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Christopher H. Hanna
Southern Methodist University, Dedman School of Law

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MOORE, THE SIXTEENTH AMENDMENT, AND THE UNDERPINNINGS OF THE DEEMED REPATRIATION PROVISION

Christopher H. Hanna[*]

ABSTRACT

In *Moore v. United States*, the U.S. Supreme Court will consider a rare Sixteenth Amendment case. On its face, the case deals with deemed repatriation, a discrete provision of the 2017 Tax Cuts and Jobs Act that included in income past accumulated earnings held abroad. This short Article seeks to contextualize the deemed repatriation provision in terms of why it was passed and how it comports with principles underlying the U.S. tax code. Drawing on firsthand experience researching and drafting the Tax Cuts and Jobs Act, the Article shows the analysis that went into enacting the provision, focusing on the traditional elements of tax reform and legislation: equity, efficiency, and simplicity.

I. INTRODUCTION

On June 26, 2023, the U.S. Supreme Court granted the taxpayer's petition for writ of certiorari in *Moore v. United States*,[1] concerning whether the deemed repatriation provision under Section 965 is constitutional.[2] The specific question

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[*] Alan D. Feld Endowed Professor of Law and Altshuler Distinguished Teaching Professor, SMU Dedman School of Law, Dallas, Texas; Senior Policy Advisor for Tax Reform, U.S. Senate Committee on Finance, 2011–2018. I thank Jennifer Acuna, George Callas, Tony Coughlan, Susan Morse, Mark Prater, and Eric Ruben for their comments on an early draft of this Article.

1. Moore v. United States, No. C19-1539, 2020 WL 6799022 (W.D. Wash. Nov. 19, 2020), *aff'd*, 36 F.4th 930 (9th Cir. 2022), *cert. granted*, 143 S. Ct. 2656 (2023).

2. The deemed repatriation provision under Section 965 is sometimes referred to as the transition tax, deemed repatriation tax, mandatory repatriation tax, or mandatory deemed repatriation tax. *See The Continuing US Tax Impact Of The 'One-Time' Section 965 Transition Tax*, WITHERSWORLDWIDE (Oct. 30, 2020), https://www.withersworldwide.com/en-

presented is "[w]hether the Sixteenth Amendment authorizes Congress to tax unrealized sums without apportionment among the states."[3]

The code section in question, Section 965, was enacted as part of the Tax Cuts and Jobs Act (TCJA),[4] which President Donald J. Trump signed into law on December 22, 2017.[5] Generally, the Section provides that a U.S. shareholder that owns 10% or more of a deferred foreign income corporation must include in its gross income (as Subpart F income), its pro rata share of the greater of accumulated post-1986 deferred foreign income of such foreign corporation as of November 2, 2017, or December 31, 2017.[6] That amount is taxed at 8%, 15.5%, or a combination of both rates depending on the U.S. shareholder's pro rata share of the cash position of the foreign corporation.[7]

Generally, the taxpayer's argument in *Moore* is that Section 965 requires the taxpayer to include an amount in gross income for which no realization event has taken place.[8] And, the argument goes, that the federal income tax requires a realization event.[9] Without the realization event, according to the taxpayer, the tax is not an income tax, and therefore must be apportioned among the states.[10]

This Article will discuss the background leading to the enactment of Section 965. In addition, it will cover the policy discussion behind Section 965 and some of the major issues that were discussed as part of its enactment. As this Article shows, the discussion relating to the enactment of Section 965 did not feature concerns about the realization doctrine. Rather, Section 965 was viewed as a necessary piece of U.S. international tax reform and represented an effort to tax income that U.S. multinationals had earned but not repatriated in a fair, efficient, and simple manner.

II. BACKGROUND

As part of the TCJA, Congress substantially changed the U.S. international tax system.[11] Prior to enactment of TCJA, the United States had a worldwide

gb/insight/read/the-continuing-us-tax-impact-of-the-one-time-section-965-transition-tax [https://perma.cc/X5WJ-WGK4].

3. Petition for Writ of Certiorari at i, *Moore*, 143 S. Ct. 2656 (2023) (No. 22-800), 2023 WL 2241819.

4. Although the tax reform enacted in 2017 is often referred to as the Tax Cuts and Jobs Act, its actual title is "An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018." Pub. L. No. 115-97, 131 Stat. 2054 (2017).

5. *Id.* Congress originally enacted Section 965 in 2004 as part of the American Jobs Creation Act of 2004. American Jobs Creation Act of 2004, Pub. L. No. 108-357, § 422(a), 118 Stat. 1418, 1514–15. It had temporary application and was in essence dormant for many years prior to the enactment of the Tax Cuts and Jobs Act in 2017.

6. I.R.C. § 965(a). November 2, 2017, was the date the Tax Cuts and Jobs Act was introduced in the House of Representatives as H.R. 1. H.R. 1, 115th Cong. (2017).

7. I.R.C. § 965(c).

8. Reply Brief for Petitioners at *1, *Moore*, 143 S. Ct. 2656 (2023) (No. 22-800), 2023 WL 3778866.

9. *Id.*

10. *Id.*

11. *Compare* I.R.C. §§ 951, 951A (subjecting U.S. shareholders of a controlled foreign corporation to immediate taxation on income earned by a controlled foreign corporation), *with* J. Clifton Fleming, Jr. et al., *Worse than Exemption*, 59 EMORY L.J. 79, 87–89 (2009) (explaining the

deferral system with a credit for income taxes paid to a foreign country.[12] More specifically, "the United States taxed the income of foreign subsidiaries of U.S. multinationals with a credit for foreign income taxes paid but only when the earnings were repatriated to the United States, typically by way of a dividend."[13] As part of the TCJA, Congress shifted the U.S. international tax system, eliminating much of the deferral of U.S. tax but also providing an exemption from U.S. tax for a portion of the foreign subsidiary's earnings.[14]

One goal in reforming the U.S. international tax system was to eliminate as much as possible the so-called lock-out effect.[15] Generally, the lock-out effect referred to U.S. multinationals not repatriating their foreign earnings (from low-tax countries) so as to avoid the high U.S. tax that would apply on such repatriation.[16] Such foreign earnings were said to be locked out of the United States because of the high U.S. tax on repatriation.[17] Throughout the seven years when international tax reform was under consideration, the question of how to tax these locked-out (or unrepatriated, or accumulated) earnings upon transition continued to arise.

The development of the current U.S. international tax system began in January 2011 when Representative Dave Camp (R-MI) ascended to the chair of the House Ways and Means Committee after the Republicans claimed the majority in the House of Representatives in the November 2010 elections.[18] In his role as Chairman of the House Ways and Means Committee, Camp made comprehensive tax reform his top policy priority, and even though he was no longer a member of Congress when tax reform was finally accomplished in December of 2017, he could be viewed as the single most important individual behind the first successful tax reform effort in over 30 years.[19]

Camp had his staff begin work on tax reform in early 2011.[20] His staff spent a number of months developing a discussion draft for international tax, which

deferral system in which U.S. multinationals generally did not owe U.S. tax on income earned by a controlled foreign corporation until the corporation repatriated the income to the United States).

12. Christopher H. Hanna & Cody A. Wilson, *U.S. International Tax Policy and Corporate America*, 48 J. CORP. L. 261, 262 (2023).

13. *See id.*

14. I.R.C. §§ 245A (100% deduction for foreign-source portion of dividends received by domestic corporations from specified 10% owned foreign corporations), 951 (Subpart F income included in gross income of United States shareholders), 951A (global intangible low-taxed income included in gross income of United States shareholders); *see also* Hanna & Wilson, *supra* note 12, at 267 (providing details of the new U.S. international tax system).

15. *See* REP. STAFF OF S. COMM. ON FIN., 113TH CONG., COMPREHENSIVE TAX REFORM FOR 2015 AND BEYOND, S. Prt. No. 113-31, at 253 (2014) [hereinafter SFC 2014 REPORT].

16. *See Tax Talk: The $2+ Trillion Lockout*, U.S. S. COM. ON FIN. (July 26, 2017), https://www.finance.senate.gov/chairmans-news/tax-talk-the-2-trillion-lockout. [https://perma.cc/C9JM-995U].

17. *Id.*

18. Press Release, U.S. House of Rep., Comm. on Ways & Means, Camp Selected as Ways and Means Chairman (Jan. 5, 2011), https://gop-waysandmeans.house.gov/camp-selected-as-ways-and-means-chairman-2/ [https://perma.cc/7ARJ-X77M].

19. *See* Hanna & Wilson, *supra* note 12, at 264.

20. *See* Press Release, U.S. House of Rep., Comm. on Ways & Means, Camp Releases International Tax Reform Discussion Draft (Oct. 26, 2011), https://gop-

was released on October 26, 2011.[21] In the discussion draft, Camp proposed shifting the U.S. international tax system from a worldwide deferral system to a territorial type of system.[22] This was accomplished through a 95% deduction of dividends received by a U.S. multinational from its foreign subsidiaries.[23] In addition, the discussion draft contained a mandatory deemed repatriation of accumulated foreign earnings and profits taxed at a reduced rate of 5.25% to be paid over a period of up to eight years.[24] The rate of 5.25% was consistent with the rate of the elective repatriation that was enacted as part of the American Jobs Creation Act of 2004.[25] At the time of Camp's discussion draft, many estimates of accumulated foreign earnings were about $1 to $1.5 trillion.[26]

A few months later, the late Senator Mike Enzi (R-WY) released his own discussion draft on international taxation.[27] Enzi also proposed a 95% deduction for dividends received by a U.S. multinational from its foreign subsidiaries but took a very different approach than Camp in addressing the accumulated foreign earnings of such subsidiaries.[28] Under the Enzi draft, U.S. multinationals could make an election to include in gross income their pro rata share of the foreign earnings currently being held offshore.[29] These earnings would be taxed at a reduced U.S. tax rate through a 70% deduction.[30] The tax due on these earnings could be paid over a period of up to eight years.[31] If a company chose not to make the election, then such earnings would be subject to the full U.S. tax rate when the earnings were brought back to the United States.[32]

waysandmeans.house.gov/camp-releases-international-tax-reform-discussion-draft/ [https://perma.cc/8W2M-EMSE].

21. *Id.*

22. *Id.*

23. *Id.*

24. COMM. FOR RESPONSIBLE FED. BUDGET, REFORMING THE CORPORATE TAX CODE 9 (2012), https://www.crfb.org/sites/default/files/documents/Reforming_the_Corporate_Tax_Code.pdf [https://perma.cc/A7VE-74AB].

25. American Jobs Creation Act of 2004, Pub L. No. 108-357, § 422(a), 118 Stat. 1418.

26. *See, e.g.*, Jesse Drucker et al., *Lobbying for a Trillion-Dollar Tax Holiday*, BLOOMBERG (Sept. 29, 2011, 5:56 PM), https://www.bloomberg.com/news/articles/2011-09-29/lobbying-for-a-trillion-dollar-tax-holiday#xj4y7vzkg [https://perma.cc/TRG8-G82D] ("U.S. multinationals like Pfizer, Cisco, and Apple have parked more than $1.3 trillion in profit overseas, avoiding federal income taxes."); Patrick Temple-West, *Profit Tax Holiday Could Blunt US Exports -Gov't*, REUTERS (Oct. 31, 2011, 11:51 AM), https://www.reuters.com/article/usa-tax-crs/profit-tax-holiday-could-blunt-us-exports-govt-idUSN1E79U08F20111031 [https://perma.cc/4HCB-4TLM] ("An estimated $1.2 trillion to $1.5 trillion in U.S. corporate profits is presently parked abroad avoiding the corporate income tax."); Kevin Drawbaugh, *Fitch Slams Proposed Foreign Profit Tax Break*, REUTERS (Oct. 6, 2011, 10:45 AM), https://www.reuters.com/article/us-usa-tax-hagan/fitch-slams-proposed-foreign-profit-tax-break-idUSTRE79558120111006 [https://perma.cc/B27D-D9SB] ("Corporations are sitting on an estimated $1.5 trillion in overseas profits.").

27. United States Job Creation and International Tax Reform Act of 2012, S. 2091, 112th Cong. (2012); 158 CONG. REC. 1371–72 (2012) (statement of Sen. Michael B. Enzi).

28. United States Job Creation and International Tax Reform Act of 2012, S. 2091, 112th Cong. § 101(a) (2012).

29. *Id.* § 104.

30. *Id.*

31. *Id.*

32. *Id.*

Meanwhile, after the release of the 2011 discussion draft, Camp received substantial feedback that, because a significant portion of accumulated foreign earnings had been re-invested in foreign illiquid assets, the 5.25% rate imposed a high burden on such earnings. At the same time, some U.S. multinationals continued to accumulate large sums of foreign earnings in low-tax jurisdictions, which they held as cash and cash equivalents, refusing to repatriate such earnings due to the high U.S. residual tax.[33] The dichotomy between earnings re-invested in illiquid assets and earnings simply held offshore as cash to avoid U.S. tax led to pressure from the business community to impose a lower rate on illiquid assets than on cash and cash equivalents.

On February 26, 2014, Camp released draft legislation entitled the Tax Reform Act of 2014.[34] Near the end of 2014, he formally introduced that draft as H.R. 1, the Tax Reform Act of 2014.[35] As part of his tax plan, Camp proposed a two-tier rate schedule for the accumulated foreign earnings in transitioning to a territorial-type of international tax system.[36] The Camp proposal would deem accumulated post-1986 foreign earnings, currently held abroad in cash, as repatriated and taxed at once at an effective 8.75% rate achieved through a 75% deduction.[37] Any remaining non-cash post-1986 accumulated foreign earnings held abroad (for example, foreign income that had been reinvested in property, plant, and equipment) would be deemed repatriated and taxed at an effective 3.5% rate achieved through a 90% deduction.[38] The taxpayer had the option to pay the tax over an eight-year period.[39]

Based on feedback from certain elements of the business community, Chairman Camp's 2014 proposal also introduced an opportunity for individual (i.e., non-corporate) taxpayers owning 10% or more of a foreign corporation—and therefore subject to the deemed repatriation provision—to avoid paying their share of the tax on accumulated foreign earnings.[40] The proposal allowed individual taxpayers to contribute their shares to a subchapter S corporation which would enable them to defer payment of the tax until the occurrence of a specified triggering event. The triggering events, which would have caused an immediate requirement to pay the full tax, generally related to transactions that

33. Jena McGregor, *Tim Cook, the interview: Running Apple 'is sort of a lonely job'*, WASH. POST (Aug. 13, 2016), https://www.washingtonpost.com/sf/business/2016/08/13/tim-cook-the-interview-running-apple-is-sort-of-a-lonely-job/ [https://perma.cc/2LDE-F5YL] ("The tax law right now says we can keep that in Ireland or we can bring it back. And when we bring it back, we will pay 35 percent federal tax and then a weighted average across the states that we're in, which is about 5 percent, so think of it as 40 percent. We've said at 40 percent, we're not going to bring it back until there's a fair rate. There's no debate about it.").

34. Press Release, U.S. House of Rep., Comm. on Ways & Means, Camp Releases Tax Reform Plan to Strengthen the Economy and Make the Tax Code Simpler, Fairer and Flatter (Feb. 26, 2014), https://waysandmeans.house.gov/camp-releases-tax-reform-plan-to-strengthen-the-economy-and-make-the-tax-code-simpler-fairer-and-flatter/ [https://perma.cc/D5N4-MJWY].

35. Tax Reform Act of 2014, H.R. 1, 113th Cong. (2014).

36. *Id.* § 4003.

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.*

could result in the transfer of the shares in the foreign corporation to a U.S. corporation eligible for the section 245A dividends-received deduction.

III. U.S. INTERNATIONAL TAX SYSTEM ENACTED AS PART OF THE TAX CUTS AND JOBS ACT[41]

After enactment of TCJA, generally, the earnings of a controlled foreign corporation (CFC) of a U.S. multinational can be placed into one of three categories.[42] The first category is Subpart F income, which is generally mobile or passive income that continues to be covered by pre-TCJA law.[43] Mobile income is referred to as foreign base company sales income and foreign base company services income.[44] Foreign base company sales income is generally income derived by a CFC from the purchase or sale of personal property involving a related party in which the goods are manufactured and sold for use or consumption outside the CFC's country of incorporation.[45] Foreign base company services income is income derived by a CFC in connection with the performance of technical, managerial, engineering, architectural, scientific, skilled, industrial, commercial, or like services for or on behalf of any related person outside the CFC's country of organization.[46] Passive income, referred to as foreign personal holding company income, generally includes income of a CFC such as dividends, interest, royalties, rents, annuities, and net gains on dispositions of property producing any of the foregoing types of income.[47] Subpart F income is taxed annually (in the year earned by the CFC) to the U.S. parent corporation at the U.S. corporate tax rate (i.e., no deferral), which is currently 21%.[48] A credit is provided for foreign income taxes paid on Subpart F income, with any unused credits carried back one year and forward for up to ten years.[49]

The second category of income of a CFC is tested income/global intangible low-taxed income (GILTI), a new category created by TCJA.[50] Income in this second category is generally income that is not Subpart F income, and which exceeds 10% of the adjusted basis of depreciable tangible property of the foreign subsidiary (referred to as a "qualified business asset investment" or QBAI).[51] Income in this category is taxed annually to the U.S. parent corporation (i.e., no deferral) at effectively half of the U.S. corporate tax rate, which is achieved

41. The discussion in this section previously appeared in Hanna & Wilson, *supra* note 12, at 267–271.
42. *See id.* at 267.
43. I.R.C. § 951(a).
44. I.R.C. §§ 954(d)(1)(A)–(B), 954(e)(1)(A)–(B).
45. I.R.C. § 954(d)(1)(A)–(B).
46. I.R.C. § 954(e)(1)(A)–(B).
47. I.R.C. §§ 954(a)(1), (c)(1).
48. I.R.C. §§ 11, 951.
49. I.R.C. §§ 904(c), 960(a).
50. I.R.C. §§ 951A(b), (c).
51. I.R.C. § 951A(c)(2)(A); Treas. Reg. §§ 1.951A-2(b)(1), (c) (2022).

through a 50% deduction of GILTI.[52] A credit is provided for foreign income taxes paid on tested income.[53] The credit is reduced by 20%, and any unused credits may not be carried back or forward and are therefore either utilized in the current year or lost.[54]

The third category of income is a residual category—income that is not Subpart F income or GILTI and that is, as a practical matter, exempt from U.S. taxation.[55] It is generally composed of income up to 10% of the adjusted basis of the QBAI of the foreign subsidiary, known as a CFC's net deemed tangible income return.[56] But it also includes high-taxed Subpart F income and high-taxed GILTI if elected pursuant to the high-tax exception.[57] The residual category income is deferred from U.S. taxation until repatriated to the U.S. multinational by way of dividends.[58] Upon repatriation, it technically is subject to U.S. taxation, but the U.S. multinational is entitled to a Section 245A 100% dividends-received deduction, with the result of an effective U.S. tax rate of zero on income in the third category.[59] No foreign tax credits are permitted for income in the residual category.[60]

The current U.S. international tax system can be viewed in at least one of four ways.[61] These views are organized in the Table below. First, it is a hybrid territorial/worldwide tax system.[62] The first category of income of a CFC—Subpart F income—represents the worldwide nature of the current system.[63] It is taxed in full by the United States.[64] The third category of income—the residual category—is not taxed at all by the United States, representing the territorial

52. I.R.C. §§ 250(a)(1)(B), (a)(2). The 50% deduction declines to 37.5% beginning in 2026. I.R.C. § 250(a)(3)(B).

53. I.R.C. § 960(d).

54. I.R.C. §§ 904(c)–(d)(1)(A), 960(d).

55. I.R.C. § 951A(b).

56. *Id.*

57. Treas. Reg. §§ 1.951A-2(c), 1.954-1(d)(1) (2022). The Subpart F high-tax exception is provided in the Tax Code. I.R.C. § 954(b)(4). A very limited GILTI high-tax exception is provided in the Tax Code. *See* I.R.C. § 951A(c)(2)(A)(i)(III). The Treasury, through regulations, expanded the GILTI high-tax exception, although some members of Congress objected, feeling that the Treasury had exceeded its authority in doing so. *See* Treas. Reg. § 1.951A-2 (2022); Press Release, U.S. Senate, Comm. on Fin., Wyden Statement on GILTI High-Tax Exception Regulations (July 20, 2020), https://www.finance.senate.gov/ranking-members-news/wyden-statement-on-gilti-high-tax-exception-regulations [https://perma.cc/67VZ-Z8Y7]; Press Release, U.S. Senate, Comm. on Fin., Wyden, Brown Introduce Bill to Block Latest Trump Administration Corporate Giveaway (Feb. 12, 2020), https://www.finance.senate.gov/ranking-members-news/-wyden-brown-introduce-bill-to-block-latest-trump-administration-corporate-giveaway [https://perma.cc/5LYS-XH3K].

58. I.R.C. § 245A(a).

59. I.R.C. §§ 245A(a), 951A(b)(1).

60. I.R.C. § 245A(d)(1).

61. *See* Hanna & Wilson, *supra* note 12, at 269–71.

62. The hybrid modifier is necessary because the goal of a territorial tax system is to tax income only in its source jurisdiction. *See* SFC 2014 REPORT, *supra* note 15, at 246; KYLE POMERLEAU & KARI JAHNSEN, TAX FOUND., DESIGNING A TERRITORIAL TAX SYSTEM: A REVIEW OF OECD SYSTEMS (Rachel Shuster ed., July 2017), https://files.taxfoundation.org/20170822101918/Tax-Foundation-FF554-8-22.pdf [https://perma.cc/N3HF-BGHJ] (providing an overview of taxing foreign profits).

63. I.R.C. § 952.

64. I.R.C. § 951.

nature of the current system.[65] The second category—GILTI—partially represents a worldwide system and partially represents a territorial system.[66] It is taxed by the United States, reflecting its worldwide nature. But it is effectively only partially taxed by the United States through a 50% deduction, reflecting its territorial nature.[67]

A second view is that the current system is a hybrid no-deferral/deferral system. Both Subpart F income and GILTI are taxed annually to the U.S. parent of the CFC.[68] There is no deferral of the taxes owed on the income.[69] With respect to the third category of income—the residual category—the taxing event does not occur until the income is repatriated by way of dividends to the U.S. parent.[70] And, in almost all cases, the U.S. parent qualifies for a Section 245A 100% dividends-received deduction.[71] As a result, the residual category of income is deferred from U.S. taxation but ultimately not taxed by the United States.

A third view is that the system is an overall system, as opposed to a country-by-country one. The second category of income—GILTI—is thought to be the largest category of income of most CFCs. It is applied as an aggregate of income and not on a country-by-country basis.[72] More specifically, each CFC computes its tested income or tested loss.[73] These amounts are aggregated for all CFCs of the U.S. parent and result in net tested income.[74] In addition, QBAI is aggregated for all CFCs.[75] GILTI is the excess (if any) of net tested income over 10% of QBAI.[76] GILTI is not determined on a CFC-by-CFC basis or a country-by-country basis.[77]

65. I.R.C. § 245A.
66. I.R.C. § 951A.
67. I.R.C. § 250.
68. I.R.C. §§ 11(b), 951(a); 951A.
69. *Id.*
70. I.R.C. §§ 61(a)(7), 245A(a).
71. *See* Hanna & Wilson, *supra* note 12, at 269.
72. The Treasury Department has issued regulations permitting an expanded high-tax exception for GILTI, similar to the high-tax exception for Subpart F income. Treas. Reg. § 1.951A-2(c) (as amended in 2020). In calculating the effective foreign tax rate to apply the exception, in essence, a country-by-country determination is made. The Treasury has also issued proposed regulations conforming the high-tax exception for Subpart F income with the expanded high-tax exception for GILTI. Guidance under Section 954(b)(4) Regarding Income Subject to a High Rate Foreign Tax, 85 Fed. Reg. 44650 (July 23, 2020) (codified at 26 C.F.R. pt. 1). President Biden and Congress have proposed applying GILTI on a country-by-country basis. *See* U.S. DEP'T OF TREASURY, GENERAL EXPLANATIONS OF THE ADMINISTRATION'S FISCAL YEAR 2022 REVENUE PROPOSALS 4–8 (May 2021); Build Back Better Act, H.R. 5376, 117th Cong., § 138126 (2021).
73. I.R.C. § 951A(c)(2).
74. I.R.C. § 951A(c)(1).
75. I.R.C. § 951A(b)(2).
76. I.R.C. § 951A(b)(1).
77. In July 2020, the Treasury released the final GILTI high-tax exception regulations. The final regulations adopt a tested unit approach in calculating the foreign effective tax rate. Treas. Reg. § 1.951A-2(c)(7)(iv)(A) (as amended in 2020). Under a tested unit combination rule, all tested units of a U.S. shareholder that are tax residents or located in the same foreign country are treated as a single tested unit. *Id.* § 1.951A-2(c)(7)(iv)(C). The result of the tested unit combination rule in the final regulations is that the foreign effective tax rate for purposes of applying the GILTI high-

Finally, and probably most importantly, the current U.S. international tax system is a tax on supernormal or excess returns earned by a CFC, which are generally returns associated with an intangible asset.[78] An excess or supernormal return is a return that generally cannot be duplicated and is thought in most, if not all, cases to arise from skill or luck and not simply from a capital investment.[79] Supernormal returns can be taxed at high rates because they cannot be duplicated; therefore, the investment will continue.[80] However, because such returns are generally associated with intangible assets, which are highly mobile, it is thought that taxing such returns at a high rate will cause the intangible to migrate to a low-tax jurisdiction.[81] GILTI, which is the excess of tested income of a CFC over 10% of its QBAI, represents the excess or supernormal return.[82] The 10% of QBAI represents the normal return, which is effectively exempt from U.S. tax by falling into the third category of income—the residual category.[83]

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tax exclusion is determined on a country-by-country basis. This means that, in one aspect, GILTI is applied on a country-by-country basis.

78. The focus and discussion of supernormal returns did not enter the tax law literature until the mid-1990s, so it is a relatively recent development in tax policy. *See, e.g.*, William M. Gentry & R. Glenn Hubbard, *Distributional Implications of Introducing a Broad-Based Consumption Tax*, 11 TAX POL'Y & ECON. 1, 2 (1997); Alvin C. Warren, Jr., *How Much Capital Income Taxed Under an Income Tax is Exempt Under a Cash Flow Tax?*, 52 TAX L. REV. 1 (1996); Richard A. Musgrave, *Clarifying Tax Reform*, 70 TAX NOTES 731 (1996). And even more recent is the association of supernormal returns and intangible assets. Former House Ways and Means Chairman Dave Camp noted the linkage in his discussion draft of international taxation in October 2011. *See* Press Release, Camp Releases International Tax Reform Discussion Draft, *supra* note 20.

79. *See, e.g.*, Warren, *supra* note 78, at 5; David Elkins & Christopher H. Hanna, *Taxation of Supernormal Returns*, 62 TAX LAW. 93, 102 (2008) ("[S]upernormal return should not be considered an element of the return on capital but rather a return on skill or labor or, in some cases, simply a windfall."); CHRISTOPHER H. HANNA, TAX POLICY IN A NUTSHELL 87–88 (2d ed. 2022) ("[S]upernormal return . . . is the return due to a unique idea, entrepreneurial skill, or simply luck.").

80. *See generally* Reuven S. Avi-Yonah, *A New Corporate Tax*, 168 TAX NOTES FED. 653, 657–58 (July 27, 2020) (describing how these types of returns can be taxed at rates up to 80% at a very high-income threshold).

81. *See* Hanna & Wilson, *supra* note 12, at 270.

82. *Id.*

83. I.R.C. §§ 245A(a), 951A(b)(2).

Table: Summary of Ways to View the Current U.S. International Tax System

Income Category	**Territorial/ Worldwide**	**No Deferral/ Deferral**	**Overall/Country -by-Country**	**Supernormal Returns**
Subpart F Income	Worldwide	No Deferral	CFC-by-CFC	N/A
GILTI	Part Worldwide/ Part Territorial	No Deferral	Overall	Taxed
Residual	Territorial	Deferral	Overall	N/A

As a result of the enactment of the new U.S. international tax regime in TCJA, lock-out is no longer an issue. Much of the earnings of a CFC will be taxed annually to the U.S. shareholders with no deferral and no U.S. tax on repatriation of such earnings. And any CFC earnings that are deferred can be repatriated with no U.S. tax as a result of the section 245A 100% dividends-received deduction.

IV. RATIONALE FOR DEEMED REPATRIATION PROVISION

During enactment of the new U.S. international tax regime as part of TCJA, Congress gave a great deal of thought to the tax treatment of the accumulated foreign income held by foreign subsidiaries of U.S. shareholders, with many of the shareholders being U.S. multinationals. This accumulated foreign income represented income that had been earned by foreign subsidiaries but that had not been repatriated, in part because of the lock-out effect. Much of the discussion focused on three traditional elements of tax legislation and reform: equity, efficiency, and simplicity.

As noted, as part of TCJA, Congress shifted the U.S. international tax system from a worldwide deferral system to a territorial type of system.[84] U.S. multinationals had accumulated well over $2 trillion in foreign earnings at the time of enactment of TCJA, with approximately $1 trillion in cash, held mostly in U.S. fixed income securities.[85] Discussion ensued on whether those accumulated foreign earnings should be taxed and if so, at what rate or rates.

84. *Repatriation*, TAX. FOUND., https://taxfoundation.org/taxedu/glossary/repatriation/ [https://perma.cc/45XK-FF8R] (last visited Sep. 26, 2023).

85. *See, e.g.*, Letter from Thomas A. Barthold, Chief of Staff, Joint Comm. on Taxation, to Hon. Kevin Brady and Hon. Richard Neal (Aug. 31, 2016), https://waysandmeans.house.gov/wp-content/uploads/2016/09/20160831-Barthold-Letter-to-BradyNeal.pdf [https://perma.cc/56GD-ZPVU] ("The most recent year for which we have tax return data reporting the amount of undistributed post-1986 not previously taxed earnings and profits is 2012. The Statistics of Income Division of the Internal Revenue Service has reported that the end of year accumulated amount of undistributed earnings and profits for CFCs was $2.3 trillion. Given ordinary growth of the world economies and corporate earnings and profits, we estimate that undistributed post-1986 not previously taxed earnings for 2015 were approximately $2.6 trillion."); INST. ON TAX'N AND ECON. POL'Y & U.S. PIRG EDUC. FUND, OFFSHORE SHELL GAMES 2017 (Oct. 17, 2017) ("Fortune 500 companies are holding more than $2.6 trillion in accumulated profits offshore for tax purposes."); Jesse Drucker, *How Tax Bills Would Reward Companies That Moved Money Offshore*, N.Y. TIMES (Nov. 29, 2017), https://www.nytimes.com/2017/11/29/business/taxes-offshore-repatriation.html

The United Kingdom and Japan were two of the most recent countries to shift their international tax regime to a territorial type of system.[86] Both countries gave a free pass, whether knowingly or inadvertently, to the accumulated foreign earnings of their multinationals.[87] In other words, both countries did not tax the accumulated foreign earnings of foreign subsidiaries of their multinationals. Consideration was given to doing the same for U.S. multinationals but Congress decided that would result in an unfair benefit for such U.S. multinationals in addition to foregoing much-needed revenue.[88]

U.S. multinationals that had previously repatriated foreign earnings in the many years prior to the TCJA had been subject to a 35% top corporate tax rate on such repatriated earnings less any associated foreign tax credits.[89] It did not seem fair that a U.S. multinational that did not repatriate its earnings from its CFCs prior to enactment of tax reform would pay no U.S. tax on such earnings while a U.S. multinational that repatriated earnings immediately prior to enactment paid the full U.S. corporate tax rate of 35% less foreign tax credits.

Consideration was given to Senator Enzi's elective approach in his 2012 international tax discussion draft.[90] Congress, however, decided against this approach.[91] If the pre-enactment accumulated foreign earnings were subject to U.S. tax only if the earnings were brought back to the United States (the elective approach), then this would perpetuate indefinitely the very lock-out effect that the new U.S. international tax regime intended to eliminate.[92] It would also add complexity and administrative burden, in that taxpayers would have to track two pools of foreign earnings: a pool subject to the old deferral system and a pool subject to the new system. Faced with these choices, Congress decided that the simplest and most equitable solution was to wipe accumulated earnings off of

[https://perma.cc/R3FY-RZX3] ("Now, companies have accumulated approximately $2.8 trillion in profits offshore . . ."); Michael Smolyansky et al., *U.S. Corporations' Repatriation of Offshore Profits: Evidence from 2018*, BD. GOVERNORS FED. RES. SYS. (Aug. 6, 2019), https://www.federalreserve.gov/econres/notes/feds-notes/us-corporations-repatriation-of-offshore-profits-20190806.html [https://perma.cc/2GBK-6FHB] (". . . and, by the end of 2017, U.S. MNEs had accumulated approximately $1 trillion in cash abroad, held mostly in U.S. fixed-income securities.").

86. *See* SFC 2014 REPORT, *supra* note 15, at 251.

87. *Id.* at 253.

88. *Id.* at 254.

89. *Id.*

90. United States Job Creation and International Tax Reform Act of 2012, S. 2091, 112th Cong. (2012).

91. SFC 2014 REPORT, *supra* note 15, at 253–54.

92. *Id.* In addition, in early 2015, Senators Rand Paul (R-KY) and Barbara Boxer (D-CA) introduced an elective repatriation proposal with a 6.5% tax rate. Invest in Transportation Act, S. 981, 114th Cong. (2015). They claimed it would raise revenue, which would be used for the Highway Trust Fund. *Id.* But the JCT scored it as losing $117.9 billion over eleven years. *See, e.g.*, *Testimony of the Staff of the Joint Committee on Taxation Before the Select Revenue Measures Subcommittee of the House Committee on Ways and Means Hearing on the Taxation of the Repatriation of Foreign Earnings as a Funding Mechanism for a Multi-Year Highway Bill*, JCX-98-15 9 (June 24, 2015); Richard Rubin, *Repatriation Tax Break from Boxer, Paul Cost $118 Billion*, BLOOMBERG (Apr. 30, 2015, 6:07 PM), http://www.bloomberg.com/news/articles/2015-04-30/repatriation-tax-break-from-paul-boxer-would-cost-118-billion [https://perma.cc/MPY4-F92F].

taxpayers' books, but without giving them a windfall.[93] Thus, those historical earnings were taxed once, at reduced rates, and never to be taxed again. This was consistent with the approach taken by Camp in his 2011 and 2014 tax reform packages.[94]

Several major issues arose once a decision was made that the accumulated foreign earnings would be deemed repatriated to the U.S. shareholder. A U.S. shareholder would include its pro rata share of a foreign corporation's accumulated post-1986 deferred foreign income.[95] If the U.S. shareholder also had an interest in a foreign corporation that had an aggregate foreign earnings and profits deficit, could the pro rata share of the deficit amount offset the pro rata share of the accumulated deferred foreign income resulting in a net mandatory inclusion amount?[96] If the answer was no, that appeared to be taxing gross income rather than net income. Therefore, Congress allowed a pro rata share of the earnings and profits deficit in a CFC to offset the U.S. shareholder's pro rata share of the accumulated deferred foreign income of another CFC.[97] This approach was consistent with Camp's approach in 2011 and 2014.[98] In addition, the netting or overall approach would be consistent with the new U.S. international tax regime, which taxed tested income (or GILTI) on a net or overall basis rather than country-by-country or CFC-by-CFC.[99]

A second issue was the rate or rates that would apply to the accumulated foreign income. Camp in 2011 utilized a single rate of 5.25% achieved through a deduction equal to 85% of the amount included as Subpart F income.[100] That rate was consistent with the rate in 2004 when Section 965 was originally enacted and provided an elective mechanism for taxing accumulated foreign earnings. Enzi's elective approach in 2012 provided a rate of 10.5% achieved through a 70% deduction.[101] Camp, in 2014, however, introduced a two-tier rate system.[102] One rate (8.75%) would apply to the accumulated foreign income held in the form of cash or cash equivalents by the CFC and a lower rate (3.5%) would apply to the accumulated foreign income held as non-cash, such as plant and equipment.[103] President Barack Obama had proposed a single 14% rate on

93. SFC 2014 REPORT, *supra* note 15, at 254.

94. Kyle Pomerleau & Andrew Lundeen, *The Basics of Chairman Camp's Tax Reform Plan*, TAX FOUND. (Feb. 26, 2014), https://taxfoundation.org/blog/basics-chairman-camp-s-tax-reform-plan/ [https://perma.cc/RW72-QFLE].

95. I.R.C. § 965(b)(2)(A).

96. *Id.*

97. I.R.C. § 965(b).

98. *See* U.S. HOUSE COMM. ON WAYS & MEANS, 113TH CONG., TAX REFORM ACT OF 2014 DISCUSSION DRAFT 795 (Comm. Print 2014).

99. I.R.C. § 951A(c).

100. Kevin Drawbaugh & Patrick Temple-West, *Tax Cuts, Corporate Breaks Urged by Top Republican*, REUTERS (Oct. 26, 2011), https://www.reuters.com/article/us-usa-tax-camp-proposals/tax-cuts-corporate-breaks-urged-by-top-republican-idUSTRE79P7WM20111027 [https://perma.cc/XQD6-87M8].

101. United States Job Creation and International Tax Reform Act of 2012, S. 2091, 112th Cong. § 104 (2012).

102. *See* U.S. HOUSE COMM. ON WAYS & MEANS, 113TH CONG., TAX REFORM ACT OF 2014 DISCUSSION DRAFT SECTION-BY-SECTION SUMMARY 143 (Comm. Print 2014).

103. *Id.*

the accumulated foreign income,[104] and President Donald Trump, as a candidate in 2016, had proposed a single 10% rate on such income.[105]

In determining the rate or rates, Congress adopted two principles: (1) no windfall to U.S. multinationals, and (2) no windfall to the U.S. government.[106]

> If all earnings are deemed repatriated immediately and taxed at the full U.S. tax rate, then this would be a windfall to the U.S. government. It would be far worse than the expectations of U.S. multinational corporations. These companies have come to expect and rely on indefinite deferral and have done so reasonably. But mandatory deemed repatriation is necessary to be done with the lock-out effect [and avoid a windfall to U.S. multinationals, especially in comparison to corporations that had repatriated earnings in the years before the passage of the TCJA]. Thus, the deemed repatriation could be spread out over many years (to more closely resemble the pre-enactment experience of repatriation of dividends) and/or the U.S. multinational corporations could be subjected to a lower U.S. corporate tax rate on the repatriated earnings.[107]

Initially, some argued that a single rate should apply to the accumulated foreign earnings. Such a single rate would eliminate tax planning and possible abuse that would occur with two rates, with U.S. multinationals attempting to secure the lower rate for all of their accumulated foreign earnings. But Corporate America pushed back on a single rate stating that Camp had opened the door to two rates and that if a single rate were to be utilized, it should be along the lines of Camp's lower rate of 3.5%. The result was that Congress enacted the two-rate structure: a 15.5% rate on the portion of accumulated post-1986 deferred foreign income held as the aggregate foreign cash position and an 8% rate for the remainder.[108]

Another issue was how to structure the tax on deemed repatriated earnings in order to maximize efficiency. Generally, the term "efficiency," when describing a tax provision, means that a tax should interfere as little as possible with a taxpayer's economic behavior.[109] A tax provision is efficient if it does not interfere or distort a taxpayer's investment or business decisions. On Capitol Hill, however, many times the term "efficiency" is used interchangeably with "economic growth." So, to many members of Congress and the Trump Administration, a tax provision was efficient if it enhanced economic growth. A

104. *See* U.S. DEP'T OF TREASURY, GENERAL EXPLANATIONS OF THE ADMINISTRATION'S FISCAL YEAR 2016 REVENUE PROPOSALS 23 (Feb. 2015).

105. *See* ALAN COLE, TAX FOUND., DETAILS AND ANALYSIS OF THE DONALD TRUMP TAX REFORM PLAN, SEPTEMBER 2016, at 4 (Rachel Shuster ed., Sept. 2016).

106. *See* SFC 2014 Report, *supra* note 15, at 253.

107. *Id.* at 254. *See also* Susan C. Morse, *A Corporate Offshore Profits Transition Tax,* 91 N.C. L. REV. 549, 552, 604 (2013) (". . . the transition tax should seek to match taxpayer expectations"; "With respect to the appropriate tax rate, efficiency concerns support a transition tax that matches taxpayer expectations. A transition tax that is less burdensome than taxpayers expect would cause a windfall.").

108. I.R.C. § 965(c).

109. *See* MICHAEL J. GRAETZ & DEBORAH H. SCHENK, FEDERAL INCOME TAXATION: PRINCIPLES AND POLICIES 28 (7th ed., 2013).

driving force behind the tax reform in 2017 was the need for efficiency, or more specifically, a tax plan that would increase economic growth.[110]

At one point, early in the tax reform process, the thinking was that tax reform would be revenue neutral over the budget period, similar to the Tax Reform Act of 1986.[111] However, the idea of revenue-neutral tax reform changed to a tax cut type of tax reform. In late 2017, the House of Representatives and the Senate passed the concurrent budget resolution for fiscal year 2018, which provided that the House Ways and Means Committee and the Senate Finance Committee "shall report changes in laws within its jurisdiction that increase the deficit by not more than $1,500,000,000,000 for the period of fiscal years 2018 through 2027."[112] The result was that tax reform would be a tax cut or increased deficit of up to $1.5 trillion over the ten-year budget period.

Under the JCT macroeconomic models, generally, lowering the cost of capital will generate increased economic growth while increasing the cost of capital will decrease economic growth.[113] Provisions in the tax laws that increase a

110. *See, e.g.*, Martin Crutsinger, *Mnuchin Says Goal is to Pass Tax Reform by August*, GREENFIELD RECORDER (Feb. 23, 2017, 10:40:35 PM), https://www.recorder.com/Mnuchin-says-goal-is-to-pass-tax-reform-by-August-8292990 [https://perma.cc/Q7YP-FAHE] ("Treasury Secretary Steven Mnuchin said Thursday the administration is committed to getting major tax reform legislation through Congress by August. He predicted that President Donald Trump's economic proposals will be able to boost growth significantly to annual rates above 3 percent. Mnuchin said that tax reform is the administration's top economic priority and the goal is to have a measure approved by the time Congress takes its August recess."); Jim Puzzanghera, *Mnuchin Says Trump Tax Overhaul Could Happen by August*, L.A. TIMES (Feb. 23, 2017, 12:10 PM), https://www.latimes.com/business/la-fi-tax-reform-mnuchin-20170223-story.html [https://perma.cc/E2AH-ULEY] ("But Mnuchin's first goal is to push for a tax overhaul, which he said is key to boosting economic growth to 3% annually or higher, from the lackluster 2% level in recent years. 'Our economic agenda, the No. 1 issue is growth, and the first most important thing that will impact growth is a tax plan,' Mnuchin said in an interview with CNBC."); Gillian B. White, *Steven Mnuchin Thinks Trump Can Fix Taxes*, THE ATLANTIC (Apr. 26, 2017), https://www.theatlantic.com/business/archive/2017/04/mnuchin-trump-taxes/524406/ [https://perma.cc/59XG-8TRP] ("When asked about this lack of offsets, Mnuchin insisted that the [tax] plan would be paid for, at least in part, by the additional economic growth unleashed by Trump's economic policies and slashed taxes—growth that Mnuchin and Trump's advisors say will be around 3 percent."); Press Release, U.S. Dep't of the Treasury, Statement by Secretary Mnuchin on President Trump's Tax Reform Speech (Aug. 30, 2017), https://home.treasury.gov/news/press-release/sm0150 [https://perma.cc/6YFW-37P2] ("At the Treasury Department, we are committed to continuing to advance the President's vision on tax reform while working with Congress to pass a plan that will lead to economic growth and job creation to benefit all Americans.").

111. For example, Camp's Tax Reform Act of 2014 was revenue neutral (actually, a $3.0 billion slight increase in revenue over the period 2014–2023). *See* STAFF OF THE JOINT COMM. ON TAX'N, TECHNICAL EXPLANATION, ESTIMATED REVENUE EFFECTS, DISTRIBUTIONAL ANALYSIS, AND MACROECONOMIC ANALYSIS OF THE TAX REFORM ACT OF 2014, A DISCUSSION DRAFT OF THE CHAIRMAN OF THE HOUSE COMMITTEE ON WAYS AND MEANS TO REFORM THE INTERNAL REVENUE CODE, JCS-1-14 654 (Sept. 2014).

112. H.R. Con. Res. 71, 115th Cong. § 2001 (2017) (establishing the congressional budget for the United States Government for fiscal year 2018 and setting forth the appropriate budgetary levels for fiscal years 2019 through 2027).

113. *See* STAFF OF THE JOINT COMM. ON TAX'N, OVERVIEW OF JOINT COMMITTEE MACROECONOMIC MODELING, JCX-33-18 2 (Apr. 23, 2018) ("The three models that the Joint Committee staff uses are the Joint Committee staff Macroeconomic Equilibrium Growth model (MEG), an Overlapping Generations model (OLG), and the Joint Committee staff Dynamic Stochastic General Equilibrium model (DSGE). All three models start with the standard, neoclassical production framework in which the amount of output is determined by the quantity of

taxpayer's tax liability on an additional (marginal) dollar of investment, such as increasing the corporate tax rate or slowing down cost recovery, will increase the after-tax cost of capital for that taxpayer. Provisions that decrease a taxpayer's tax liability on an additional (marginal) dollar of investment, such as decreasing the corporate tax rate or allow expensing of equipment, will decrease the after-tax cost of capital for the taxpayer. The JCT utilized three macroeconomic simulation models to simulate growth effects of the Tax Cuts and Jobs Act.[114] The JCT estimated that TCJA "would increase the average level of output (as measured by Gross Domestic Product ('GDP')) by about 0.7 percent relative to average level of output in the present law baseline over the 10-year budget window. That increase in output would increase revenues, relative to the conventional estimate of a loss of $1,456 billion over that period, by about $451 billion."[115]

The individual tax reform provisions of the TCJA were estimated by the JCT to cost $1,126.6 billion over the budget period of 2018–2027.[116] The business tax reform provisions had an estimated cost of $653.8 billion over the budget period.[117] And the international tax reform provisions were pretty close to being revenue neutral ($14.4 billion over the budget period).[118] As a result, the total estimated cost of the tax reform provisions of the TCJA was almost $1.8 trillion—$300 billion in excess of the tax cut or increased deficit amount set by the concurrent budget resolution.[119]

A deemed repatriation provision could raise $300 billion-plus over the ten-year budget period depending on the rate or rates.[120] That would bring the total cost of the tax reform legislation below $1.5 trillion in accordance with the

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labor and capital used by firms, and the productivity of those factors of production, and long-run aggregate demand equals aggregate supply at full employment. Both individuals and firms are assumed to make decisions based on observed characteristics of the economy, including wages, prices, interest rates, tax rates, and government spending levels. In particular, the amount of labor available to the economy is affected by individuals' understanding of their after-tax returns to working, which depends on both wage rates and tax rates. Similarly, the amount of capital available to the economy is determined by investors' predictions of after-tax returns to capital, which depend on anticipated gross receipts, costs of factor inputs, and tax rates that affect those factors. The underlying structure of the MEG model relies more on reduced form behavioral response equations, while the OLG and DSGE models incorporate more theoretical microeconomic foundations.") (footnote omitted).

114. *See* STAFF OF THE JOINT COMM. ON TAX'N, MACROECONOMIC ANALYSIS OF THE CONFERENCE AGREEMENT FOR H.R. 1, THE "TAX CUTS AND JOBS ACT," JCX-69-17 3 (Dec. 22, 2017).

115. *Id.* The JCT estimated the net cost of TCJA on a macroeconomic basis of $1.005 trillion or $1.071.4 trillion if interest costs on the debt were included. *Id.* at 7, 9.

116. *See* STAFF OF THE JOINT COMM. ON TAX'N, ESTIMATED BUDGET EFFECTS OF THE CONFERENCE AGREEMENT FOR H.R. 1, THE "TAX CUTS AND JOBS ACT," FISCAL YEARS 2018 – 2027, JCX-67-17 3 (Dec. 18, 2017).

117. *Id.* at 6.

118. The $14.4 billion cost is the international tax provisions not including the deemed repatriation provision. *Id.* at 7–8.

119. *Id.* at 3, 6.

120. As enacted, the JCT estimated that the deemed repatriation provision would raise $338.3 billion over the 10-year budget period. *See* STAFF OF THE JOINT COMM. ON TAX'N, ESTIMATED BUDGET EFFECTS OF THE CONFERENCE AGREEMENT FOR H.R. 1, THE "TAX CUTS AND JOBS ACT," FISCAL YEARS 2018 – 2027, JCX-67-17 6 (Dec. 18, 2017).

instructions of the concurrent budget resolution.[121] And equally as important as the revenue generated by a deemed repatriation provision, it could have little or no negative impact on economic growth under the macroeconomic models. It is a tax on past events and earnings.[122] As a result, it has little impact on future investments and future earnings and does not raise the after-tax cost of capital.[123] It did have a slight impact on future investments as the taxpayer that paid the tax under the deemed repatriation provision (over eight years) had slightly less capital to invest.

In 2017, during the tax reform process, other proposals, similar to the deemed repatriation provision, were also considered—ones that would raise revenue in an equitable and efficient manner.[124] As part of the TCJA, Congress reduced the top corporate tax rate from 35% to a single corporate tax rate of 21%. The reduction in the corporate tax rate provided a significant windfall benefit to many corporations that had utilized accelerated depreciation (or expensing) on its property, plant and equipment.[125] The effect of utilizing accelerated depreciation, when compared to straight-line depreciation, is that taxable income is reduced in the years when accelerated depreciation exceeds straight-line depreciation and is increased in later years when straight-line depreciation exceeds accelerated depreciation.[126] The result is that accelerated depreciation produces a deferral of tax liability relative to the tax liability if straight-line depreciation were utilized.[127]

If tax rates stay constant, then the amount of tax that is deferred as a result of accelerated depreciation exceeding straight-line depreciation will exactly equal the amount of tax that is paid in later years when straight-line depreciation

121. The JCT estimated the total cost of TCJA at $1.456.0 trillion over the 10-year budget period. *Id.* at 8.

122. *See* Stephen E. Shay, et al., *Territoriality in Search of Principles and Revenue: Camp and Enzi*, 141 TAX NOTES 173, 209 (2013) ("Some will claim that taxing old earnings is the most favored way to raise revenue because it will have the least distortive effect on future behavior under a territorial system. The choice to tax those earnings, and preannouncement of the intended policy, will trigger pre- and post-enactment behavioral responses (and likely has already done so). These responses will restrict revenue gains and may adversely affect future tax policy credibility.").

123. *But see, e.g.*, Peter Diamond & Emmanuel Saez, *The Case for a Progressive Tax: From Basic Research to Policy Recommendations*, 25 J. ECON. PERSPECTIVES 165, 179 (2011) (in addressing taxing *existing* wealth rather than *future* capital income, ". . . taxing initial wealth as much as the available tax tools allow (whether as a wealth tax or a capital income tax) strains the relevance of the assumption that the government is committed to a policy that this taxation of wealth will not be repeated. Without a credible commitment (which may not be possible), confiscatory wealth taxation would adversely affect saving behavior and have serious efficiency costs because of concerns that such taxation will return.") (emphasis added).

124. For example, Camp had a proposal as part of his Tax Reform Act of 2014 to repeal the last-in, first-out (LIFO) inventory accounting method. Tax Reform Act of 2014, H.R. 1, 113th Cong. § 3310 (2014). Any increase in income would be taken into account over four taxable years under Section 481 (adjustments required by changes in method of accounting). *Id.* § 3310(d)(1)(C)(i). Other proposals that resulted in an income inclusion under Section 481 had a similar effect of raising revenue without increasing the after-tax cost of capital.

125. *See* CHRISTOPHER H. HANNA ET AL., CORPORATE INCOME TAX ACCOUNTING 45–46 (2022); Christopher H. Hanna, *Corporate Tax Reform: Listening to Corporate America*, 35 J. CORP. L. 283, 309–14 (2009).

126. *See* HANNA ET AL., *supra* note 125, at 187–89.

127. *Id.*

exceeds accelerated depreciation. So, the benefit of accelerated depreciation relative to straight-line depreciation is the interest-free deferral of tax (time value of money).[128] If, however, tax rates decrease for the later years, a taxpayer receives an unexpected windfall benefit by, in essence, taking (accelerated depreciation) deductions at a high rate (35%) but being taxed on increased income (when those deductions reverse) at a low rate (21%).[129] This benefit is in addition to the intended benefit of interest-free deferral of tax (time value of money) as part of accelerated depreciation.

One proposal for an efficient tax would have taxed the windfall benefit of corporations as a result of the significant reduction in the corporate tax rate by looking at a corporation's deferred tax liability as recorded in the financial statements.[130] In many corporations, the deferred tax liability is primarily due to accelerated depreciation and expensing of assets.[131] Prior to TCJA, a corporation recorded a deferred tax liability at a 35% tax rate.[132] After TCJA, the deferred tax liability would be restated at a 21% corporate tax rate.[133] That difference represents the windfall benefit and is generally recorded as income for financial accounting purposes.[134] Taxing that windfall benefit, even at a very low tax rate, would generate a significant amount of revenue.[135] In addition, it would have little or no negative impact on economic growth and would not distort investment or business decisions.[136] In that sense, it was similar to the deemed repatriation provision. For various reasons, however, the proposal was not adopted.[137]

Another proposal that was under consideration during the tax reform process that was similar to the deemed repatriation provision was to tax a domestic corporation on its accumulated earnings and profits.[138] The United States has a classical system of taxing corporate income, meaning the corporate income is

128. *Id.*

129. *Id.*

130. *See* James Poterba et al., *The Significance and Composition of Deferred Tax Assets and Liabilities* 7 (Nat'l Bureau of Econ. Rsch., Working Paper No. 12923, 2007), http://www.nber.org/papers/w12923 [https://perma.cc/BH9Z-NJLB].

131. *Id.* at 10 ("The most important source of deferred tax liabilities was Property, Plant and Equipment (PPE).").

132. *See* HANNA ET AL., *supra* note 125, at 45–46.

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.*

137. While the proposal was being considered, it was discovered that a similar proposal was made during the enactment of the Tax Reform Act of 1986. In The President's Tax Proposals to the Congress for Fairness, Growth, and Simplicity released in May 1985, many times referred to as Treasury II, President Ronald Reagan included a proposal that "in order to prevent taxpayers from obtaining the unexpected windfall benefit . . ., 40 percent of a taxpayer's 'excess depreciation' taken between January 1, 1980, and July 1, 1986, would be included in income over a three-year period." RONALD REAGAN, THE PRESIDENT'S TAX PROPOSALS TO THE CONGRESS FOR FAIRNESS, GROWTH, AND SIMPLICITY 193 (May 1985).

138. This proposal was developed in conjunction with a proposal to transition the individual and corporate taxes into an integrated tax system, with the intention of taxing corporate earnings only once and more closely equalizing the tax treatment of debt and equity.

subject to two levels of tax.[139] Corporate income is taxed once at the corporate level and a second time when distributed to shareholders in the form of a dividend.[140] Domestic corporations had accumulated trillions of dollars of income appearing in the form of accumulated earnings and profits. Those accumulated earnings and profits could be taxed if and when distributed to shareholders in the form of a dividend or indirectly taxed when a shareholder sold stock in the corporation at a gain.[141] The proposal was to lightly tax a corporation on its accumulated earnings and profits and then either provide that dividends paid out of the accumulated earnings and profits would be tax-free to the shareholders or provide the shareholders a credit for the tax paid by the corporation.

Like the deemed repatriation provision, a tax on a corporation's accumulated earnings and profits would raise a significant amount of revenue (at even a very low tax rate) and was highly efficient—minimal distortion to investment or business decisions and little negative impact on economic growth. But the proposal never went past the idea stage.

Simplicity was also an issue in enacting the deemed repatriation provision. One issue that arose was how far back the provision should apply to accumulated deferred foreign income. For example, should it apply to all of a foreign corporation's accumulated deferred foreign income? In his 2011 discussion draft, Camp initially proposed including all accumulated deferred foreign income. In his 2014 tax proposals, however, Camp limited the deemed repatriation provision to post-1986 accumulated deferred foreign income.[142] Limiting the provision to post-1986 accumulated deferred foreign income seemed to make sense from both a simplicity—i.e., record keeping—and materiality standpoint. In fact, in providing feedback on the 2011 discussion draft, taxpayers made the case that because of the foreign tax credit changes made in the Tax Reform Act of 1986, many of them were only required to maintain reliable records that far. As one tax commentator wrote, in his written testimony for a House subcommittee hearing after Camp released his 2011 international tax discussion draft: "Since the Tax Reform Act of 1986, U.S. multinationals have had to keep records of cumulative earnings and profits for most, if not all, CFCs for foreign tax credit calculation purposes. For prior earnings (likely to be relatively small in amount), record keeping can be a real

139. *See* SFC 2014 REPORT, *supra* note 15, at 122; Christopher H. Hanna, *Corporate Tax Integration: Past, Present and Future*, 75 TAX LAW. 307, 312 (2022).

140. SFC 2014 REPORT, *supra* note 15, at 122. A dividend is defined as "any distribution of property made by a corporation to its shareholders— (1) out of its earnings and profits accumulated after February 28, 1913, or (2) out of its earnings and profits of the taxable year (computed as of the close of the taxable year without diminution by reason of any distributions made during the taxable year), without regard to the amount of the earnings and profits at the time the distribution was made." I.R.C. § 316(a).

141. Part of the appreciation in the value of stock may be due to the accumulated earnings of the corporation. *See* SFC 2014 REPORT, *supra* note 15, at 228.

142. TAX REFORM ACT OF 2014 DISCUSSION DRAFT, *supra* note 98, at 794.

issue."[143] As a result, for simplicity and materiality purposes, it seemed to make sense that only post-1986 accumulated deferred foreign income would be subject to the deemed repatriation provision.

V. CONCLUSION

The deemed repatriation provision was viewed as a necessary component of the U.S. international tax regime enacted as part of the TCJA. Transitioning from a worldwide deferral tax system to a territorial type of tax system required addressing the accumulated deferred foreign income of foreign subsidiaries of U.S. shareholders. From both a fairness and simplicity standpoint, the accumulated deferred foreign income should be taxed. Giving taxpayers with deferred foreign income a free pass would have been unfair in that some U.S. multinationals would receive a windfall as a reward for keeping their earnings outside the United States while other U.S. multinationals, prior to TCJA, repatriated their overseas earnings at a 35% corporate tax rate less foreign tax credits. Taxing it on a mandatory basis rather than an elective basis also eliminated the lock-out effect, which would still exist if pre-TCJA deferred foreign income still faced a U.S. residual tax when repatriated voluntarily—an important goal of the new U.S. international tax regime. The rate(s) of tax was also important. Taxing at the full corporate tax rate would have resulted in a windfall to the government because corporations had previously assumed that they could defer repatriation indefinitely. So, some preferential rate(s) that factored in corporations' lower expectations about the burden of their eventual tax liability were appropriate.

The deemed repatriation provision was viewed as an efficient tax proposal. It applied to past events and past earnings. Therefore, while it was estimated to raise a substantial amount of revenue, it would have minimal distortion on investment or business decisions, and it would not raise the after-tax cost of capital on marginal (or additional) investments thereby having minimal negative impact on economic growth.

Limiting the tax to post-1986 accumulated deferred foreign income was viewed as primarily a simplification measure. U.S. multinationals may have had difficulty determining pre-1987 accumulated deferred foreign income, and even if they could make the determination, it would, in almost all cases, be a relatively insignificant amount when compared to (or included in) the estimated $2.5 trillion of accumulated deferred foreign income in 2017.

143. *Ways and Means International Tax Reform Discussion Draft: Testimony Before the Subcomm. on Select Revenue Measures of the H. Comm. on Ways & Means*, 112th Cong. 55 (2011) (statement of Paul W. Oosterhuis, Partner, Skadden, Arps, Slate, Meagher & Flom LLP).