” reporting their foreign profits on their U.S. tax returns. It’s not that we want to tax actual foreign earnings — we give companies a full tax credit for the taxes they pay to foreign governments if they ever report the foreign income. But deferral opens up the door to other scams companies use to shift their American profits on paper to tax-haven countries, and our current anti-abuse rules are far too weak.

Eliminating deferral would stem these abuses and hugely simplify the corporate tax laws to boot. That’s exactly what the Kennedy administration unsuccessfully proposed back in the early sixties, and what both the House and Senate passed in the mid-

seventies — unfortunately not at the same time.

Is there any chance of really taking on multinational corporate tax sheltering, given our current political leadership? On the negative side, Bill Thomas, the California Republican who chairs the House Ways and Means Committee, has been an outspoken advocate of *expanding* multinational loopholes, and the Bush administration seems to have similar views. On the other hand, the outrageous Enron tax-haven situation and the blatantly unpatriotic cynicism of the accounting firms in promoting the new wave of phony offshore schemes ought to create considerable public pressure on lawmakers.

Senator Chuck Grassley of Iowa, ranking Republican on the Senate Finance Committee, has rarely been known as a corporate tax reformer, but in this case he believes something needs to be done. “There is no business reason for doing this, other than to escape U.S. taxation,” he told the *Times*. I believe the Finance Committee needs to investigate this activity.” Likewise, Rep. Charles Rangel of New York, the ranking Democrat on the House Ways and Means Committee, says that companies shouldn’t be allowed to “choose profits over patriotism.”

So maybe this will be the year that the tax-avoiding companies and their sneering

tax advisors get their comeuppance. We can always hope.

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Itep Analysis Finds Illinois Tax System Still Regressive

The Illinois tax system is regressive and out of balance, and recent tax changes have done little to correct the situation, according to a study released February 19 in Springfield, IL by the Washington, DC-based Institute on Taxation and Economic Policy (ITEP).

“No one would intentionally design a tax structure that applies the highest rates to low-income taxpayers, and the lowest rates to the wealthy. Yet that’s effectively how the Illinois tax system works,” said Matthew Gardner, principal author of the study, at a morning press conference held in the State Capitol Building.

The ITEP study, *Balancing Act: Tax Reform Options for Illinois*, found that the state’s tax system is *regressive* — that is, middle- and low-income families pay a higher share of their income in state and local taxes than do the well-off.

Balancing Act identifies the key features contributing to the tax system’s overall regressivity: highly regressive sales and excise taxes, high property taxes, and an insufficiently progressive personal income tax.

The state’s reliance upon regressive sales and excise taxes means that low-income Illinoisans face the highest tax burden, as a percentage of their income, of any income group — while the low income tax burden means that the wealthiest Illinoisans pay the *least* as a percentage of income.

Indeed, the poorest twenty percent of Illinois families and individuals — with incomes below \$15,000 — pay 13.0 percent of their income in state and local taxes while the middle twenty percent — with average incomes of \$36,400 — pays 10.0 percent. But the wealthiest one percent of the people in the Land of Lincoln — with incomes averaging

\$1.2 million — pay only 6.0 percent of their income in Illinois taxes.

The study documents the imbalance between property taxes and income taxes. While the Illinois property tax burden is more than 20 percent *above* the national average — the state income tax burden is more than twenty percent *below* the national average. And at a time when many states have moved to reduce reliance on regressive local property taxes through a tax shift toward income taxes, Illinois has done just the opposite: property taxes are a greater share of Illinois total taxes today than 20 years ago.

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“Illinois relies heavily on regressive local property taxes to fund important public services,” said Gardner. “The series of small-scale tax changes enacted in recent years have done little to change this imbalance.”

Despite the unpopularity of property taxes among taxpayers, and despite a series of blue-ribbon commissions recommending a reduction in property taxes,

lawmakers have continued to make property taxes the workhorse of the Illinois tax structure.

The state income tax, traditionally used by states to partially offset the impact of sales and property taxes on low-income taxpayers, falls heavily on low-income Illinoisans.

“Illinois has done relatively little to shelter low-income taxpayers from the income tax,” said Gardner. “At the same time, lawmakers have been more than willing to grant wealthier taxpayers loopholes that reduce their effective tax rate below the rate paid by middle-class taxpayers.”

Each of the state’s major taxes — income, sales and property — include targeted tax breaks which provide little or no benefit to large groups of

Illinoisans while providing smaller groups with substantial tax reductions.

- The state sales tax applies to sales of goods, but not services. For example, a low-income taxpayer purchasing a roach trap is taxed, but a wealthier taxpayer hiring an exterminator is exempt.
- The state income tax allows a credit for educational expenses which is unavailable to many low-income families with children, and exempts all pension and Social Security benefits received by elderly taxpayers — while fully taxing all wages earned by seniors.
- Illinois provides several types of property tax relief to homeowners — but the biggest of them, the 5 percent property tax credit, is less useful for low-income homeowners because it is applied as a credit against personal income taxes. Taxpayers who are property rich but income poor may not receive this credit at all. And taxpayers who rent, rather than own, their home, are completely ineligible for the property tax credit. Finally, the low-income circuit breaker provides tax relief for substantially less of the population — and provides less tax relief to those that receive it — than when it was first enacted.
- The corporate income tax “single sales factor” benefits large manufacturing firms while *increasing* tax liability for smaller firms that sell their goods in Illinois.

Each of these tax breaks undermine the perceived fairness of the Illinois tax system by treating similarly situated taxpayers in very different ways.

Balancing Act presents a detailed description of 30 options for resolving the sources of imbalance in the Illinois tax system and includes revenue-raising proposals, revenue-neutral “tax swap” options, and revenue-reducing options.

The report is available free of charge on the ITEP website at <http://www.itepnet.org/ilmenu.htm>.

more on Enron . . .

. . . and how research by
CTJ's Bob McIntyre
helped to turn up the heat on
America's seventh-largest corporation

Terry Gross, host of National Public Radio's *Fresh Air*, interviewed New York Times reporter David Cay Johnston as part of the January 23, 2002 broadcast. Gross asked Johnston, a 2001 Pulitzer Prize winner, about his reports on Enron.

Terry Gross: Last week, David Cay Johnston broke the story that Enron paid no taxes in four out of the last five years, and was actually eligible for \$382 million in tax refunds. I asked David Cay Johnston how he discovered that Enron avoided paying taxes.

David Cay Johnston: One of the things I spend an inordinate amount of time doing is reading footnotes in financial statements. And you know, companies organize their annual reports to make it appear that they are very heavily taxed. But if you know how to read the footnotes and you go and start examining them, you can figure out how much they actually wrote a check for, and how much they deferred into the future, and how much they got in a refund.

And in this case, after I had done a rough analysis of it, I went to **Bob McIntyre at Citizens for Tax Justice**. He is from a labor-funded group that believes the tax system is unfair to the poor in this country, but his analyses are accepted by everybody I know in Washington, across the political spectrum, as being honest on the numbers. That is, people that disagree with his view of the world agree that his numbers are all honest.

And it turned out that he had run the numbers that very afternoon when I called [sic], and he came up with the figures that we used: that in four out of five years, Enron paid no taxes and was eligible for refunds of \$382 million during that time period. . . .

TG: What was the fact-checking process like at *The New York Times* when you reported this information?

DCJ: Well the fact-checking process is, every time you write a story like that, you put your job on the line — literally, Terry.

TG: Tell me more.

DCJ: I mean, . . . let's say the next day Enron had come back and said, “Here's copies of our tax returns; we paid a billion dollars in those five years” — I at least couched the story in terms of “Here's what the public record shows” — but you know, I would have been in a lot of trouble about that. That's the fundamental fact-checking system that is employed by big newspapers. People have track records; they either get it right or they don't get it right.

Corporate Loophole Lobbying Conquers House

Misdirected house "stimulus" bill gives corporate tax avoiders \$8 for every dollar for unemployed workers

AS WE GO TO PRESS . . .

March 8th — Senate "rubber stamps" bill 85 - 9.
March 9th — President Bush signs it into law.

The so-called "stimulus" bill that the House overwhelmingly passed March 7th offers the same \$114 billion in corporate tax concessions over the next three years as the failed bill House Republicans put forward last December. Despite growing public pressure on House GOP leaders to pass a clean extension of unemployment benefits, almost all House Democrats cravenly joined in kowtowing to corporate special interests instead.

The changes will wipe out more than a fifth of otherwise expected corporate income tax payments over the next three years. In doing so, the bill provides \$8 in corporate tax cuts for every dollar allocated to help unemployed workers.

The centerpiece of the corporate tax-break program remains the same: 30 percent in extra "depreciation" write-offs in each of the next three years, at an estimated cost of \$97 billion. This new loophole will supposedly sunset thereafter, but experience shows that it is more likely to be routinely extended. Last year, Democrats correctly condemned the three-year plan as far too costly and economically nonsensical.

Like the December legislation, the new bill offers \$9 billion in tax relief to multinational corporations using offshore tax havens to shelter their U.S. profits from taxes. It also makes it easier for companies with an excess of loopholes to apply for rebates of taxes paid in earlier years, and waives the corporate AMT's curbs on profitable companies using the new loopholes to pay little or no tax. Also like the earlier bill, the new bill provides \$15 billion in extended unemployment and welfare benefits over the next three years.

"Every penny of this unwarranted batch of corporate giveaways will come straight out of the Social Security trust fund," said Citizens for Tax Justice director Robert S. McIntyre.

There are some changes from the failed December legislation. The new bill drops a \$14 billion Democratic effort to extend last year's tax rebates to low-income people who were ineligible. It also scraps almost all of the other individual tax cuts in the earlier bill and drops a contentious plan to completely repeal the corporate alternative minimum tax (which in its December version would have cost \$6 billion over the next 3 years).

Assuming future extension of the supposedly "temporary" corporate tax loopholes, the bill will slash corporate taxes by some \$330 billion over the upcoming decade.

"Every penny of this unwarranted batch of corporate giveaways will come straight out of the Social Security trust fund," said Citizens for Tax Justice director Robert S. McIntyre. "Those who voted for it should be ashamed to style themselves as defenders of Social Security, fiscal responsibility or tax fairness. And they should stifle their

**The March 2002 "Stimulus Bill" and its Predecessor
 Cost FY 2002 – 2004**

	Mar. 02	Dec. 01
Corporate tax cuts	-114.0	-114.7
Individual tax cuts	-1.4	-56.7
Miscellaneous tax changes	+6.3	+6.3
Total tax changes	-109.2	-165.1
Unemployment & TANF	-14.6	-15.1
Total cost	-123.8	-180.1

hypocritical complaints about Enron's egregious tax avoidance, too."

Unlike some organizations, CTJ uses its newsletter as the principal means of asking for your financial support. And, I am happy to report, many of our readers and members respond by sending one or more contributions to us each year.

In spite of the fact that we need every dollar we can get our hands on (it costs money to take on the Enrons of the world) you won't find us in your mailbox every month. For one thing, those mailings cost a lot of money.

Yes, I know. Sometimes, you have to spend money to make money. But our experience is that this newsletter offers the best of both worlds — the chance to get "tax news you can use" to your doorstep and, in return, your gracious and generous contribution so we may continue our work.

Recently, however, several of our supporters have told me that they would like to receive an annual membership renewal letter. I would prefer to continue with the newsletter as our principal means of asking for your financial support. But I would first like to hear your suggestions for renewing memberships — or just about anything else on the topic of tax fairness! Please write me at the address below, or send an email message to me at bruben@ctj.org or call me at 888-626-3780 x 25. I like hearing from you. Thanks, as always, for your terrific support. And know that we are very much a "shoestring" operation, so your money is put to good use!

Thanks for your support!

Bonnie Rubenstein
Development Director