Are We GILTI of High Business Taxes? An Examination of the GILTI Tax

Center Forward Basics

March 2021

Overview

In the 2017 Tax Cuts and Jobs Act (TCJA), Congress included a new minimum tax on United States companies' foreign income known as global intangible low-taxed income (GILTI) and a one-time toll tax on prior earnings was also introduced to transition into the new system. The new tax is often viewed as a global minimum tax and despite what the acronym implies, it subjects U.S. headquartered companies (the tax does not apply to foreign headquartered companies) to at least a 10.5% tax (up to 13.125% depending on local jurisdiction tax rates) on all foreign earnings in the year they are earned, not just earnings from intangibles. It was intended only to tax foreign income subject to tax rates lower than 10.5% and replaced the former "deferral system" where companies waited to bring earnings on-shore to the U.S. because of the high tax rates that would be incurred with repatriation. Congress implemented this tax to help pay for the general corporate tax rate reduction and to provide guardrails for U.S. firms to limit moving their assets and profits to other countries with tax rates lower than the U.S. It's important to note that no other country within the OECD has introduced a similar concept, and proposals to date focus on a 12.5% minimum rate. Also important, after 2025, the tax will increase to 13.125% (up to 16.4% depending on local jurisdiction tax rates). The Biden Administration and members of Congress have expressed interest in both changing the structure of the GILTI tax and increasing the baseline GILTI rate beyond the 2025 measures, to raise incremental revenue.

History of GILTI

Companies headquartered in the United States are taxed in many ways, including in the U.S. on both their U.S. and foreign profits (a so-called worldwide tax regime), as well as, abroad on foreign profits. With the stated intention of reducing incentives for profit-shifting to foreign countries, the 2017 TCJA introduced GILTI as a special tax imposed on foreign income earned by CFCs of U.S. companies. It was also introduced as an offset for reducing the federal corporate tax rate. Coupled with foreign-derived intangible income (FDII) regime, the GILTI regime aimed to encourage businesses to keep highly mobile intangible assets in the U.S. instead of migrating them to foreign jurisdictions. But the GILTI tax has also led to several unintended consequences including subjecting foreign earnings to tax at rates in excess of the 10.5% intended by the GILTI tax due to the application of certain expense allocation provisions within the U.S. foreign tax credit rules.

What does GILTI mean for U.S. companies?

The effective GILTI minimum tax rate is 10.5%, or half of the 21% U.S. corporate tax rate. This GILTI rate ensures that foreign profits are at least subject to some minimum level of taxation. However, the idea is to not provide a rate of tax that disadvantages American companies against their foreign competitors that do not have similar minimum tax regimes. It also serves to reduce the incentive for U.S.

Center Forward Basics

Center Forward brings together members of Congress, not-for profits, academic experts, trade associations, corporations and unions to find common ground. Our mission: to give centrist allies the information they need to craft common sense solutions, and provide those allies the support they need to turn those ideas into results.

In order to meet our challenges we need to put aside the partisan bickering that has gridlocked Washington and come together to find common sense solutions.

For more information, please visit www.center-forward.org

Key Terms

- **Intangible assets:** patents, trademarks, and copyrights.
- **Controlled Foreign Corporation (CFC)**: a corporate entity that is registered and conducts business in a different jurisdiction or country than the residency of the controlling owners. A U.S. corporation that operates overseas with U.S. shareholders who have 50% or value of that corporation.
- **Foreign-Derived Intangible Income (FDII)**: income that comes from exporting products or royalty income tied to intangible assets held in the United States. The TCJA introduced this concept.

based multinational corporations to shift profits out of the U.S. into lower-tax jurisdictions.

The Future of GILTI

Under the TCJA, the rate on GILTI will rise after 2025 to 13.125 (up to 16.4% depending on local jurisdiction tax rates). Additionally, President Biden proposed raising the GILTI rate during the 2020 presidential campaign. Specifically, President Biden proposed increasing the corporate tax rate to 28% and the GILTI rate to 21%. He also introduced the idea of imposing the tax on a country-by-country basis which would prevent taxpayers cross-crediting GILTI tax amounts between high-tax and low-tax countries as the current GILTI rules work on an aggregate basis. American-headquartered companies are against the GILTI tax increase because it already significantly impacts their ability to compete with foreign companies that don't have a minimum tax. Any increase to the GILTI rate would impact the ability for American-headquartered companies to compete with their foreign competitors who are not subject to a similar tax in their home jurisdictions. It would likely have the unintended consequence of reducing employment in the U.S. by returning to the days of corporate inversions. As a result, an increase would harm the ability of American companies to compete and grow even further and could also negatively impact American jobs.

Members of Congress have also indicated support of international tax reform, including GILTI. In February 2020, Senators Ron Wyden and Sherrod Brown released legislation to change some of the Treasury Department's high-tax exception rules.

Additionally, later this year the Organization for Economic Cooperation and Development (OECD) plans to propose their own cross-border global minimum tax in order to eliminate double taxation of cross-border earnings. The proposed 21% GILTI rate is significantly higher than the 12.5% rate on similar earnings proposed by the OECD. There is also no guarantee that countries will adopt such measures. If no other countries choose to change their tax rate, the U.S. will be the only country with a similar worldwide minimum tax system to date.

While GILTI was first introduced to discourage firms from shifting income abroad, in practice it has led many U.S. companies to be subject to a higher overall tax rate when compared to foreign competitors doing identical or similar activities in the same jurisdictions. In the next few years, U.S. lawmakers and OECD aim to examine new standards for corporate and international tax policies.

Links to Other Resources

- JDSUPRA - Elective GILTI Exclusion for High-Taxed GILTI
- The Joint Committee on Taxation - Macroeconomic Analysis Of The Conference Agreement For H.R. 1, The Tax Cuts And Jobs Act
- MNE Tax - Can GILTI and the GloBE be harmonized in a Biden administration?
- SSRN - The Effect of U.S. Tax Reform on Foreign Acquisitions
- The Tax Advisor - GILTI: A new age of global tax planning
- Tax Foundation - Detail and Analysis of President Joe Biden's Tax Plan
- Tax Foundation - U.S. Cross-border Tax Reform and the Cautionary Tale of GILTI
- Tax Policy Center - What is global intangible low-taxed income and how is it taxed under the TCJA?
- U.S. Chamber of Commerce - Preventing Changes to GILTI That Hurt Competitiveness

- U.S. Senate Committee on Finance - Wyden, Brown Introduce Bill to Block Latest Trump Administration Corporate Giveaway