

# Estimates of TCJA Repatriation of Foreign Earnings on Investment and GDP

---

By Austin Herrick

An important part of the discussion surrounding the passage of the [Tax Cuts and Jobs Act \(TCJA\)](#) was the accumulation of untaxed profits in U.S. corporations' foreign subsidiaries, which were [estimated to be as high as \\$2.8 trillion](#) in 2017. Before 2018, these earnings were generally not subject to U.S. taxes unless they were paid to the U.S. parent corporation as a dividend ("repatriated"), leading many companies to accumulate profits abroad. The TCJA introduced a deemed repatriation provision, which provides a tax "holiday" for foreign earnings by taxing them at a reduced rate of 15.5 percent on cash and eight percent on other assets. Speaker Paul Ryan argued that the TCJA's tax holiday for foreign dividend payments directly affects the economy because, "[money will come back and that will help economic growth.](#)" Indeed, [many companies](#) have already committed to significant repatriation amounts, with Apple notably pledging to pay [\\$38 billion](#) in tax on repatriated income.

At the same time, past experience can help inform the likely impact of the TCJA's tax holiday on investment and GDP. In 2004, Congress enacted a tax repatriation holiday as part of the American Job Creation Act (AJCA). Since the qualifications for AJCA holiday were stricter than those for the TCJA, the experience from the AJCA can help paint an upper bound on the likely impact of the TCJA's tax holiday on investment. Of the trillions of dollars accumulated abroad, we estimate that the TCJA's tax holiday will produce a modest \$28 billion in investment that otherwise would have not been made. Indeed, the biggest impact on GDP (equal to less than 0.2% over 10 years) comes more indirectly, from debt reduction stemming from the \$254 billion in additional revenue over the next decade.<sup>1</sup>

## **Past Experience: The American Job Creation Act (AJCA) of 2004**

Prior to the TCJA, the most recent repatriation provision was the [Homeland Investment Act \(HIA\)](#), passed as part of the [American Job Creation Act \(AJCA\)](#) of 2004. The legislation instituted a one-time holiday for earnings returned to a US parent company as a dividend from a foreign subsidiary. The holiday reduced the tax rate faced by multinationals on foreign earnings from 35 to 5.25 percent for one year. Some proponents [suggested](#) that this provision would spur domestic investment, particularly because income repatriated at the discounted rate was required to be used for specific corporate activities such as capital investments.<sup>2</sup> As a result of the AJCA, corporations repatriated approximately \$300 billion in earnings in 2005, compared to an average of \$90 billion in previous and subsequent years.<sup>3</sup>

Despite its strict requirements on uses of repatriated funds, many studies found that income repatriated through the AJCA was largely not used for domestic investment. Clausing (2005)<sup>4</sup> notes that firms were able to satisfy the investment requirements of the provision by using the repatriated income to fund domestic investment they already intended to pursue. Firms then shifted income that otherwise would have been spent on those investments to shareholders by paying larger dividends. Clemons (2013),<sup>5</sup> Dharmapala et al (2011),<sup>6</sup> and Baghai (2012)<sup>7</sup> each argue that firms would only invest repatriated profits if they were cash-constrained or if they were poorly governed by executives looking for excuses to spend the new cash. Dharmapala et al (2011) conclude that the overwhelming majority of repatriated funds were returned via share repurchases or dividends, with less than one cent of each dollar used for new investment in the U.S.

The AJCA also changed how firms managed their foreign earnings. Oler et al (2007)<sup>8</sup> found that investors capitalized potential reduced repatriation tax into stock prices prior to the AJCA, increasing stock prices of firms with foreign asset holdings. The paper also finds that after the holiday, stock prices for these firms implied that investors believed future repatriation holidays were likely. Brennan (2010)<sup>9</sup> supports these results, finding that multinational corporations increased the share of foreign earnings reinvested abroad following the AJCA in order to take advantage of future tax holidays.

### Application to the TCJA (2017)

Under the TCJA, controlled foreign corporations' (CFCs) and other foreign corporations' accumulated earnings are deemed repatriated with a 15.5 percent tax levied on cash and cash-equivalents, and an eight percent tax levied on other earnings, over an eight year period.<sup>10</sup> Under the new law, all assets eligible for repatriation must be reported in the next year and taxed over the next eight years while future earnings will be taxed under the new system of international taxation established as part of the TCJA.

Experience from the AJCA, however, indicates that *direct* economic effects from repatriated income are likely to be very small. In fact, there are two reasons why the TCJA's holiday is likely to have a smaller effect on domestic investment than the AJCA's holiday. First, many firms were [already able to invest](#) foreign earnings prior to repatriation. Second, the TCJA's shift toward territorial corporate income taxation creates new incentives for companies to invest abroad that did not exist during the previous holiday. Considering findings from the AJCA,<sup>11</sup> these differences from the previous holiday imply that at most one percent (\$28 billion) of earnings repatriated under the TCJA will be used for new investment in the United States.

Rather, the biggest effect of TCJA repatriation is more *indirect*. In [our previous estimate](#) of the effects of the TCJA, PWBM estimated that TCJA-related repatriation will raise \$254 billion in revenue over the next ten years, thereby reducing debt and positively contributing to private capital formation and GDP. Based on our analysis of similar changes to revenue, we expect that the indirect effect will be to increase GDP by less than 0.2 percent after 10 years.

- 
1. This estimate is an upper bound as it assumes that the money would have otherwise not been repatriated indefinitely. [↔](#)
  2. Stipulated activities included employment, capital investments, and R&D (corporations were also limited to a \$500 million cap on repatriation during the holiday). [↔](#)
  3. Data taken from BEA International Transactions Accounts, Table 4.1, Line three. See JCT "Estimated Budget Effects of the Conference Agreement for H.R. 4520, The "American Jobs Creation Act Of 2004" for revenue estimate. [↔](#)
  4. Clausing, K. (2005). Tax Holidays (and Other Escapes) in the American Jobs Creation Act. *National Tax Journal*, 58(3), 331-346. Retrieved from <http://www.jstor.org/stable/41790272>. [↔](#)
  5. Clemons, Roy and Kinney, Michael, An Analysis of the Tax Holiday for Repatriation Under the Jobs Act (August 25, 2008). *Tax Notes*, Vol. 120, No. 8, 2008. Available at SSRN: <https://ssrn.com/abstract=2339752>. [↔](#)
  6. Dharmapala, Dhammika & C. Fritz Foley & Kristin J. Forbes, 2011. Watch What I Do, Not What I Say: The Unintended Consequences of the Homeland Investment Act. *Journal of Finance*, American Finance Association, vol. 66(3), pages 753-787, June. [↔](#)

7. Baghai, Ramin, Corporate Governance and Extraordinary Earnings Repatriations: Evidence from the American Jobs Creation Act (April 3, 2012). AFA 2010 Atlanta Meetings Paper. Available at SSRN: <https://ssrn.com/abstract=1311429> or <http://dx.doi.org/10.2139/ssrn.1311429>. ↵
8. Oler, M., Shevlin, T., & Wilson, R. (2007). Examining Investor Expectations Concerning Tax Savings on the Repatriations of Foreign Earnings under the American Jobs Creation Act of 2004. ↵
9. Brennan, T. J. (2010). What happens after holiday: Long-term effects of the repatriation provision of the ajca. *Northwestern Journal of Law and Social Policy* 5(1), 1-18. ↵
10. As under the previous system, foreign tax credits can reduce the amount owed toward these 15.5 percent and eight percent rates, although the exact mechanics of reducing tax burden have changed. Furthermore, in addition to a lower rate, repatriating firms also do not need to pay their entire tax burden in a single year, and can instead pay via a schedule – with eight percent of taxes owed due in each of the first five years, followed by 15 percent, 20 percent, 25 percent of tax due in the each of the last three years respectively. For more details on specific rules, see this [Tax Policy Center report](#). ↵
11. Dharmapala, Dhammika & C. Fritz Foley & Kristin J. Forbes, 2011. Watch What I Do, Not What I Say: The Unintended Consequences of the Homeland Investment Act. *Journal of Finance*, American Finance Association, vol. 66(3), pages 753-787, June. ↵