GLOBALIZATION AND INTERNATIONAL TAXATION

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In 1984, Congress created a new tax-preferred corporation called a Foreign Sales Corporation (FSC) to qualify as a FSC a foreign corporation must: *[Section 922 of the Internal Revenue Code.]*

1. be created under the laws of foreign country or U.S. possession other than Puerto Rico,
2. have fewer than 25 shareholders,
3. not issue any preference shares,
4. maintain a permanent establishment in the country or U.S. possession in question and maintain appropriate accounting records in the U.S., and
5. have a non-U.S. resident as a member of the board of directors.

Under the FSC provisions a portion of foreign trade income related to the sale of export property, the lease of property for use outside the U.S. or services relating thereto, is exempt from U.S. taxes. The World Trade Organization (WTO) ruled last summer that these exemptions are considered illegal subsidies.

American multinationals claim that the loss of these exemptions without a suitable replacement could undermine the ability of U.S. exporters to compete in a global trade environment. Credit Suisse First Boston, predicted that the loss of the tax break would chop billions off the market capitalization of key exporters like Boeing, Caterpillar and United Technologies as earnings will decline.

Currently, the European Union threatening to have $4 billion in retaliatory tariffs to force the U.S. to change the tax law.

At the heart of the matter is an effort to keep U.S. corporate tax burdens in line with what foreign-based firms face. In the meantime, the U.S. has to comply with WTO regulations.

The Congress and the administration considering some alternative tax measures to replace the FSC. One proposal was to repeal the FSC with a short transition period, and to include corporate tax forms like an expansion of R&D tax credits, a one-year tax holiday allowing companies to repatriate foreign earnings at a low tax rate. Some estimate the cost to the treasury to be $60 billion over the next 10 years. The administration's interest is to pass a bill to help multinational corporations. They are less concerned with the cost. The Democrats argue that more breaks for companies will deepen the deficit.

REFERENCES

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