The Daily Dish

Finishing the TCJA

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Eakinomics: Finishing the TCJA

There is a now a mini-industry of columns and blog posts claiming the Tax Cuts and Jobs Act (TCJA) "failed." I find this amusing because, as just reported by *The Wall Street Journal* (WSJ), "the Treasury Department issued new rules implementing two major pieces of the 2017 tax law." That's right, the TCJA is still being implemented, particularly with respect to important international tax provisions that are intended to transform the United States to be a tax-competitive location for global investment.

Among the most important of the final regulations are those implementing the minimum tax on Global Intangible Low-Taxed Income (GILTI). As part of modernizing the tax code, TCJA explicitly considered the role of investment in intellectual property (IP). It taxes intangible income derived from serving foreign markets through U.S.-based operations (called Foreign-Derived Intangible Income, or FDII) at a 13.125 percent rate. And in order to ensure the new territorial approach does not cause companies to move valuable IP abroad to tax havens, the TCJA added the GILTI provision that is intended to apply a minimum tax when a company's aggregate foreign tax rate on its intangible income is below the 13.125-percent FDII rate.

The tax on GILTI was intended to be fully offset by foreign tax credits when a company's aggregate foreign tax rate was 13.125 percent or higher. As stated in the conference report to the bill as voted on by members of Congress, "At foreign tax rates greater than or equal to 13.125%, there is no residual U.S. tax owed on GILTI, so that the combined foreign and U.S. tax rate on GILTI equals the foreign tax rate."

Unfortunately, because of the interaction between legacy "expense allocation" rules, which limit the foreign tax credits that companies can claim, and the GILTI regime, the intent of Congress was being thwarted. Looking forward, Congress's key intent is that incentives point to the United States for IP-based activities. It matters much less what happens to the actual tax liabilities of existing firms for existing activities.

While it is commonplace to demean the efforts of "government bureaucrats" and lambast DC-based "swamp dwellers," the reality is that the Treasury did yeoman's work with the TCJA. When the world's largest economy changes for the first (and last) time from a worldwide system to a more territorial system of income taxation, there are bound to be glitches in the statute, and these have been minimized to the extent possible.