The Daily Dish

Tax Reform Marches On — the GILTI Rule

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Eakinomics: Tax Reform Marches On — the GILTI Rule

Tax reform is not really a single bill. Usually there is "technical corrections" legislation that fixes drafting errors, but the partisanship on Capitol Hill has taken that off the table for the Tax Cuts and Jobs Act (TCJA). Also, there are always rules that must be written to implement legislation; for the TCJA that process continues. In particular, late last week the Treasury issued its rule implementing the provision known as GILTI — a minimum tax on Global Intangible Lightly Taxed Income.

Recall that GILTI is defined as income in excess of a return of 10 percent — the rate policymakers deemed to be the norm for tangible assets. Taxpayers reporting GILTI were supposed to face effective tax rates of at least 10.5 percent through 2025 and 13.125 percent thereafter on GILTI income. The logic of the GILTI tax was impeccable: In those circumstances where the level of reported income was inordinately high compared to the depreciable assets that would generate income, presume this income stems from geographically mobile intellectual property (IP) and levy a tax on income in excess of a normal rate of return.

The problem was that there was no real attempt to identify income from intellectual property or other intangibles. Instead, as written the law started to generate strange results. For example, Tupperware filed a 10-Q that reported its effective tax rate rose from 26.2 percent in the first quarter of 2017 to 38.8 percent in the first quarter of 2018, saying, "The change in the rate was primarily due to the estimated impact of Global Intangible Low-taxed Income under the newly enacted Tax Cuts and Jobs Act." This outcome was hardly the plan.

The Treasury rule goes part of the way — but only part — to making the implementation match the intent of the TCJA. In particular, when computing the GILTI levy, companies can choose whether to exclude foreign income that was taxed at a rate greater than 18.9 percent (rather than the originally conceived 13.125 percent). Obviously, there's still a gap between legislative intent (a true minimum tax) and reality (GILTI). But on the whole this shift represents an important improvement by the Treasury.

Ultimately, however, it will be necessary to pass legislation to fix the international tax provisions of the TCJA. This is hardly surprising, as international competition had never before forced the United States to go from taxing worldwide income to focusing on a more territorial income base. There were bound to be mistakes, but to truly enhance the competitiveness of U.S. workers and firms, Congress should get to work fixing the law.