Effective Tax Rates for the 10 Largest Pharma MNEs And Their Implications for U.S. International Tax Reform

by Thomas Horst

Thomas Horst

Thomas Horst is a managing director of Horst Frisch Inc. in Washington. He thanks Kimberly Clausing, Alex Curatolo, Bill Morgan, Barbara Rollinson, and H. David Rosenbloom for their constructive comments on earlier drafts, and Elizabeth Browne and Sophia Dillon Davidson for their help in tabulating financial statement data.

In this article, the author analyzes financial data and effective tax rates for the largest U.S. and international multinational pharmaceutical corporations and considers the implications of those statistical results for U.S. tax reform.

The 2020 election campaign highlighted concerns about offshoring U.S. jobs. Proposed U.S. tax reform has focused on revising the global intangible low-taxed income regime enacted in 2017 or amending subpart F to include a controlled foreign corporation's income from exports to the United States.[1] A common feature of the GILTI and subpart F rules is their application to income derived by CFCs of U.S. multinational enterprises but not to comparable income derived by foreign affiliates of U.S. branches and subsidiaries of non-U.S. MNEs.

In opposing those tax reform proposals, U.S. MNEs argue that the additional U.S. taxes will put them at a competitive disadvantage vis-à-vis foreign MNEs that are not subject to home-country tax on comparable income. The evidence cited to support claims of a competitive disadvantage is typically based on descriptions of other countries' international tax systems, rather than quantitative analyses of the effective tax rates (ETRs) for non-U.S. MNEs.

A recent survey for the world's 10 largest pharmaceutical companies in terms of revenue included five U.S. MNEs (Pfizer Inc., Merck & Co. Inc., Johnson & Johnson, AbbVie Inc., and Bristol-Myers Squibb) and five foreign MNEs (Roche Group, Novartis International AG, GlaxoSmithKline PLC, Sanofi SA, and AstraZeneca PLC).[2] Given the debate over the appropriate tax treatment of U.S. MNEs, I thought it would be useful to investigate what information about 2019 ETRs and related financial data were available in the annual financial statements for the five largest non-U.S. MNEs and how their results compared with similar results for the five largest U.S. MNEs.

My principal findings are that: (1) U.S. sales account for 40 percent of global U.S. sales for non-U.S. pharmaceutical MNEs versus 52 percent for U.S. MNEs; and (2) all MNEs, whether based in the United States or other countries, have shifted pretax profits from the United States and foreign countries with similar tax rates to low-tax jurisdictions. Based on those findings, I conclude that proposed reforms to tax profits derived by foreign affiliates from their export of goods and services to their U.S. affiliates should apply to all MNEs with substantial U.S. sales, including those with foreign parents.

[1] *See, e.g.*, Mindy Herzfeld, "Biden's Onshoring Incentives in a 'World Without Work,'" *Tax Notes Int'l*, Sept. 21, 2020, p. 1547; and Reuven S. Avi-Yonah and Gianluca Mazzoni, "Biden's International Tax Plan," *Tax Notes Int'l*, Oct. 26, 2020, p. 525.

[2] Cheryl Barton, "Annual Revenue of Top 10 Big Pharma Companies," The Pharmaletter, Mar. 3, 2020.

Table 1. Financial Statement Data for 10 Largest Pharmaceutical MNEs, 2019

	<A>	<B>	<C>	<D>	<E>	<F>	<G>
	Multinational Enterprise	Total Revenue ($ millions)	R&D/Total Revenue	U.S. Revenue/ Total Revenue	Pretax Profit/Total Revenue	U.S. Pretax Profit/Total Pretax Profit	GAAP Tax Exp./Pretax Profit
1	Johnson & Johnson	$82,059	14%	51%	21%	20%	13%
2	Pfizer Inc.	$51,750	17%	46%	34%	45%	8%
3	Merck & Co. Inc.	$46,840	21%	43%	24%	4%	15%
4	AbbVie Inc.	$33,266	19%	72%	25%	-33%	7%
5	Bristol-Myers Squibb Company	$26,145	24%	59%	19%	11%	31%
6	Roche Group[a]	$63,349	20%	49%	26%	N/A	15%
7	Novartis Group	$47,498	20%	34%	19%	9%[d]	20%
8	GlaxoSmithKline[b]	$43,097	14%	41%	18%	N/A	15%
9	Sanofi S.A.[c]	$40,439	17%	35%	7%	N/A	5%
10	AstraZeneca	$24,384	25%	33%	6%	-31%[e]	21%
11	Average — 5 largest U.S. MNEs	$48,012	19%	52%	25%	9%	14%
12	Average — 5 largest non-U.S. MNEs	$43,754	19%	40%	15%	N/A	15%

Source: Annual financial statements filed with companies' SEC forms 10-K or 20-F.

[a]Reported amounts stated in Swiss francs were converted into U.S. dollars at annual exchange rate calculated by U.S. Federal Reserve Bank.

[b]Reported amounts stated in U.K. pounds were converted into U.S. dollars at annual exchange rate calculated by U.S. Federal Reserve Bank.

[c]Reported amounts stated in euros were converted into U.S. dollars at annual exchange rate calculated by U.S. Federal Reserve Bank.

[d]Pretax profit outside Switzerland as percent of total pretax profit.

[e]Pretax profit in the Americas as percent of total pretax profit.

I. Results for 10 Largest Pharma MNEs

A. 2019 Results

Financial and ETR data for U.S. MNEs are included in the annual financial statements and notes those companies must file with their SEC Forms 10-K. The stock of large non-U.S. MNEs are typically traded on the New York Stock Exchange or other U.S. stock markets, and the SEC requires those companies to file annual financial statements with their SEC Forms 20-F and provide those statements to their shareholders. Although the information requirements for SEC Forms 20-F are not as strict as those for SEC Form 10-K, Form 20-F helps standardize the reporting requirements of foreign companies and allows more accurate comparisons of foreign MNE financial results with U.S. MNE results.[3]

[3]Will Kenton, "SEC Form 20-F," Investopedia, Apr. 20, 2020.

Table 1 includes the 2019 financial results for the 10 largest pharmaceutical MNEs.[4] In summary:

- Research and development expenditures as a percentage of total revenue for the five largest non-U.S. pharmaceutical companies averaged 19 percent, the same as the comparable percentage for the five largest U.S. pharmaceutical companies.
- Revenue from sales to U.S. customers averaged 40 percent of global sales for the five largest non-U.S. pharmaceutical companies, which is large but less than the 52 percent average share of U.S. revenues for the five largest U.S. pharmaceutical companies.
- Global pretax profit averaged 15 percent of global sales for the five largest non-U.S. pharmaceutical companies, less than the comparable 25 percent average pretax profit margin for the five largest U.S. companies. That differential may result from the combination of higher than average gross profit margins on U.S. pharmaceutical sales by all companies, together with the higher share of U.S. sales in global sales for the five largest U.S. MNEs noted above.
- For the five largest U.S. MNEs, pretax profits reported by U.S. operations averaged 9 percent of their global pretax profits, which is well below the 52 percent average share of U.S. revenues noted above.
- As explained below, only two of the five largest non-U.S. MNEs disclosed any allocation of global pretax profit to geographic areas, and their disclosures did not report pretax profits or losses for their U.S. operations.
- Finally, the generally accepted accounting principles ETR[5] for the five largest non-U.S. pharmaceutical MNEs averaged 15 percent, which closely approximates the 14 percent average GAAP ETR for U.S. MNEs. Both are lower than the home-country statutory rates for corporations reported by MNEs based in the United States (21 percent), the United Kingdom (19 percent), and France (34.4 percent).[6]

B. Pretax Profits vs. Revenues, 2015-2019

The share of pretax profits from U.S. operations shown in Column <F> of Table 1 fluctuates widely from year to year and company to company. Table 2 shows the fluctuating U.S. shares of pretax profit for each of the five years from 2015 to 2019. The weighted average share for all five years shown in Column <F> provides a more reliable basis for evaluating the extent of profit shifting than does the value for any one year, including the value for 2019 shown in Table 1.

For comparison with Table 2, Table 3 shows the share of U.S. sales in global sales for each of the same five years and the weighted average value for those five years taken together. The key conclusion to be drawn from tables 2 and 3 is that the weighted average U.S. share of pretax profits for U.S. pharmaceutical MNEs for those five years is 5 percent, whereas the weighted average U.S. share of total sales for those same five years is 51 percent.[7] Evidence like that of profit shifting by U.S. MNEs is providing the impetus for proposals to reform the U.S. international tax system.

Unlike pretax profit allocation data reported by U.S. MNEs on their SEC Forms 10-K, three of the five non-U.S. MNEs (Roche, GlaxoSmithKline, and Sanofi) did not disclose how their total pretax profits were allocated among the countries where they conducted business.

Novartis's disclosure was limited to the allocation of its total pretax profit between Switzerland and all other countries. Those other countries' weighted average share of Novartis's total pretax profits from 2015 to 2019 was 29 percent, so the weighted average share of pretax profits allocated to Switzerland was the remaining 71 percent. Novartis does not disclose its sales in Switzerland; its total European sales

[4]The annual reports for three of the non-U.S. MNEs (Roche, GlaxoSmithKline, and Sanofi) report financial amounts in currencies other than the U.S. dollar. The total revenues for 2019 shown in Column <B> of Table 1 have been converted into U.S. dollars based on the average exchange rate for 2019 published by the U.S. Federal Reserve Bank.

[5]The GAAP ETR for an MNE equals its total provision for income tax (current and deferred) expressed as a percentage of total pretax profit, both of which are reported in its consolidated income statement for 2019.

[6]Unlike the other eight MNEs included in tables 1-3, Roche and Novartis, the two Swiss MNEs, do not report a home-country statutory tax rate in their public financial statements.

[7]*See* tables 2 and 3, Column <F>, Line 11.

Table 2. Pretax Profit From U.S. Operations as Percent of Total Pretax Profit for 10 Largest Pharmaceutical Companies, 2015-2019

		<A>	<B>	<C>	<D>	<E>	<F>	<G>
	Company	2015	2016	2017	2018	2019	Wtd. Avg. 2015-2019	Notes
1	Johnson & Johnson	43%	38%	28%	31%	20%	32%	
2	Pfizer Inc.	-76%	-102%	-56%	-37%	45%	-32%	
3	Merck & Co. Inc.	42%	11%	53%	43%	4%	28%	
4	AbbVie Inc.	-16%	-21%	-35%	-82%	-33%	-35%	
5	Bristol-Myers Squibb Company	-64%	52%	44%	39%	11%	29%	
6	Roche Group							
7	Novartis Group	29%	60%	41%	16%	9%	29%	Pretax profit outside Switzerland as percent of total pretax profit
8	GlaxoSmithKline							
9	Sanofi S.A.							
10	AstraZeneca	27%	26%	37%	-59%	-31%	7%	Pretax profit in the Americas as percent of total pretax profit
11	Five U.S. company average	-14%	-4%	7%	-1%	9%	5%	
12	Five non-U.S. company average	N/A	N/A	N/A	N/A	N/A	N/A	

Source: Annual financial statements filed with companies' SEC forms 10-K or 20-F.

accounted for 38 percent of its global sales. While the available data do not allow exact comparisons, it seems clear that Novartis's 29 percent share of pretax profits allocated to all countries other than Switzerland is a fraction of the share of its global revenues from those other countries.

AstraZeneca's percentages reflect the shares of its total pretax profit accruing to all countries in the Americas. For the five years at issue, the Americas accounted for 7 percent of AstraZeneca's total pretax profits. By contrast, the weighted average share of AstraZeneca's total sales to the Americas was 40 percent.[8] That is, the weighted average share of AstraZeneca's pretax profit for 2015-2019 allocated to the Americas (7 percent) was a fraction of the comparable weighted average share of AstraZeneca's total sales (40 percent).

In summary, for both Novartis and AstraZeneca, the United States is included in a geographic group of countries for which the weighted average share of pretax profits for 2015-2019 is a fraction of that group's weighted average share of total revenues.

II. Implications for U.S. Tax Reform

Given the considerable evidence that U.S. MNEs have avoided U.S. tax by shifting pretax profits to low-tax foreign jurisdictions,[9] several

[8] That share of total revenues was also derived from AstraZeneca's financial statements but is not reported in table 1 or 2.

[9] For two recent articles on profit shifting by U.S. MNEs, see Kimberly A. Clausing, "5 Lessons on Profit Shifting From U.S. Country-by-Country Data," *Tax Notes Int'l*, Nov. 9, 2020, p. 759; and Martin A. Sullivan, "The Effect of the TCJA on Big Tech," *Tax Notes Int'l*, Nov. 2, 2020, p. 605.

Table 3. Revenues From U.S. Sales as Percent of Total Revenues for 10 Largest Pharmaceutical Companies, 2015-2019

		<A>	<B>	<C>	<D>	<E>	<F>
	Company	2015	2016	2017	2018	2019	Wtd. Avg. 2015-2019
1	Johnson & Johnson	47%	53%	52%	51%	51%	51%
2	Pfizer Inc.	44%	50%	50%	47%	46%	47%
3	Merck & Co. Inc.	44%	46%	43%	43%	43%	44%
4	AbbVie Inc.	59%	62%	65%	66%	72%	65%
5	Bristol-Myers Squibb Company	49%	55%	55%	56%	59%	55%
6	Roche Group	44%	44%	45%	47%	49%	46%
7	Novartis Group	37%	35%	33%	33%	34%	34%
8	GlaxoSmithKline	34%	37%	37%	39%	41%	38%
9	Sanofi S.A.	35%	37%	34%	33%	35%	35%
10	AstraZeneca	40%	34%	30%	33%	33%	34%
11	Five U.S. company average	47%	52%	52%	51%	52%	51%
12	Five non-U.S. company average	38%	38%	37%	38%	40%	38%

Source: Annual financial statements filed with companies' SEC forms 10-K or 20-F.

recent proposals for U.S. international tax reform would either tighten the GILTI rules enacted in 2017 or extend subpart F provisions that originated in 1962 and have been amended many times since.[10] A hallmark of both the GILTI and subpart F provisions is their application to U.S., but not foreign, MNEs. Given the evidence in Section I, U.S. concerns about international profit shifting should apply to all MNEs doing business in the United States, not just those with U.S. parent companies.

In 2017 U.S. concerns about international profit shifting by all MNEs, not just those based in the United States, were manifest in the base erosion and antiabuse tax provisions of the Tax Cuts and Jobs Act. Those provisions (IRC section 59A) sought to remedy U.S. tax avoidance by U.S. corporate taxpayers, including U.S. branches and subsidiaries of foreign corporations, that made base erosion payments to their foreign affiliates. Base erosion payments are generally payments to a related foreign party that result in deductions from the U.S. taxpayer's gross income. Because gross income from a trade or business equals net sales less the cost of goods sold, that cost itself is not a deduction from gross income. For that reason, payments made to foreign related parties that are included in the U.S. taxpayer's cost of goods sold are not base erosion payments and thus do not trigger a BEAT liability. Because of that and other exceptions and limitations, the BEAT provisions have had little reported effect on MNEs in manufacturing industries like pharmaceuticals.

The BEAT rules generally deny a deduction for 100 percent of a base erosion payment to a foreign related party. However, those rules make an exception for services that are eligible for the services cost method under section 482. In those cases, an exclusion from base erosion payments is allowed for the foreign affiliate's cost of providing eligible services, but with no markup on the affiliate's costs.[11]

[10] Avi-Yonah and Mazzoni, *supra* note 1.

[11] IRC section 59A(d)(5).

Taking the BEAT services cost method as precedent, I thought it would be useful to describe a tax reform proposal under which the United States would disallow the deduction by a U.S. affiliate for a foreign affiliate's profit markup on the export of goods and services to the U.S. affiliate. A U.S. affiliate would include a U.S. branch or subsidiary of a foreign parent company — that is, my proposal would not differentiate between MNEs with U.S. parents and MNEs with foreign parents.

To explain my proposal, I describe in the appendix a simple numerical example of an MNE in which a U.S. subsidiary sells to third-party U.S. customers a product manufactured by, and purchased from, a foreign affiliate in a low-tax jurisdiction. The parent company, which may be incorporated either in or outside the United States, is a holding company that owns 100 percent of the shares of both its U.S. sales affiliate and its foreign manufacturing affiliate. My example considers three alternative U.S. tax treatments of the foreign affiliate's pretax profit on export sales to its U.S. affiliate.

The first alternative reflects current U.S. tax law, which includes the foreign affiliate's pretax profit as tested income in calculating the GILTI of a U.S., but not a foreign, parent. The ETR of 14.9 percent based on the MNE's consolidated pretax profit is 1.2 percentage points higher when the MNE has a U.S. parent that is subject to GILTI than the comparable rate of 13.7 percent for the MNE with a foreign parent.[12]

The second alternative reflects a reform of the U.S. tax system under which the foreign affiliate's pretax profit from exports to its U.S. sales affiliate would result in subpart F income for the U.S. parent company. Because of the deemed paid foreign tax credit allowed under IRC section 960, the ETR based on the U.S. MNE's consolidated pretax profit would equal the U.S. statutory rate of 21 percent. Because subpart F does not apply to a foreign parent company, the low 13.7 percent ETR for the non-U.S. MNE would be unaffected by a change to subpart F.[13]

Under the third alternative:

- The U.S. MNE would have the same 21 percent ETR based on its consolidated pretax profit as it would under the subpart F tax treatment just described. However, the additional U.S. tax would result from denying a deduction to the U.S. sales affiliate in an amount equal to its foreign affiliate's pretax profit, rather than treating that pretax profit as subpart F income of its U.S. parent.
- Because the same deduction would be disallowed for the U.S. sales subsidiary of a non-U.S. MNE, that MNE would also have a 21 percent ETR on its consolidated income from third-party U.S. sales.[14] That is to say, the U.S. and non-U.S. MNE would pay the same amount of total tax — U.S. and foreign — on their consolidated pretax profit from third-party U.S. sales.
- The additional income of the U.S. sales affiliate resulting from the disallowed deduction would, like subpart F income, be treated as foreign-source income, and a deemed paid FTC would be allowed for income tax paid by the foreign manufacturing affiliate. Consequently, no international double taxation would result from the tax treatment under this alternative.[15]

In summary, my proposal would address profit shifting by U.S. taxpayers purchasing goods and services from foreign affiliates in low-tax countries. It is more attractive from a U.S. international tax policy perspective than the subpart F alternative because it would raise additional U.S. tax revenue and would restore a

[12] Appendix Table A-1, Column <E>, lines 31, 38, and 39.

[13] Appendix Table A-2, Column <E>, lines 20 and 27.

[14] Appendix Table A-3, Column <E>, Line 33.

[15] My disallowed deduction method is inconsistent with nondiscrimination article 24 of the U.S. model, which provides that for determining the taxable profits of an enterprise of a contracting state, interest, royalties, and other disbursements paid by that enterprise to a resident of the other contracting state are deductible "under the same conditions as if they had been paid to a resident of the first-mentioned Contracting State." Overriding that article is necessary to offset the tax advantage that non-U.S. MNEs would otherwise enjoy vis-à-vis U.S. MNEs when supplying goods and services to their U.S. sales affiliates from low-tax offshore entities. While my method would allow the United States to tax a foreign affiliate's markup on products and services sold to its U.S. affiliate, the foreign affiliate's country of residence would retain the primary right to tax that income, and the U.S. deemed paid FTC would avoid international double taxation on that profit.

level playing field not only between U.S. and non-U.S. MNEs, but also between U.S. and foreign production of goods and services sold to U.S. customers by both U.S. and non-U.S. MNEs.

Appendix

This appendix presents a simple numerical example to compare three alternative U.S. tax treatments of income derived by an affiliated foreign corporation from the intercompany export of goods to its U.S. affiliate. The three alternatives are: (1) the current U.S. tax treatment, including the GILTI provisions; (2) treating the income as subpart F income rather than tested income for GILTI; and (3) disallowing the U.S. affiliate's tax deduction for the portion of its intercompany import costs that represents its foreign affiliate's pretax profit. For all three alternatives, I have compared the tax treatment of an MNE group when the parent is incorporated in the United States with that of an MNE group when the parent is incorporated in a foreign country.

Table A-1 presents my calculations based on current U.S. tax law. Column <F> shows how various amounts are calculated, so only key points are explained here:

- For simplicity, the MNE consists of a U.S. subsidiary that sells a finished product to U.S. customers (Column <A>), a foreign sister subsidiary that manufactures the finished product in a foreign country for intercompany export to its U.S. affiliate (Column <B>), and a parent company whose only function is to hold 100 percent of the shares of its two subsidiaries (Column <C>).
- Lines 1-7 summarize my assumptions about revenues, expenses, and profit before tax (from operations).
- Lines 8-31 describe the foreign and U.S. tax consequences under current U.S. tax law for a U.S. MNE. The complex GILTI-related provisions are described in lines 11-29 of Column <C>.
- Lines 32-38 describe the foreign and U.S. tax consequences for a foreign MNE. Those computations are much simpler because a foreign parent is not subject to the GILTI provisions.
- Based on the consolidated company results shown in Column <E>, the overall ETR for the U.S. MNE (14.9 percent, Line 31) is 1.2 percentage points higher than the ETR for the non-U.S. MNE (13.7 percent, Line 38). That differential reflects GILTI's effect on the U.S. MNE, but not the foreign MNE.

Table A-2 presents my calculations assuming that the pretax profit from the foreign subsidiary's intercompany export income is subpart F income, rather than tested income resulting in GILTI:

- Lines 10-20 in Column <C> show the calculations for a U.S. MNE.
- Because subpart F, unlike GILTI, does not provide any exclusion of the return on qualified business asset investment or a section 250 deduction, the ETR for the consolidated income of a U.S. MNE under subpart F treatment would be 21 percent (Line 20 of Column <E>), which is notably higher than the 14.9 percent ETR under current U.S. law (Line 31 of Column <E> of Table A-1).
- Like GILTI, subpart F does not apply to foreign parents. Accordingly, the ETR for an MNE with a foreign parent would be 13.7 percent (Line 38 of Column <E> of Table A-2), the same as the ETR under current U.S. tax law calculated in Table A-1.

Table A-3 presents my calculations assuming the U.S. subsidiary's deduction for its intercompany purchases is reduced to exclude the pretax profit of its foreign affiliate:

- Lines 10-20 in Column <A> show the calculations for a U.S. parent corporation. The consolidated company's ETR of 21 percent (Line 20 of Column <E>) is identical to the comparable consolidated company ETR under the subpart F alternative (Line 20 of Column <E> of Table A-2).
- Lines 21-33 show the tax calculations when the MNE is incorporated in a foreign country, rather than the United States.
- The critical difference between tables A-2 and A-3 is that the foreign MNE is exempt from the subpart F treatment shown in Table A-2, but not from the disallowed deduction treatment shown in Table A-3.
- Consequently, the consolidated company ETR of 21 percent (Line 33 of Column <E> of Table A-3) for a foreign MNE is the same as the comparable ETR for a U.S. MNE.

Table A-1. Current U.S. Tax System (Including GILTI)

		<A>	<B>	<C>	<D>	<E>	<F>
		U.S. Sub	For. Sub	Parent	Elim.	Cons.	Explanation
	Revenues						
1	Third-Party Sales	100	0	0	0	100	Assumed values
2	Intercompany Sales	0	80	0	(80)	0	Assumed values
3	Total Revenues	100	80	0	(80)	100	#1 + #2
	Expenses						
4	Third-Party Costs	10	60	0	0	70	Assumed values
5	Intercompany Costs	80	0	0	(80)	0	Assumed values
6	Total Expenses	90	60	0	(80)	70	#4 + #5
7	**Profit Before Tax**	10	20	0	0	30	#3 - #6
	1. MNE With U.S. Parent						
8	Foreign Income Rate		10%				Assumed tax rate
9	Foreign Income Tax		2			2	#7 x #8
10	U.S. Taxable Income From Operations	10		0			#7
11	Net Tested Income From CFC			18			Col. <B>, #7 - #9
12	QBAI			50			Assumed value
13	Allowed Return on QBAI (%)			10%			Per IRC
14	Allowed Return on QBAI			5			#12 x #13
15	GILTI Income			13			#11 - #14
16	GILTI Income (%)			72.2%			#15 / #11
17	Foreign Subsidiary Income Tax			2			Col. <B>, #9
18	Section 78 Grossup			1.4			#16 x #17
19	GILTI Income + Section 78 Grossup			14.4			#15 + #18
20	Section 250 Deduction (%)			50%			Per IRC section 250
21	Section 250 Deduction			7.2			#19 x #20
22	Taxable Income re GILTI			7.2			#19 - #21
23	U.S. Taxable Income	10		7.2			#10 + #22
24	U.S. Income Tax Rate	21%		21%			Per IRC
25	U.S. Income Tax Before FTC	2.1		1.5			#23 x #24
26	Deemed Paid Credit Available (%)			80%			Per IRC
27	Deemed Paid Credit Available			1.2			#18 x #26

Table A-1. Current U.S. Tax System (Including GILTI) *(Continued)*

		<A>	<B>	<C>	<D>	<E>	<F>
		U.S. Sub	**For. Sub**	**Parent**	**Elim.**	**Cons.**	**Explanation**
28	Foreign Tax Credit			1.2			Min (#25, #27)
29	U.S. Income Tax After FTC	2.1		0.4		2.5	#25 - #28
30	Total Income Tax	2.1	2	0.4		4.5	#9 + #29
31	Effective Tax Rate	21%	10%	N/A		14.9%	#30 / #38
	2. MNE With Foreign Parent						
32	Foreign Income Rate		10%	10%			Assumed tax rate
33	Foreign Income Tax		2	0		2	#7 x #32
34	U.S. Taxable Income	10				10	#7
35	U.S. Income Tax Rate	21%					Assumed tax rate
36	U.S. Income Tax	2.1				2.1	#34 x #35
37	Total Income Tax	2.1	2	0		4.1	#33 + #36
38	Effective Tax Rate	21%	10%	N/A		13.7%	#37 / #7
39	**Effective Tax Rate Differential**	0%	0%	N/A		1.2%	#31 - #38

Table A-2. U.S. Tax System With Subpart F Treatment of Foreign Affiliate Profit From I/C Sales

		<A>	<B>	<C>	<D>	<E>	<F>
		U.S. Sub	For. Sub	Parent	Elim.	Cons.	Explanation
	Revenues						
1	Third-Party Sales	100	0	0	0	100	Assumed values
2	Intercompany Sales	0	80	0	(80)	0	Assumed values
3	Total Revenues	100	80	0	(80)	100	#1 + #2
	Expenses						
4	Third-Party Costs	10	60	0	0	70	Assumed values
5	Intercompany Costs	80	0	0	(80)	0	Assumed values
6	Total Expenses	90	60	0	(80)	70	#4 + #5
7	**Profit Before Tax**	10	20	0	0	30	#3 - #6
	1. MNE With U.S. Parent						
8	Foreign Income Rate		10%				Assumed tax rate
9	Foreign Income Tax		2			2	#7 x #8
10	U.S. Taxable Income From Operations	10		0			#7
11	Subpart F Income			18			Col. <B>, #7 - #9
12	Grossup for Foreign Inc. Tax			2			Col. <B>, #9
13	U.S. Taxable Income	10		20		30	Sum (10: #12)
14	U.S. Income Tax Rate	21%		21%			Assumed tax rate
15	U.S. Income Tax Before Credit	2.1		4.2		6.3	#13 x #14
16	Deemed Paid Foreign Tax			2			#12
17	Foreign Tax Credit			2			Min (#15, #16)
18	U.S. Income Tax After Credit	2.1		2.2			#15 - #17
19	Total Income Tax	2.1	2	2.2		6.3	#9 + #18
20	Effective Tax Rate	21%	10%	N/A		21%	#19 / #27
	2. MNE With Foreign Parent						
21	Foreign Income Rate		10%	10%			Assumed tax rate
22	Foreign Income Tax		2	0		2	#7 x #21
23	U.S. Taxable Income	10				10	#7
24	U.S. Income Tax Rate	21%					Assumed tax rate
25	U.S. Income Tax	2.1				2.1	#23 x #24
26	Total Income Tax	2.1	2	0		4.1	#22 + #25
27	Effective Tax Rate	21%	10%	N/A		13.7%	#26 / #7
28	Effective Tax Rate Differential	0%	0%	N/A		7.3%	#20 - #27

Table A-3. U.S. Tax System With Disallowed Deduction of Foreign Affiliate Profit From I/C Sales

		<A>	<B>	<C>	<D>	<E>	<F>
		U.S. Sub	**For. Sub**	**Parent**	**Elim.**	**Cons.**	**Explanation**
	Revenues						
1	Third-Party Sales	100	0	0	0	100	Assumed values
2	Intercompany Sales	0	80	0	(80)	0	Assumed values
3	Total Revenues	100	80	0	(80)	100	#1 + #2
	Expenses						
4	Third-Party Costs	10	60	0	0	70	Assumed values
5	Intercompany Costs	80	0	0	(80)	0	Assumed values
6	Total Expenses	90	60	0	(80)	70	#4 + #5
7	**Profit Before Tax**	10	20	0	0	30	#3 - #6
	1. MNE With U.S. Parent						
8	Foreign Income Rate		10%				Assumed tax rate
9	Foreign Income Tax		2			2	#7 x #8
10	U.S. Taxable Income From Operations	10		0		10	#7
11	Adjustment for Disallowed After-Tax Profit	18				18	Col. <B>, #7 = #9
12	Adjustment for Tax on Disallowed Profit	2				2	Col. <B>, #9
13	U.S. Taxable Income	30				30	Sum (10: #12)
14	U.S. Income Tax Rate	21%					Assumed tax rate
15	U.S. Income Tax Before Credit	6.3				6.3	#13 x #14
16	Deemed Paid Foreign Tax	2				2	#12
17	Foreign Tax Credit	2				2	Min (#15, #16)
18	U.S. Income Tax After Credit	4.3				4.3	#15 - #17
19	Total Income Tax	4.3	2	0		6.3	#9 + #18
20	Effective Tax Rate	43%	10%	N/A		21%	#19 / #33
	2. MNE With Foreign Parent						
21	Foreign Income Rate		10%	10%			Assumed tax rate
22	Foreign Income Tax		2	0		2	#7 x #21
23	U.S. Taxable Income — Current Law	10		0		10	#7
24	Adjustment for Disallowed After-Tax Profit	18				18	Col. <B>, #7 - #22

Table A-3. U.S. Tax System With Disallowed Deduction of Foreign Affiliate Profit From I/C Sales *(Continued)*

		<A>	<B>	<C>	<D>	<E>	<F>
		U.S. Sub	**For. Sub**	**Parent**	**Elim.**	**Cons.**	**Explanation**
25	Adjustment for Tax on Disallowed Profit	2				2	Col. <B>, #22
26	U.S. Taxable Income	30				30	Sum (23: #25)
27	U.S. Income Tax Rate	21%					Assumed tax rate
28	U.S. Income Tax Before Credit	6.3				6.3	#26 x #27
29	Deemed Paid Foreign Tax	2				2	#25
30	Foreign Tax Credit	2				2	Min (#28, #29)
31	U.S. Income Tax After Credit	4.3				4.3	#28 - #30
32	Total Income Tax	4.3	2	0		6.3	#22 + #25
33	Effective Tax Rate	43%	10%	N/A		21%	#32 / #7
34	**Effective Tax Rate Differential**	0%	0%	N/A		0%	#20 - #33

■