Measuring Rates of Return for Lobbying Expenditures:

An Empirical Analysis Under the American Jobs Creation Act

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Abstract

The lobbying industry has experienced exponential growth within the past decade. The general public, the media, and special interest groups perceive lobbying to be a powerful mechanism affecting public policy. However, academic research finds inconclusive results when quantifying the rate of return on political lobbying expenditures. In this paper we use audited corporate tax disclosures relating to a tax holiday on repatriated earnings created by the American Jobs Creation Act of 2004 to examine the return on lobbying. We find firms lobbying for this provision have a return in excess of $220 for every $1 spent on lobbying, or 22,000%. Repatriating firms are more profitable overall, but surprisingly, profitability is not a predictor of repatriation amount. Rather, industry and firm size are most predictive of repatriation. Cash on hand, a proxy for ability to repatriate, is not associated with the repatriation decision or the repatriation amount. This paper provides compelling evidence that lobbying expenditures have a positive and significant return on investment.

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I. INTRODUCTION

Lobbying is a multi-billion dollar industry with over $5 billion in lobbying activity taking place during the 2003-2004 election cycle alone.[1] The common perception among both the public and lobbyists is that lobbying expenditures provide high returns to contributors.[2] The academic research on lobbying, however, has found inconclusive results.[3]

In an efficient market, the lobbying industry could not survive without providing a perceived value to customers.[4] The conflict between the reality of a thriving, expanding lobbying industry and prior research rests with the inability of academic researchers to estimate the value of lobbying activities. Clearly, valuing non-monetary policies such as improved education arising from the "No Child Left Behind" legislation is difficult. Even for monetary-based policies such as minimum wage legislation, benefits accruing to private entities can only be roughly estimated.

The tax law is, perhaps, the only legislation that can be used to quantify lobbying returns; a comparison of taxpayers' tax liabilities prior to and after a tax law change demonstrates additional tax savings or tax expenditures. However, researchers outside the Internal Revenue Service cannot access this tax liability data because tax returns are confidential[5] and, to date, no corporation publicly discloses tax return information. The dividend repatriation provision of the American Jobs Creation Act of 2004 (AJCA)

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[1] *See* The Center for Public Integrity, available at www.publicintegrity.com.

[2] Jeffery Birnbaum, *Clients' Rewards Keep K Street Lobbyists Thriving,* WASHINGTON POST, Feb. 14, 2006, at A1.

[3] *See* John M. de Figueiredo & Brian S. Silverman, Academic Earmarks and the Returns to Lobbying, NBER Working Paper 9064 (July 2002), *see also* Nixon v. Shrink Missouri Government PAC*,* 528 U.S. 377 (2000) (acknowledging the public perception that money buys legislative influence but stating that no academic consensus of such influence exists).

[4] In fact, the number of registered lobbyists doubled from 2000 to 2005 and the average fee has increased by 100% in some cases. Jeffrey Birnbaum. *The Road to Riches Is Called K Street*, WASHINGTON POST, June 22, 2005, at A1.

[5] IRC § 6103.

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provides a unique opportunity to quantify the returns to lobbying as the tax benefits were limited to a single taxable year and the benefits accruing to each company were publicly disclosed in financial statements.

The AJCA allowed U.S. multinationals a one-time opportunity to bring home foreign earnings and pay taxes on only 15% of this repatriated income.[6] Because the amounts repatriated typically had a material effect on companies' taxes, information about the repatriation is usually disclosed in the financial statements of publicly traded companies.[7] Further, public accounting firms audit financial statements disclosures and attest to their accuracy. Thus, this is the first study to provide actual values of the financial savings arising from tax law changes, and the first to use data that has been audited by independent accounting firms.

Another difficulty researchers encounter when calculating rates of return to lobbying is measuring lobbying expenditures. In this study we overcome this limitation by hand collecting lobbying data from the Senate database on lobbying expenditures,[8] the Federal Election Commission,[9] and from annual reports of all publicly traded firms. Our study identifies 496 firms reporting repatriating under the auspices of the ACJA. Of these, 476 provide information about the amount repatriated, the amount of tax paid because of the repatriation, or the taxes saved by repatriating. Based on these 476 firms' information, we analyze $298 billion of repatriations under the AJCA.[10]

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[6] IRC § 965. More specifically, the legislation permitted corporations a deduction equal to 85% of the cash dividends repatriated. This deduction effectively reduces the tax rate from 35% to a maximum 5.25% on the repatriation amounts.

[7] Generally Accepted Accounting Principles (GAAP) require disclosure of information regarding material transactions or economic events. The SEC requires companies with publicly traded stock or debt to submit their financial statements and provides public access to them.

[8] http://www.senate.gov/pagelayout/legislative/g_three_sections_with_teasers/lobbyingdisc.html.

[9] http://www.fec.gov/.

[10] Repatriating companies that did not report amounts likely repatriated smaller, immaterial amounts that require less disclosure under GAAP. Some companies repatriating immaterial amounts may not have mentioned repatriation at all.

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We identify 93 firms engaged in lobbying for the rate reduction. Combined, they repatriated $208 billion (or 70% of the total). We estimate that the lobbying group spent $282.7 million on lobbying expenditures and received $62.5 billion in tax savings, or a 220:1 return on investment. Using a statistical regression, we estimate that lobbying activity is highly associated with amount repatriated even after controlling for firm industry, size, profitability, liquidity and growth prospects. Surprisingly, this tax provision was so lucrative that several firms borrowed funds to repatriate the cash as earnings.

The paper proceeds as follows: Section II explains the repatriation holiday legislation and provides background information; Section III.A. describes the data collection method, sets out the empirical model, and identifies variables that predict whether a corporation repatriated in response to the legislation; Section III.B. sets out the model calculating returns to lobbying; and Section IV describes the implications of our results. We contribute to the existing literature by providing strong evidence demonstrating that lobbying has a positive return on investment.

II. DIVIDEND REINVESTMENT UNDER THE AJCA OF 2004

A. *Deferral and Lock-Out*

Section 965 made a fundamental, albeit elective and temporary, change to how the U.S. taxes domestic corporations on their overseas earnings. As a general rule, the United States taxes U.S. residents and domestically-chartered corporations on their "worldwide" income, whether derived within the United States or abroad.[11] A domestic corporation with branch operations in another country that are not conducted through a separate subsidiary corporation reports the earnings for U.S. tax purposes when those earnings accrue. If, instead, the domestic corporation conducts operations abroad through

[11] I.R.C. § 61(a) ("gross income means all income from whatever source derived"). Exceptions do exist. *See, e.g.,* I.R.C. § 911 (providing an exclusion from gross income for a limited amount of foreign earned income).

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a foreign subsidiary corporation, the U.S. tax on those earnings is generally deferred until the earnings are remitted to the U.S. parent corporation in the form of dividends.[12] Once reported for U.S. tax purposes, a foreign tax credit available to the domestic parent corporation helps ensure that the corporation's foreign source income is not taxed twice.[13]

A domestic corporation's ability to defer indefinitely U.S. tax on income derived by its foreign subsidiary until such income is repatriated in the form of dividends is a long-standing, but controversial, component of U.S. international tax policy.[14] The deferral privilege has been criticized by some for allowing U.S. corporations with multinational operations to avoid U.S. tax on their foreign source income by retaining the income abroad in low-tax jurisdictions.[15] Other commentators describe the deferral issue slightly differently, viewing the residual U.S. tax imposed on the foreign source earnings, once repatriated, as a barrier to repatriation.[16] Known as the "lock out" effect, the residual tax is said to encourage domestic corporations with foreign subsidiaries to

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[12] *See* Boris I. Bittker & Lawrence Lokken, FUNDAMENTALS OF INTERNATIONAL TAXATION: U.S. TAXATION OF FOREIGN INCOME AND FOREIGN TAXPAYERS ¶ 65.1.4 (2002 ed.). U.S. tax may also apply when the U.S. parent sells the stock of the foreign subsidiary at a gain. *Id.* Limitations on the scope of the deferral benefit exist in the form of several anti-deferral regimes. For example, if the foreign subsidiary derives income from the ownership of passive assets or from sources thought to be easily manipulated by taxpayers, the U.S. taxes the domestic parent corporation on that income on a current basis under the controlled foreign corporation rules in subpart F and the passive foreign investment company rules. I.R.C. §§ 951-864, 1291-1298.

[13] I.R.C. §§ 901, 902, *see also* §§ 960, 1291(g).

[14] Rosanne Altshuler & T. Scott Newlon, *The Effects of U.S. Tax Policy on the Income Repatriation Patters of U.S. Multinational Corporations*, in STUDIES IN INTERNATIONAL TAXATION 91 (Alberto Gioannini ed. 1993); Clifton J. Fleming, Jr. & Robert J. Peroni, *Exploring the Contours of a Proposed U.S. Exemption (Territorial Tax) System*, 41 TAX NOTES INT'L 217 (2006); Clifton J. Fleming, Jr. & Robert J. Peroni, *Eviscerating the U.S. Foreign Tax Credit Limitations and Cutting the Repatriation Tax – What's ETI Repeal Got to Do With It?*, 35 TAX NOTES INT'L 1081, 1099 (2004) [hereinafter "ETI Repeal"]; Michael J. Graetz, *Taxing International Income: Inadequate Principles, Outdated Concepts, and Unsatisfactory Policies*, 54 TAX L. REV. 261 (2001); John P. Steines, *Whether, When, and How to Tax the Profits of Controlled Foreign Corporations*, 26 BROOKLYN J. INT'L L. 1595 (2001).

[15] *See* Robert J. Peroni *et al.*, *Getting Serious About Curtailing Deferral of U.S. Tax on Foreign Source Income*, 52 SMU L. REV. 455 (1999), *see also* Charles I. Kingston, *The Great American Jobs Caper*, 58 TAX L. REV. 327, 373 (2005) (viewing deferral not so much as an impediment to repatriation of foreign earnings but as an impediment to taxing those earnings as they accrue).

[16] See Staff of Joint Comm. on Tax'n, THE U.S. INTERNATIONAL TAX RULES: BACKGROUND AND SELECTED ISSUES RELATING TO THE COMPETITIVENESS OF U.S. BUSINESSES ABROAD (Comm. Print 2003).

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reinvest the subsidiary's earnings abroad rather than repatriate the profits and invest them within the United States.[17]

While the source and extent of the lock-out effect is subject to debate,[18] the Treasury Department and Congress obviously viewed the existing U.S. tax system as creating a disincentive to repatriate offshore earnings.[19] As part of an effort to reduce the perceived lock-out effect, Congress enacted section 965, which granted U.S. corporate shareholders a one-year, 85% deduction for repatriated dividends from controlled foreign corporations.[20] The deduction lowered the effective U.S. corporate tax rate on those profits from 35% to 5.25%.[21]

B. *Purpose and Legislative History*

The dividend deduction in section 965 was initially introduced as a stand-alone bill, the Homeland Investment Act. It eventually found its way into a legislative package known as the American Jobs Creation Act of 2004 (AJCA).[22] The AJCA began as a legislative response to the long-running controversy between the United States and the

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[17] *Id.*

[18] *See* ETI Repeal, at 1096 n.122, *see also* John R. Graham, Michelle Hanlon, & Terry Shevlin, *Barries to Mobility: The Lockout Effect of U.S. Taxation of Worldwide Company Profits*, *available at* http://ssrn.com/abtract = 1316576 (survey data showing that nearly 75% of the funds repatriated under the AJCA came from cash and liquid assets. According to the authors, "The fact that the repatriated funds were already in liquid form, but not repatriated under the tax burden was reduced, is consistent with the lockout effect of U.S. tax policy and an impediment to capital mobility.")

[19] Conf. Rep. No. 108-755 (2004) (hereinafter Conference Report).

[20] I.R.C. § 965(a)(1). A foreign corporation is generally considered a controlled foreign corporation (CFC) if more than 50% of its total voting power or value is owned by U.S. shareholders for an uninterrupted period of 30 days or more during the taxable year. I.R.C. § 957(a).

[21] If a U.S. corporate shareholder were entitled to deduct 85% of dividends that were otherwise taxed at 35%, *see* I.R.C. § 11, the 35% tax on the 15% of the dividends remaining after the deduction equates to a 5.25% tax on the entire amount of the dividend.

[22] Pub. L. No. 108-357, _ Stat. _ (2004). Legislation included as part of the Gulf Opportunity Zone Act of 2005, Pub. L. No. 109-135, Stat. (2005) made several amendments to the original version of the statute enacted in 2004. The AJCA contained other provisions that expand the U.S. parent's ability to defer reporting foreign source income. For example, the AJCA contracted the scope of the anti-deferral provisions under subpart F. *See, e.g.,* I.R.C. § 956(c)(2)(L), 956(c)(2)(M).

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European Union over the U.S.'s tax benefits for exporters.[23] Over the years Congress had enacted a variety of tax incentives to encourage exports by U.S. businesses. One attempt, the Extraterritorial Income Exclusion Act of 2000 (ETI),[24] allowed U.S. corporations a partial income exclusion for export profits, thereby raising the domestic corporation's after-tax return and allowing domestic corporations either to make higher profits or lower the prices of goods sold abroad.[25] As they had with respect to earlier U.S. efforts, representatives from the European Union objected to the ETI provisions and convinced the World Trade Organization in 2001 to declare them to be impermissible export subsidies.[26] The WTO ruling opposing the ETI regime opened the door for the European Union to impose $4 billion in retaliatory tariffs on U.S. imports, which the EU began implementing in March 2004.[27]

With pressure to repeal the ETI, but with continuing concerns about encouraging U.S. exports and job creation within the U.S., Congress cobbled together the AJCA, which the President promptly signed into law. The AJCA did phase-out the then-existing ETI regime,[28] but by the time the legislation hit the President's desk, the AJCA had become a broad-based business tax bill that incorporated a host of corporate tax

[23] *See* David L. Brumbaugh, *The 2004 Corporate Tax and FSC/ETI Bill: The American Jobs Creation Act of 2004*, Congressional Research Service CRS RL32652 (2004) [hereinafter 2004 Corporate Tax]. For an explanation of the history of the dispute, see David L. Brumbaugh, *A History of the Extraterritorial Income (ETI) and Foreign Sales Corporation (FSC) Export Tax Benefit Controversy*, CONGRESSIONAL RESEARCH SERVICE CRS REPORT RL31660 (2004).

[24] Pub. L. No. Stat.

[25] I.R.C. § 114(a), (b) (repealed by AJCA).

[26] *See* Alan S. Lederman & Bobbe Hirsh, *AJCA Replaces Tax Incentives for Exports With a Domestic Production Tax Break and a One-Time DRD*, 102 J. TAX'N 6, 6-8 (2005).

[27] 2004 Corporate Tax, at 2-3.

[28] AJCA § 101(a). The ETI regime was replaced with a deduction for qualified production activities income. I.R.C. § 199. When fully phased-in in 2010, taxpayers will be entitled to deduct up to 9% of the taxpayer's qualified production activities income. I.R.C. § 199(a)(1). If a corporate taxpayer were paying tax at the maximum rate of 35%, I.R.C. § 11, the deduction would be the equivalent to a tax rate reduction to 31.85%. *See generally* Lederman & Hirsh, at 8-15.

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provisions, as well as special interest provisions benefiting Alaskan whaling captains, NASCAR race track owners, and importers of Chinese ceiling fans, among others.[29]

Like most of the provisions in the AJCA, the deduction in section 965 for repatriated dividends was largely unrelated to the ETI controversy. Congress's stated purpose behind section 965 was, instead, to "stimulate the U.S. domestic economy by triggering the repatriation of foreign earnings that otherwise would have remained abroad."[30] The legislative history, however, reveals a somewhat narrower purpose. The original Senate version of the legislation was entitled the Jumpstart Our Business Strength (JOBS) Act.[31] True to both the legislation's original title and the comprehensive title of the enacted legislation (the American Jobs Creation Act), members of Congress viewed the dividend repatriation provision in section 965 primarily as a job growth measure.[32] For example, during debate leading up to the Code

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[29] *See, e.g.,* I.R.C. § 170(n), *see generally* Joint Committee on Taxation, GENERAL EXPLANATION OF TAX LEGISLATION ENACTED IN THE 108TH CONGRESS, JCS-5-05 (May 2005). The impact of the AJCA has been the subject of intense debate. Charles Kingston, a noted practitioner in the international tax area, publicly described the philosophy behind the AJCA as "crap". Lee A. Sheppard, *Hicks Previews Jobs Creation Act Guidance*, 2004 TNT 233-3 (Dec. 3, 2004), *see also* Part III, below.

[30] House Rep. No. 108-548 (2004) (hereinafter the "Conference Report"). The report of the Senate Finance Committee on the companion bill contains similar statements. *See* S. Rep. No. 108-192, at 51 (2003). The Congressional Budget Office (CBO) estimated that the provisions in the AJCA would increase federal revenues by approximately $1.5 billion in 2004 and decrease revenues by approximately $42.2 billion over the periods 2004-2014. Congressional Budget Office, Cost Estimate: H.R. 4520, American Jobs Creation Act of 2004 (June 16, 2004). The CBO estimated that the temporary section 965 deduction, along with several other provisions aimed at domestic business activity, would increase governmental receipts by about $2.7 billion in 2004 and decrease receipts by about $7.2 billion over the period 2004-2014. *Id.* The Joint Committee on Taxation scored the net revenue loss from section 965 at a mere $3.5 to $3.9 billion. *See* Staff of the Joint Committee on Tax'n, Comparison of the Estimated Budget Effects of H.R. 4520, The "American Jobs Creation Act of 2004," as Passed by the House of Representatives, and H.R. 4520, the "Jumpstart Our Business Strength ('JOBS') Act," as Amended by the Senate, at 3 (Comm. Print 2004). *But see* Joel Friedman, *Temporary Tax Provisions in the Corporate Tax Bill Mask Its Long Term Impact on the Deficit*, Center on Budget and Policy Priorities (2004) (estimating that tax breaks in the AJCA could add over $80 billion to the deficit over 10 years).

[31] S. 1637, 108th Cong. Earlier versions of the legislation were contained in bills known as the "Homestead Investment Act" and the "Invest in USA Act". _ Stat. __.

[32] *See, e.g.,* Cong. Rec. S4861 (May 5, 2004) (statement of Sen. Breaux) ("[T]his is a jobs bill. . . . Our legislation, . . . is about responsibility and accountability, about creating jobs in this country, not stock buybacks that enrich a few at the expense of jobs in this country."); S4863 (statement of Sen. Smith) ("If we could create 660,000 jobs on a short-term basis – we hope that money then stays here – then we have done a tremendous thing for the American worker and the American economy . . . .); S4875 (statement of Sen. Graham ("The rationale for [section 965] is that reducing the tax rate will encourage U.S.

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provision's passage, supporters of the measure repeatedly cited a report prepared by the noted economist Allen Sinai.[33] The Sinai report projected that, in response to the deduction, U.S. corporations would repatriate between $265 and $406 billion in offshore earnings, leading to a gain of 660,000 jobs in 2005, the post-enactment year.[34] The 660,000 jobs estimate was considered conservative.[35]

The statutory language of section 965 that Congress eventually enacted and included in the AJCA also reveals an effort aimed at job creation within the U.S. Along with provisions imposing a one-year window for the deduction,[36] an aggregate limit on the amount of the deduction,[37] and anti-abuse restrictions,[38] legislators included qualifications on the U.S. parent corporation's use of the repatriated funds. Most

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multinational companies to expatriate income held offshore in order to make investments in the United States that will create jobs."). *But see* Joann M. Weiner, *Bring Back the Repatriation Tax Holiday*, TAX NOTES 573 (2009) (questioning whether the AJCA was intended to be a jobs creation provision).

[33] Allen Sinai, *Macroeconomic Effects of a Temporary Reduction in the Tax Rate on Repatriation of Foreign Subsidiary Earnings* (Oct. 21, 2003). *See, e.g.,* Cong. Rec. S4863 (statement of Sen. Smith); S4884 (statement of Sen. Ensign); Cong. Rec. S4884 (statement of Sen. Breaux).

[34] Sinai at __.

[35] Id. Cite updated Sinai study.

[36] The provision was temporary and elective. The U.S. corporate shareholder must have made the election either for the shareholder's last taxable year that began before October 22, 2004, or the shareholder's first taxable year that began during the one-year period starting on October 22, 2004. I.R.C. § 965(f). Section 965(f) further required the election to be made on the shareholder's timely-filed return, including extensions, for the election year. The Conference Report also includes the following language: "The conferees emphasize that this is a temporary economic stimulus measure, and that there is no intent to make this measure permanent, or to "extend" or enact it again in the future." Conf. Rep. No. 108-755.

[37] Section 965 limited the amount of dividends otherwise qualifying for the deduction to the greater of $500 million or the amount shown on the applicable financial statements with respect to the U.S. shareholder as "earnings permanently reinvested" outside the United States. I.R.C. § 965(b)(1). The "earnings permanently reinvested" outside the U.S. concept derives from Accounting Principles Board Opinion 23. The opinion excepts U.S. tax liability on undistributed earnings of foreign subsidiaries from the general rule requiring recognition of temporary book-tax differences if that liability meets specified criteria for indefinite deferral. *See* Conference Report, at 67 n. 111. The amount of dividends eligible for the deduction was also limited to repatriations in excess of those during a base period specified in the statute. *See* I.R.C. § 965(b)(2). Dividends had to be extraordinary.

[38] The primary anti-abuse provision is in section 965(b)(3), which reduces the dividend amount otherwise eligible for a deduction by related party indebtedness. The rule is designed to prevent a deduction for any dividend from a CFC financed, directly or indirectly, by a U.S. shareholder. In such cases, there may be no net repatriation of funds. *See* Conf. Rep. 108-755.

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importantly, the deduction applied only if the U.S. corporate shareholder invested the repatriated dividends that generated the deduction within the United States pursuant to a domestic reinvestment plan (DRIP) approved first by the corporation's upper-management – the CEO or comparable official -- then subsequently re-approved by the corporation's board of directors or similar body.[39] Moreover, the DRIP had to provide for the reinvestment of the repatriated dividends as a funding source for "worker hiring and training, infrastructure, research and development, capital investments, or the financial stabilization of the corporation for the purposes of job retention and creation."[40]

Although the list of permitted uses in section 965 was not exclusive,[41] the mention of "worker hiring" and "job creation" was no afterthought. In fact, legislators had rejected an earlier House version of section 965 that would have conditioned the deduction for repatriated earnings by requiring merely that the earnings "be invested in the United States pursuant to a plan approved by the senior management and board of directors."[42] The statute's only clear admonition on the use of repatriated funds was that they could not be used to pay executive compensation and at the same time support a deduction.[43]

[39] I.R.C. § 965(b)(4)(A).

[40] I.R.C. § 965(b)(4)(B).

[41] I.R.C. § 965(b)(4). *See also* Conf. Rep. No. 108-755 ("The conferees note that the list of permitted uses is not exclusive. . . . Dividends with respect to which the deduction is not being claimed are not required to be included in any domestic reinvestment plan.")

[42] H.R. Rep. No. 108-548, at 146-47 (2004). *See also* text accompanying notes 33-37. The list of permitted uses in section 965(b)(4) appears to be the result of political compromise. Legislators rejected a Senate amendment that would have limited the amount of qualifying dividends to those used to increase wages, capital expenditures, research expenditures, and nondeductible pension contributions during 2005 through 2007 over the corresponding amounts of these same expenditures incurred during 2001-2003. Senate Amendment 1137, 150 Cong. Rec. S4918, S4861 (May 5, 2004). Supporters of the amendment described it as an enforcement mechanism necessary to ensure that corporations used the repatriated funds for job creation purposes. *See, e.g.,* Cong. Rec. S4861 (statement of Sen. Breaux). Detractors rejected the amendment as an unnecessary attempt to interfere with a company's finances. *See, e.g.*, Cong. Rec. S4863 (statement of Sen. Smith).

[43] I.R.C. § 965(b)(4).

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C. *Permitted Uses*

The statute's lack of clarity left open many questions and its one-year election period required the need for prompt IRS guidance.[44] The IRS issued a series of three notices, the first of which, Notice 2005-10, was close to 75 pages long.[45] The guidance was, in large part, warmly received by U.S. corporations and the tax practitioner community because of its broad interpretation of what constituted a permitted use.[46] For instance, beyond requiring the parent corporation to prepare and approve a DRIP, Congress had failed to include a segregation or direct tracing requirement in the statute. The IRS also dismissed the need for the taxpayer to source the permitted investment to the repatriated funds, declaring such a rule to be too difficult to administer.[47] Thus, when the IRS subsequently issued guidance declaring that repatriated amounts could not be used to pay dividends or redeem stock,[48] the prohibition had lost much of its impact. As an example, in December 2004, after Congress passed the AJCA, Microsoft declared a $32 billion extraordinary dividend.[49] Three months later, Microsoft's quarterly report

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[44] I.R.C. § 965(f). Practitioners highly anticipated guidance from the IRS about permitted uses of repatriated funds. *See* Robert Goulder, *DeVovio Previews Coming Repatriation, Manufacturing Deduction Guidance*, 2004 TNT 222-4 (Nov. 17, 2004), Christopher M. Netram, *Repatriation Guidance to Following Deferred Compensation Rules, DeNovio Says*, 2004 TNT 235-3 (Dec. 7, 2004). *See generally* Peter H. Blessing, *Bringing It All Back Home: Repatriations Under the American Jobs Creation Act of 2004*, 105 TAX NOTES 965 (2004).

[45] Notice 2005-10, 2005-1 C.B. 474. Subsequent guidance was more narrowly tailored. Notice 2005-38, 2005-1 C.B. 1100, addressed the limitations in section 965(b) on the amount of dividends that the U.S. shareholder could treat as eligible for the deduction, including the effects of certain transactions on those limitations. Notice 2005-64, 2005-2 C.B. 471, provided guidance on foreign tax credits issues relating to section 965.

[46] *See* Margie Rollinson, *et al.*, *Welcome (Mostly) Guidance on the New Repatriation Provisions*, 106 TAX NOTES 444 (2005), New York State Bar Association Tax Section, *The U.S. Temporary Dividends Received Deduction*, 39 TAX NOTES INT'L 53 (2005).

[47] *See* Christopher M. Netram, *Repatriation Guidance to Follow Deferred Compensation Rules, DeNovio Says*, 2004 TNT 235-3 (Dec. 7, 2004). According to Notice 2005-10, the DRIP needed only to "provide sufficient detail to enable the taxpayer to demonstrate upon examination that the expenditures that subsequently occur were of the kind that were in fact contemplated at the time of the adoption of such plan." Notice 2005-10, at 14-15.

[48] Notice 2005-10, § 9.

[49] Gary Rivlin, *Microsoft to Pay Special Dividend to Shareholders*, N.Y. TIMES, July 21, 2004 at A1.

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stated: "Based on our current understanding of the [AJCA], we believe that we may repatriate from $0 to $780 million in dividends. . . . If we decide to repatriate earnings, [we] will seek the required chief executive officer and Board of Directors approval of the required domestic reinvestment plan within the timeframe the incentive is available.[50] Given the fungible nature of money, the lack of a tracing requirement allowed corporations to repatriate funds for nonpermitted purposes, then later make permitted investments out of domestic earnings.[51]

IRS guidance also failed to require any net increase, absolute or percentage-wise, in overall funds invested within the U.S. as compared with funds held overseas.[52] According to Notice 2005-10, "amounts invested in the United States pursuant to the domestic reinvestment plan are not required to exceed . . . investments that were planned by the taxpayer prior to enactment of section 965."[53] For example, if, in 2003, a corporation had decided to expand its product line and workforce beginning in 2005, the corporation could use repatriated funds to pay for the expansion and still obtain the deduction. The corporation's domestic earnings for 2005 that might have otherwise been devoted to the pre-planned expansion could be used for executive compensation, dividends, and other nonpermitted purposes.

One item in the list of permitted uses, "financial stabilization of the corporation for the purposes of job retention and creation," gave rise to considerable uncertainty and

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[50] Microsoft Corp., Quarterly Report (Form 10-Q), at 26 (Mar. 31, 2005). *See also* Kingston, at 389-90.

[51] IRS guidance also allowed the investments to take place over a reasonable period of time. Notice 2005-10 includes an example concluding that three years is a reasonable period. Notice 2005-10, at 16. Thus, the parent corporation could be entitled to a deduction for repatriated earnings despite three years of nonpermitted use. Empirical research, explained in more detail in Part III, below, reveals that corporations used a large percentage of repatriated earnings for stock repurchases. *See* Part III.A., *supra*.

[52] A Senate amendment would have imposed such a requirement, but senators rejected the amendment. *See supra* note 44. The rules relating to third-party indebtedness in section 965(b)(3) do test for a change in overall position, but those rules apply only to the amount of indebtedness owed by the foreign subsidiaries to their U.S. corporate shareholders. Furthermore, Notice 2005-38 allowed the U.S. parent corporation to retain the deduction even when it guarantees debt of the foreign subsidiary that the subsidiary uses to pay dividends. Notice 2005-38, at 13-14, 74-80.

[53] Notice 2005-10, at 12-13.

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debate about the phrase's meaning. IRS guidance adopted what might fairly be termed a trickle-down theory about what types of investments create or retain jobs.[54] Notice 2005-10, for instance, allowed the corporation to use repatriated funds to pay down corporate debt "so long as the repayment contributes to the financial stabilization of the taxpayer for the purposes of job retention or creation in the United States."[55] This open-ended interpretation is largely meaningless.[56] While improving the corporation's debt/equity ratio may contribute to its overall financial health, the connection between reduced debt and job creation is tenuous. Nevertheless, the IRS left that decision largely to the taxpayer. According to Notice 2005-10, debt payments do contribute to financial stabilization when, in the taxpayer's "reasonable business judgment," the repayment will be "a positive factor in its ability to retain or create jobs within the United States."[57]

Thus, while the IRS's broad interpretation of the permitted uses in section 965(b) did little to ensure that corporations used the repatriated funds for job creation purposes, some of its statements may have run counter to the legislation's efforts to encourage job creation.[58] For example, Notice 2005-10 permitted a corporation's acquisition of a pre-existing business as part of a tax-free reorganization to count as a permitted domestic reinvestment of foreign earnings to the extent of the acquired business's underlying assets.[59] As one commentator has pointed out, while construction of a new factory does

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[54] The IRS also interpreted the "infrastructure" and "capital investments" uses broadly. According to Notice 2005-10, these terms could include any facility that "support[s] the taxpayer's business." Notice 2005-10, at 24. The terms could also encompass "plant, property and equipment, communications and distributions systems, computer hardware and software, databases, and supporting equipment." *Id.*

[55] Notice 2005-10, at 26.

[56] Kingston described the term "financial stabilization" as signifying nothing more than "political cover". Kingston, at 388-89.

[57] Notice 2005-10, § 8.03(c).

[58] Few within the government criticized the broad scope of the notices. The harshest criticism, it seemed, came from the Treasury Inspector General for Tax Administration. The TIGTA lamented the fact that the IRS's delay in issuing the guidance cost corporations money. Allen Kenney, *TIGTA Says Repatriation Guidance Came Too Slow*, 2005 TNT 193-4 (Oct. 6, 2006).

[59] Notice 2005-10, at 31-32 (requiring the parent corporation to acquire at least a 10% interest in the acquired entity after the transaction). Notice 2005-64 did warn taxpayers that general anti-abuse provisions, such as the step-transaction and substance-over-form doctrines, applied in the context of section 965, but given the lack of a tracing requirement and the broad interpretation of permitted uses, the notice

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increase total U.S. investment, acquisition of an existing factory does not. In fact, if the business being acquired is owned by a foreign individual or entity, the repatriated funds used to acquire the business go back overseas.[60] Moreover, just because a business has a new owner does not guarantee the acquired business will expand its workforce. The acquired enterprise could just as easily cut costs, along with existing jobs.[61]

D. *Empirical Research Surrounding the Repatriation Holiday* in *Section 965*

Before Congress enacted the repatriation incentive in section 965, the Congressional Research Service released a study estimating that U.S. corporations with foreign operations were holding $639 billion in profits overseas in order to defer U.S. tax.[62] Estimates released after section 965 was enacted reveal that U.S. corporations responded enthusiastically to the repatriation incentive.[63] This research further reveals

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represented a timid attempt to halt egregious action on the part of corporations. Notice 2005-64, § 7.04 at 124, *see also* Notice 2005-64, §10.01. Technical corrections enacted in 2005 also amended section 965(b)(3) to grant the IRS authority to prevent the avoidance of the limitations contained in subsection (b)(3). TTCA of 2005, § 403(q)(3). The IRS and Treasury did not issue any regulations.

Notice 2005-10 also contained a reporting requirement, which required corporations to submit annual statements to the IRS for a five-year period specifying what percentage of their planned investments were completed during the year and whether the repatriated amounts were used for the investments set forth in the corporation's DRIP or in alternate investments. The notice also contained a safe harbor provision. The taxpayer had to file annual reports for only a three-year period as long as the taxpayer made 60% of the permitted investments set forth in the corporation's DRIP within the first three years, counting the election year. Notice 2005-10, at 43-45.

[60] Kingston, at 380.

[61] *See* John Rossheim, *Mergers and Layoffs in 2005* (noting that "[e]very wave of mergers is alike in that it generates layoffs."). The dividend repatriation provision has also been criticized for benefiting U.S. exporters that operate primarily overseas when compared with U.S. exporters that operate within the United States. *See* Kingston, at 330-331 ("[T]he Act purported to encourage U.S. competition by allowing both the future accumulation of low-taxed foreign earnings and virtual exemption from tax of those already accumulated. . . . But neither makes up for the injury to some significant U.S. exporters, and the exemption of accumulated foreign earnings widens a disadvantage of exporters that operate (and employ people) primarily in this country.").

[62] David L. Brumbaugh, Congressional Research Service, Tax Exemption for Repatriated Foreign Earnings: Proposals and Analysis 8 (Oct. 22, 2003).

[63] The American Shareholders Association (ASA) reported that by August 2005, U.S. corporations had already announced $210 billion in profit repatriations. *See* Daniel Clifton, ASA Repatriation Scorecard, $200 Billion Repatriated Back to America on Track for $350 Billion Total (Aug. 19, 2005). As of March 2006, the ASA reported that $217 billion had already been repatriated, with another $100 billion still to come. *See* Daniel Clifton, ASA Repatriation Scorecard, $217 Billion Repatriated Back to America, At Least Another $100 Billion On Its Way (March 20, 2006).

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that repatriations were concentrated within a few corporations and that only a small portion of the repatriated profits were used for job creation purposes.

In addition to our own, several studies have examined the impact of the AJCA on repatriated earnings. One set of studies focuses on the level of repatriations triggered by the incentive and the identity of those corporations that repatriated. According to the IRS's own study, 843 of the nearly 9,700 eligible corporations in 2004 took advantage of the deduction.[64] Those 843 corporations repatriated an estimated $312 billion in earnings that qualified for the rate reduction, giving rise to $265 billion in actual deductions.[65] The same study also revealed that the manufacturing sector accounted for nearly 81 percent of the qualifying dividends, with two industries within that sector accounting for over half of the repatriations: The pharmaceutical and medical industries accounted for 32 percent of the total repatriations ($98.8 billion), while the computer and electronic industry accounted for 18 percent of the total ($57.5 billion).[66] The corporations that repatriated the most operated within the manufacturing sector: Pfizer, Inc. ($37 billion); Merck & Co. ($15.9 billion); Hewlett-Packard co. ($14.5 billion); Johnson & Johnson ($10.8 billion); and IBM ($9.5 billion).[67]

Another set of studies focuses on how corporations used repatriated funds and, consequently, the increased level of economic growth triggered by the AJCA. Most studies reveal that the repatriation holiday did not stimulate economic activity within the U.S.[68] These same studies further find that corporations frequently used the repatriated

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[64] Melissa Redmiles, *The One-Time Received Dividends Deduction* , STATISTICS OF INCOME BULLETIN (Spr. 2008), available at http://www.irs.gov/pub/irs-soi/08codivdeductbul.pdf. Eighty-six percent reported the deduction in tax year 2005, 7.7 percent reported it in year 2004, and 6.8 percent reported it in 2006.

[65] Comparing the repatriated amounts to base dividends for the same corporations, researchers found a greater than eight-fold increase in repatriations attributable to the section 965. *See* Donald J. Maples & Jane G. Gravelle, *Tax Cuts on Repatriated Earnings as Economic Stimulus: An Economic Analysis*, Cong. Research Service Report (Jan. 30, 2009), *available at* BNA Daily Tax Rep. (Feb. 3, 2009).

[66] Redmiles, supra note , Figure A. *Compare* Rodney P. Mock & Andreas Simon, *Permanently Reinvested Earnings: Priceless*, TAX NOTES 835, 840 (consistent results).

[67] Mock & Simon, *supra* note , Table 1.

[68] *See* Dhammika Dharmapala, C. Fritz Foley & Kristin J. Forbes, *The Unintended Consequences of the Homeland Investment Act: Implications for Financial Constraints, Governance, and International Tax*

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earnings to support share repurchases, one of the nonpermitted uses.[69] Public source data also supports this conclusion. During 2005, corporations announced record share purchase plans. According to the American Shareholders Association, S&P 500 companies increased their share purchases from $169 billion in 2004 to $334 billion in 2005.[70] Standard and Poor's Investment Services data showed that in the first quarter of 2005 alone, stock buybacks increased 91% ($82.05 billion) from the first quarter of 2004.[71] The fact that the IRS did not issue Notice 2005-10 until early 2005, at which point most corporations probably had not yet completed their reinvestment plans, suggests that other market forces drove the increase in stock buybacks. Still, the lack of tracing requirements and the broad scope of the permitted section 965 uses likely allowed corporations to free up additional earnings, which they directed to existing shareholders, rather than for job creation purposes.[72]

Public source data also reveal increases in mergers and acquisitions activity after Congress enacted section 965,[73] as well as a boost in the dollar exchange rate.[74] These

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Policy, Working Paper (2008), *see also* Jennifer Blouin & Linda Krull, *Brining It Home: A Study of the Incentives Surrounding the Repatriation of Foreign Earnings Under the American Jobs Creation Act of 2004*, Working Paper (2008) (finding that corporations that repatriated under the AJCA increased share repurchases after the Act when compared with nonrepatriating firms). But see Graham, supra note (survey data revealing that 24 percent of repatriated funds were used for capital investment, 23.5 percent used for hiring and training of employees, 14.7 percent used for research and development activities, and 12.4% used to pay down domestic debt. A study by Lee Sheppard and Martin Sullivan analyzed public data sources and found that repatriating firms reduced their aggregate level of employment after the AJCA and were otherwise unable to expand their operations in the U.S. as a result of the repatriated earnings. Lee A. Sheppard & Martin A. Sullivan, *Multinationals Accumulate to Repatriate*, TAX NOTES 295 (2009).

[69] *See* Dharmapala *et al*. (finding that a $1 increase in repatriation increased stock repurchases by $.91), Roy Clemens & Michael R. Kinney, An *Analysis of the Tax Holiday for Repatriations Under the Jobs Act*, TAX NOTES 759 (2008) (finding that only statistically significant increase by repatriating corporations was on stock repurchases), Graham *et al.* (although not finding that repatriated funds were used directly for share repurchases, study did find that 47% of funds freed up by repatriated earnings were used to repurchase shares).

[70] Clifton, ASA Scorecard, at 5 (March 20, 2006) (citing S&P's Quantitative Services).

[71] S&P Investment Services, *Buybacks Surge 91% During First Quarter, Says S & P* (June 6, 2005).

[72] *See* Clifton, ASA Scorecard (Mar. 20, 2006) (noting that dividends and stock repurchases "translate into an increase in the stock value for shareholders." The ASA was also pleased with the "unprecedented amount of cash being returned back to shareholders.").

[73] Investors Business Daily reported that by November 2004, corporations had announced more than $920 billion in mergers and acquisitions deals. This compares with $517 billion in deals announced in 2003 and

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effects may have improved the financial health of corporations and the U.S. economy as a whole, but there is little evidence that these improvements translated into job creation. In fact, American Shareholders Association statistics show decreases in job creation throughout much of 2005, despite the large amounts of offshore earnings corporations were repatriating.[75] Along these same lines, Bureau of Labor Statistics data shows no spike in employment in 2005.[76] Instead, the data reveal only a gradual increase from April 2003 through March 2006.[77] Industry-specific data also shows no connection between repatriations and job growth.[78]

III. DATA AND EMPIRICAL MODEL

A. *Identification of Repatriating Firms and Comparison Samples*

We identify our sample of companies electing to repatriate under the auspices of the AJCA using key-word searches of the Lexis-Nexis 10-K file.[79] We search for companies mentioning repatriation in the context of the AJCA. Key-words in our search

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$843 billion announced in 2004. While the increase may have been due to other factors beyond an influx of repatriated earnings, the author concluded that "[s]ome of that [section 965] money has gone towards deal-making." Dan Gallagher, *Large Buybacks Fail to Boost Shareholder Value*, INV. BUS. DAILY (date).

[74] Large cash flows from foreign countries into the U.S. increases the demand for the U.S. dollar, which causes the dollar to appreciate against foreign currencies. *See* John Kaufmann, *Effect of Foreign Currency Translation on U.S. Repatriations of Foreign Income*, 38 TAX NOTES INT'L 607 (2005). Though Congress may not have sought this impact, some commentators claim it has given "noticeable support to the dollar". Jennifer Hughes & Dan Roberts, *Tax Amnesty Could Bring $100 Billion into U.S.*, FINANCIAL TIMES (Jan. 31, 2005). An appreciation in the value of the dollar, in turn, increases the benefits corporations received from engaging in repatriations. Kaufmann, at 609. One commentator described this situation as a double benefit for repatriating corporations. *Id.* at 613.

[75] Clifton, ASA Scorecard (Mar. 20, 2006).

[76] U.S. Department of Labor, Bureau of Labor Statistics, THE EMPLOYMENT SITUATION (Apr. 2006).

[77] *Id.*

[78] The drug industry, for example, reportedly repatriated about $100 billion in foreign profits, yet, since 2005, the industry has laid off tens of thousands of U.S. workers. Alex Bereson, *Tax Break Used by Drug Makers Failed to Add Jobs*, N.Y. TIMES (July 24, 2007), *see also* Michelle Leder, *The $104 Billion Refund: The Most Absurd Corporate Tax Giveaway of 2005* (Apr. 13, 2006), *available at* www.slate.com/id/2139782 (reporting that IBM, Pfizer, National Semiconductor, and Colgate-Palmolive repatriated significant sums in 2005 but added few, if any, jobs to their existing workforce).

[79] Publicly traded corporations must submit Form 10-K to the Securities and Exchange Commission on an annual basis along with audited financial statements.

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are "repat!" within 50 words of "American Jobs" or "AJCA" or "Homeland Investment" or "HIA."

The repatriation window opened with passage of the ACJA during October 2004, and for each company, ended with the tax year that commenced immediately after the Act was passed.[80] Thus, our sample period begins with 10-Ks for fiscal years ended October 2004, and continues through 10-Ks for fiscal years ended December 2006, filed by March 2007. This sample period encompasses the entire time frame within which companies with varying fiscal year-ends might repatriate under the Act.

We review each 10-K filing from the search -- from one to three per company -- and identify 1,350 companies that mention the possibility of repatriating under the provisions of the AJCA. These companies fall into three categories:

> "Group 1 – repatriate": 476 companies stated they did repatriate under the AJCA. Most companies within this category specify the amount repatriated as well as information about additional taxes due on the repatriated amount or the associated tax benefits.[81]

> "Group 2 – declined": 647 companies stated they had analyzed the possibility of taking advantage of the provisions of the AJCA and had decided not to do so. Most of these companies did not provide any reason for the decision; some simply stated that it would not be beneficial. A few mentioned that their tax position would not benefit from repatriation, or that they always repatriate available funds. A few others reiterated their policy to permanently reinvest foreign funds. [82]

[80] I.R.C. § 965(f).

[81] There is great variety, however, in the quantity of disclosure as well as the definition of "additional taxes" and "tax benefits."

[82] A few companies stated that the repatriation provisions of the ACJA do not affect them because they have no foreign operations or income, or because they are foreign entities themselves. As these companies are not targets of the ACJA, we deleted them from our sample.

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"Group 3 – considered": 227 companies stated that they were analyzing the possibility of repatriating under the AJCA as of the 10-K filing date, but later filings are silent on the topic. We assume these companies either decided against repatriation or that the amount repatriated was immaterial.

Most of our analysis focuses on these three categories of companies, comparing the repatriating companies in Group 1 to the combined set of companies that considered, but decided not to repatriate. That is, they either clearly stated they would not repatriate or considered repatriation, but never reported doing so (Group 2 plus Group 3). We also consider other company groupings, discussed later.

Amounts repatriated are available for 450 of the 476 repatriating companies in our Group 1 sample.[83] These amounts sum to about $298 billion. As discussed in Part II.D., above, the IRS's study of the AJCA using internal tax return data reports that 843 firms repatriated earnings in response to the AJCA and that $312 billion of repatriated funds qualified for the deduction.[84] Thus, our sample captures 56% of the firms, but over 95% of the total dollars repatriated. This suggests that a substantial number of firms repatriated amounts that were not deemed sufficiently material to require financial statement disclosure.

1. Characteristics of Repatriating and Non-Repatriating Firms

Table 1 compares average financial information for repatriating companies to companies that explicitly considered repatriating but did not. Financial information is from Standard & Poor's Compustat database, and is measured at fiscal year-end 2004. Not all companies that mention repatriation are included in the database. Therefore, the statistics below include 466 repatriating companies and 774 non-repatriating companies (98% of all identified repatriating and 89% of non-repatriating companies.) Statistically significant differences between the two groups are noted with an asterisk.

[83] The exact amount is reported by 443 companies. The other seven report tax benefits or savings which we use to estimate the amount repatriate.

[84] Redmiles, *supra* note .

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Table 1: Comparison of repatriating and non-repatriating companies

	Repatriating Companies	Non-Repatriating Companies	
Number of companies:	466	774	
Panel A: Averages			
Assets ($M)	24,833.1	6,702.8	*
Cash / Assets	15%	20%	*
Liabilities / Assets	22%	22%	
Revenues ($M)	7,371.8	3,063.1	*
Percent profitable (pre-tax)	91%	75%	*
Pre-tax Income / Revenues	12%	-32%	
Operating Cash Flow / Sales	15%	-8%	
Panel B: Medians			
Assets ($M)	2,510.5	570.1	*
Cash / Assets	10%	13%	*
Liabilities / Assets	20%	17%	*
Revenues ($M)	2,039.6	517.3	*
Pre-tax Income / Revenues	10%	6%	*
Operating Cash Flow / Sales	12%	8%	*

An analysis of the data in Table 1 reveals several important points. Panel A shows that, on average, repatriating companies are very large - with assets of nearly $25 billion.[85] This is nearly four times greater than the non-repatriating companies' average. Panel A also reveals that repatriating companies had significantly less cash on hand at the end of 2004. However, leverage is similar for both groups.

Panel A further reveals that the average repatriating company reported revenues of over $7 billion in 2004, more than twice the amount reported by non-repatriating companies. A higher percentage of repatriating companies were profitable, but despite large differences in profit and cash flow margins, the average differences are not statistically significant.

[85] These results are consistent with the IRS's analysis of repatriating firms. *Id.* at __.

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Because the presence of a few extremely large companies affected some of the averages disproportionally, we calculated in Panel B of Table 1 medians for comparison purposes. The median assets figure indicates that the typical repatriating company is much smaller than suggested by averages: median assets are $2.5 billion for repatriating firms. However, median assets remain statistically higher for repatriating companies relative to non-repatriators. [86] Statistical tests of medians measures also show that repatriating firms have more debt, are more profitable, and have higher operating cash flows than non-repatriators. Overall, repatriating companies appear to be relatively large, mature, and profitable enterprises.

2. *Industry Membership*

Table 2 presents two pictures of the industry membership of repatriating companies. The first column shows the percentage distribution of repatriating companies across Standard Industrial Classification (SIC) industry groups. Our primary level of analysis is one-digit SIC codes. We also break out two-digit level industry groups that include more than 5% of repatriating companies or repatriated dollars.

More than 60% of the repatriating companies in our sample are in manufacturing industries (SIC codes 2000 - 3900). Within these larger groups, there are several concentrations in more specific industry groups. Twelve percent of all repatriating companies are found in SIC code 2800 – Chemicals and Allied Products. This group includes pharmaceutical companies, which account for 6% of all repatriating companies. Manufactures of various computer, electronic and medical instrument manufacturers each represent 8%-9% of all repatriating companies.

[86] Averages and medians differ so greatly in part because of extremely high asset balances for financial-industry firms. For example, seven firms report asset balances greater than $600 billion. Six of the seven are from the financial industry, and all but one of the seven repatriated. (Citibank, JP Morgan, Bank of America, Morgan Stanley, Merrill Lynch and General Electric are the six repatriating companies; AIG did not report repatriating.)

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Table 2: Industry membership of repatriating companies

SIC	Industry	Distribution of repatriating companies	Percent of Industry repatriating
0,1000	Agriculture, Mining & Construction	4%	2%
2000	Food, apparel, timber and chemical manuf.	8%	9%
20	Food and kindred products	3%	9%
28	Chemicals and allied products	12%	7%
3000	Plastics and fabricated metals manuf.	14%	11%
35	Computer equip., industrial mach.	9%	10%
36	Electronic components and equip.	9%	7%
38	Medical and laboratory instr.	8%	7%
4000	Transportation	6%	3%
5000	Wholesale & Retail	7%	5%
6000	Finance, insurance & real estate	9%	1%
7000	Entertainment, lodging and business serv.	1%	3%
73	Bus services, programming, data proc	8%	3%
8000	Health, legal and other services	2%	3%
9000	Public administration	0%	0%
Total		100%	4%

Apart from manufacturing, the next largest concentrations are in SIC 6000 - Finance, insurance and real estate (9%), and Business Services (SIC 7300), which is mainly programming and data processing services. In general, these percentages are consistent with industries expected to engage in extensive foreign operations.[87]

The second column of Table 2 shows the percentage of all Compustat companies from each industry that repatriated. Percentages range from less than 1% of public administration companies included in Compustat to about 10% of manufacturing companies scattered across various SIC 2000-3000 codes. Because the Act pertains only to companies with both foreign operations and specific tax positions, it is not surprising that most companies did not repatriate under its auspices. However, the very low rates of participation may be unexpected.

[87] *Compare id.* Figure A (consistent results).

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3. *Factors Associated with Repatriation*

Logistic regression analysis, shown in Table 3, provides a combined analysis of these characteristics, to provide an assessment of which factors are most significant in determining whether a company repatriated. The model includes the company characteristics included in Table 1 and industry indicator variables for the industries shown in Table 2. None of the industry indicators is significant in the model, so their coefficients are not shown in table 3. The overall model is statistically significant, and the constant (also not shown) is negative and significant.

Table 3: Logistic Regression Results:
Repatriating companies = 1, Non-repatriating companies = 0

	Regression Coefficient	Significance Level
Total assets (natural log)	.415	.000
Cash /Assets	.225	.640
Liabilities / Assets	-.409	.269
Reporting pre-tax income (vs. loss)	.729	.001
Operating Cash Flows / Sales	1.918	.000
Indicator for each industry group in table 2	varies	> .600

These results confirm that larger, profitable companies, generating relatively higher cash flows from their revenues were more likely to repatriate. On the other hand, relative cash and liability balances do not appear to be significant factors. [88]

Turning to amounts repatriated, Table 4 provides the sum, average amount repatriated per company, and the amount repatriated as a percentage of total assets, by industry for the 450 companies with repatriation amounts available.

[88] These results are consistent if market value or sales are substituted for total assets as a measure of size. Other variables, including sales growth, ratio of foreign to total sales, and different measures of profitability and leverage were tested in the model. They were not significant and/or did not change the inferences drawn from the results shown in Table 3.

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Table 4: Amounts repatriated by industry

SIC Groups		Count	Total $M Repatriated	Ave. $M Company	Ave. % Assets
0,1000	Agriculture, Mining & Construction	19	4,015.8	211.4	6%
2000	Food, apparel, timber and chemical manuf.	35	15,806.8	451.6	6%
	20 Food and kindred products	15	19,953.2	1,330.2	7%
	28 Chemicals and allied products	52	120,180.6	2,311.2	11%
3000	Plastics and fabricated metals manuf.	59	15,392.3	260.9	7%
	35 Computer equip. industrial mach.	40	30,953.5	773.8	9%
	36 Electronic components and equip.	44	22,568.7	512.9	12%
	38 Medical and laboratory instr.	36	14,201.6	394.5	14%
4000	Transportation	28	6,534.4	233.4	2%
5000	Wholesale & Retail	32	7,645.4	238.9	6%
6000	Finance, insurance & real estate	37	17,220.9	465.4	3%
7000	Entertainment, lodging and business serv.	7	1,707.8	244.0	3%
	73 Bus services, programming, data proc.	36	19,806.3	550.2	10%
8000	Health, legal and other services	8	1,149.2	143.6	8%
9000	Public administration	2	1,223.7	611.9	1%
Total		450	298,360.0	663.0	8%

Figure 1

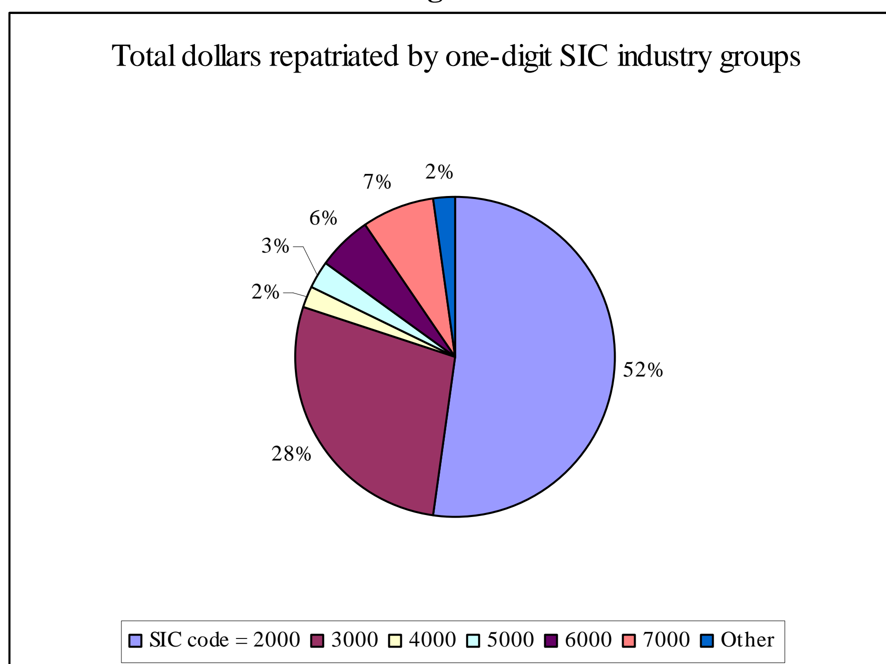

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Figure 1 shows that more than half of all repatriations are attributable to companies from the SIC 2000 codes.[89] In turn, 63 percent of SIC 2000 repatriation amounts is attributable to companies in the Drug Industry (SIC 2830). The $96 billion repatriated by these 26 pharmaceutical companies is more than four times the total amount repatriated by all 44 companies in the next largest group, Electronic Components and Equipment (SIC 3600), which repatriated a total of $22.5 billion.

Overall, the average amount repatriated per company was $663 million, with the average pharmaceutical and food company repatriating over $2 billion and $1 billion respectively. Companies in these industries also tended to repatriate amounts representing higher percentages of their total assets, as did most other manufacturing companies and those involved in business services.[90]

Similar to the logistic regression analysis above, we use regression analysis to weigh which factors are associated with repatriating higher amounts. The model in Table 5 analyzes the 434 repatriating companies with all necessary data. The overall model is statistically significant (p-value <.001), and its adjusted-R^2 is .48, suggesting about half of the variation in amounts repatriated is explained by the model.

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[89] Our results are consistent with those in the IRS Study. Redmiles, *supra* note _, Figure A.

[90] However, it is likely that service companies have relatively low asset bases since they usually do not require extensive physical plants.

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Table 5: OLS Regression Results:
Dependent variable = amount repatriated[91]

	Regression Coefficient	Significance Level
Total assets	.915	<0.001
Cash /Assets	3.702	<0.001
Liabilities / Assets	1.186	0.085
Reporting pre-tax income (vs. loss)	-.314	0.330
Operating Cash Flows / Sales	1.679	0.023
Indicator for SIC 3800	2.196	0.085
Indicator for other industry groups in table 2	varies	> .125

Our results indicate that larger companies with both more cash and more leverage are likely to repatriate higher amounts. While pre-tax profitability does not appear to be a factor (at least profitability in 2004), higher relative cash flows are associated with repatriating more dollars. After controlling for company financial characteristics, the only two-digit industry that appears to repatriate relatively higher amounts is SIC 3800, Medical and Laboratory Equipment.[92]

Appendix I presents descriptive statistics on the 105 firms that repatriated at least $500 million under the auspices of AJCA, ordered by repatriation amount. Pfizer repatriated the largest amount, $37 billion which are 30% of total assets and amount to 70% of revenue for the 2004 fiscal year.[93] Another outlier is Schering-Plough, which repatriated $9.4 billion. This amount ranks it sixth among repatriators, but first when ranked by percentage of 2004 assets at 59% and also first in ranking by percentage of revenue at 114%.

[91] OLS regression analysis assumes that variable measures follow a normal distribution. Based on tests for each variable, the equation uses the natural log of the amount repatriated, total assets, leverage, and operating cash flows, to better approximate this assumption.

[92] Large repatriators in this group include Baxer International, Becton Dickinson, Boston Scientific and Guidant Corporation; each repatriated over $1B.

[93] Our results are consistent with those reported in Mock & Simon, *supra* note , Table 1.

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B. *Repatriation and Lobbying Activity*

We expand upon our research of the AJCA by calculating the rate of return for those firms that repatriated in response to the legislation and that lobbied Congress to enact the repatriation holiday. Prior statistical studies analyzing returns to lobbying have been hampered by an inability to quantify returns to lobbying and lobbying expenditures. Focusing on the tax benefits associated with the repatriation holiday allows us to overcome the challenges of quantifying returns given that the AJCA allowed taxpayers to claim the benefits for a single year only, combined with the fact that the amounts repatriated (and sometimes the resulting tax savings) were disclosed by corporations on the firm's audited financial statement.[94] We overcome the second challenge of quantifying lobbying expenditures by analyzing disclosure statements that identify the amount a corporation spend on lobbying and the purpose of the lobbying expenditure. Our analysis is explained below.

1. *Empirical Model*

In our study we hand-collect lobbying expenditures for firms in our sample of repatriators.[95] Lobbying disclosures are required under the Lobbying Disclosure Act of 1995.[96] Each organization must file a lobbying report with the Clerk of the House of Representatives and the Secretary of State. The form identifies the Registrant (firm that has hired the lobbyist), lobbying expenditures in dollars, and the type of lobbying activity. In addition, the form requests identification of specific lobbying issues (for example, International repatriation or Homeland Investment Act). We gather the registration lobbying expense and lobbying activity from the semi-annual filings available online at http://sopr.senate.gov.

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[94] Although the AJCA included tax benefits in addition to the repatriation holiday in section 965, the financial statements we examined included disclosures reporting tax savings attributable to the repatriation holiday, separate and apart from any other tax benefits that may have been derived from other provisions in the AJCA.

[95] We also used CapitalEye.org to identify firms lobbying for the AJCA.

[96] 26 U.S.C. § 1601.

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Firms are not required to disclose amounts spent on particular initiatives, such as the AJCA, although a few did. For most firms we estimate the *maximum* amount that could have been spent related to the AJCA. Therefore, any bias in our estimated lobbying amounts is likely to overestimate amounts spent lobbying specifically for the AJCA.[97] We choose this bias over a procedure which would underestimate AJCA expenditures because lower investment leads to a higher return on investment,[98] and we do not want to overstate the estimated return.

2. *Results*

Of the 450 firms reporting repatriation amounts, we identify lobbying expenditures likely related to the AJCA for 93. Of these, 39 belonged to a coalition lobbying for the repatriation provisions in the AJCA and 54 did not.[99] Estimated lobbying amounts range from $10,000 to $24.7 million (spent by General Electric). The average amount spent is $3.0 million per company.

Table 6 compares non-lobbying companies to those lobbying with and without membership in a repatriation lobbying coalition. The 39 coalition companies repatriated over $155 billion, 52% of total repatriations. On average, these companies repatriated nearly $4 billion each. The 54 companies that lobbied, but not through a coalition, repatriated $53 billion, 18% of the total. They averaged nearly $1 billion in repatriated earnings per company. Thus, the 357 repatriating companies that did not lobby (80% of all repatriators) account for only 30% of the total amount repatriated. The average

[97] Because not all of the lobbying disclosure statements specified a single bill or piece of legislation, it became difficult to capture lobbying expenses related specifically to section 965. We coded lobbying expenditures in multiple ways (tax lobbying, tax lobbying related to international provisions, lobbying relating to AJCA or HIA). The results set forth in Table 6 reflect conservative estimates using the broadest measure of lobbying expenses. Regression analysis using more targeted estimates of lobbying relating to section 965 reveal similar results.

[98] ROI = Savings/Lobbying expenses.

[99] An additional five firms lobbied against the AJCA, in favor of alternative tax plans. Four of the five eventually repatriated. They are not counted among the firms lobbing for the AJCA.

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amount repatriated for this group was only $250 million per company, or about 1/16th of the average amount repatriated by companies participating in coalition lobbying.

Table 6: Lobbying expenditures for repatriating companies

	No Lobbying	Lobbying with coalition	Lobbying no coalition	Overall
	357	39	54	450
Repatriated amounts				
Total ($M)	89,257.2	155,667.4	53,435.4	298,360.0
Percent of total repatriations	30%	52%	18%	100%
Per company average ($M)	250.0	3,991.5	989.5	663.0
Estimated tax savings				
Total ($M)	26,554.3	46,157.5	15,897.0	88,608.8
Per company average ($M)	74.4	1,183.5	294.4	196.9
Lobbying expenditures				
Total ($M)	n/a	179.6	103.1	282.7
Per company average ($M)	n/a	4.6	1.9	3.0
Lobbying expenditure / repatriated amount				
Overall percentage	n/a	0.1%	0.2%	0.1%
Per company average percentage	n/a	0.8%	1.4%	1.2%
Savings / lobbying expenditure				
Overall return on lobbying	n/a	257	154	220
Per company average return	n/a	767	943	869
Average return for lobbying > $1M	n/a	276	198	243
Per company median	n/a	206.3	151.9	172.2

Table 6 also shows the estimated tax savings for each group. Because relatively few companies quantify the tax benefits of repatriation, and because it is not always clear how reported benefits are calculated, we use a simple estimate of tax savings based on the most likely marginal tax rate (35%). Thus, our estimated tax savings for each company is 85% of the amount that would otherwise have been paid for taxes: (amount repatriated x 35% x 85%). Using this measure, the total estimated savings by these firms is over $88 billion dollars, with more than 50% of the total savings accruing to the 39 coalition companies. The average tax savings for each of these companies is over $1 billion.

We also provide comparisons of lobbying amounts relative to dollars repatriated and estimated tax savings. Overall, the amount spent on lobbying was .1% of the total

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amount repatriated. However, because some companies spent much more than others, the average of the per company percentages of the amount spent on lobbying compared with the amount eventually repatriated was 1.2%. This percentage was lower for the coalition participants (.8%), because their repatriations were so great.

Dividing the estimated tax savings by the estimated amount spent on lobbying gives an estimate of each companies' return on their lobbying investment. This measure gives an overall return of 220 times the investment. ((46,157.5 + 15,897.0)/282.7). That is, for every dollar spent on lobbying, there was a tax savings equal to about $220. In percentage terms, this is a 22,000% return. As might be expected, returns are higher for coalition participants.[100]

However, some companies invested very little in lobbying, but repatriated large amounts, giving returns of thousands of dollars for every lobbying dollar. (The highest return is more than $13,000 for each lobbying dollar.) Therefore, the average of the per company returns are much higher: 767 times for the average coalition participant, and 943 times for the average non-coalition company lobbying for the Act.

Because of these extreme values for companies that did not invest heavily in lobbying activity, we also limit the sample to the 48 companies that appear to have spent more than $1 million lobbying for the AJCA. When we limit the sample to those with the most serious commitment to seeing the AJCA passed, the returns for these companies are similar to the overall returns. For each dollar invested, returns were about $243.

IV. IMPLICATIONS/CONCLUSION

[100] In alternative analysis, we eliminate five firms that repatriated and engaged in lobbying but for which we are less certain about their support for repatriation during the legislative process. When we exclude these firms, the return on lobbying increases to 228:1. Therefore, we present the full sample in the main results as this is a more conservative estimate.

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The one-time dividend deduction provides a unique opportunity to quantify the returns to lobbying expenditures in a tight setting. Unlike most other legislation, the proposal had a short life; the idea was spawned in 2002 and by 2004, it was enacted into law. This short life enables us to isolate the tax lobbying expenditures more precisely. In addition, the savings from the repatriation provision are publically disclosed in financial statements filed with the Securities and Exchange Commission in annual 10-K reports. Unlike other tax law changes, this provision had a material impact on many firms' financial statements and thus, disclosure was required. The disclosed amounts were audited by independent accounting firms before the report was filed.

We find that firms lobbying for this provision had a return in excess of twenty-two thousand percent on their lobbying expenses. Repatriating firms were more profitable overall, but surprisingly, profitability was not a predictor or repatriation amount. Rather industry and firm size was most predictive. Cash on hand, which proxies for ability to repatriation, was not associated with the repatriation decision or the repatriation amount.

Firms lobbying for the repatriation provision were quite effective in receiving lucrative tax benefits but the tax policy implications are troubling, particularly in light of recent efforts by some members of Congress to renew the repatriation holiday for a second time.[101] The tax benefits are accrued to older, larger firms that are declining in market value. Many economic development policies are aimed at supporting emerging firms and industries; this tax provision appears to be doing the opposite as it provides tax subsidies to well-established firms and industries with declining opportunities and market growth. Coupled with recent research that suggests firms used repatriation funds to repurchase stock and bolster their financial position instead of pursuing business opportunities,[102] the efficacy of another repatriation holiday is highly questionable.

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[101] *See* Alison Bennett, *Ensign, Boxer to Seek Repatriation Break in Senate Economic Stimulus Bill, Aide Says*, 19 BNA DAILY TAX REP. (Feb. 2, 2009) at G-4.

[102] *See* Krull & Blouin, *supra* note .

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Our results also raise larger issues about optimal lobbying expenditures by firms and firms' incentives to lobby for some benefits and not others. One would expect firms to devote to lobbying an amount that produces an acceptable, but modest, rate of return. Our results question how firms calculate an acceptable rate of return and whether firms view lobbying for tax benefits differently than other types of lobbying. Compared to other rent-seeking behavior, lobbying for tax benefits is relatively transparent. And while one might expect that the rate of return to lobbying would be lower in cases in which (1) the potential benefits are capable of being estimated in fairly specific dollar terms and (2) the information about these benefits is available to lobbyists, legislators, and other interest groups, our results seem to indicate just the opposite. Using our existing data and compiling additional data on lobbying efforts by firms to re-enact the repatriation holiday a second time, we will explore these issues in a future paper.

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Appendix 1
Companies repatriating $500M or more
(105 companies total[1])

Rank	Company	Amount Repatriated	Amount Repatriated/ Total Assets[2]	Revenue[2]
1	PFIZER	37,000	30%	70%
2	MERCK & CO	15,900	37%	68%
3	HEWLETT PACKARD	14,500	19%	18%
4	JOHNSON & JOHNSON	10,800	20%	23%
5	IBM	9,500	9%	10%
6	SCHERING-PLOUGH	9,400	59%	114%
7	DU PONT	9,100	26%	33%
8	BRISTOL-MYERS SQUIBB	9,000	30%	46%
9	ELI LILLY & CO	8,000	32%	58%
10	PEPSICO	7,500	27%	26%
11	PROCTOR & GAMBLE	7,200	13%	14%
12	INTEL	6,200	13%	18%
13	COCA-COLA	6,100	19%	28%
14	ALTRIA GROUP	6,000	6%	9%
15	MOTOROLA	4,600	15%	15%
16	DELL	4,100	18%	8%
17	MORGAN STANLEY	4,000	1%	10%
18	CITIGROUP	3,200	0%	3%
19	ORACLE	3,100	15%	26%
19	WYETH	3,100	9%	18%
21	EMC	3,000	19%	36%
21	MCDONALD'S	3,000	11%	16%
23	MATTEL	2,400	50%	47%
24	HONEYWELL INTERNATIONAL	2,200	7%	9%
24	VERIZON COMMUNICATIONS	2,200	1%	3%
26	BAXTER INTERNATIONAL	2,100	15%	22%
26	FRANKLIN RESOURCES	2,100	26%	60%
28	AMERADA HESS	1,900	12%	11%
28	JPMORGAN CHASE & CO	1,900	0%	3%

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(105 companies total[1])

Rank	Company	Amount Repatriated	Amount Repatriated/ Total Assets[2]	Revenue[2]
30	3M	1,800	9%	9%
30	MERRILL LYNCH & CO	1,800	0%	6%
32	COCA-COLA ENTERPRISES	1,600	6%	9%
33	GUIDANT	1,500	28%	40%
33	PACCAR	1,500	12%	13%
35	ILLINOIS TOOL WORKS	1,404	12%	12%
36	EMERSON ELECTRIC	1,400	9%	9%
37	BECTON DICKINSON & CO	1,300	23%	26%
38	TEXAS INSTRUMENTS	1,290	8%	10%
39	FOREST LABORATORIES	1,239	33%	40%
40	CISCO SYSTEMS	1,200	3%	5%
40	GENERAL ELECTRIC	1,200	0%	1%
42	KELLOGG	1,100	10%	11%
42	LAFARGE NORTH AMERICA	1,100	20%	27%
42	PRAXAIR	1,100	11%	17%
42	WEYERHAEUSER	1,100	4%	5%
46	ANALOG DEVICES	1,055	22%	40%
47	BOSTON SCIENTIFIC	1,046	13%	19%
48	KIMBERLY-CLARK	985	6%	7%
49	AGILENT TECHNOLOGIES	970	14%	14%
50	MEDTRONIC	934	6%	9%
51	SARA LEE	929	6%	5%
52	INTL PAPER	900	3%	4%
53	BLACK & DECKER	888	16%	16%
54	AUTOLIV	810	15%	13%
55	BAUSCH & LOMB	793	26%	36%
56	COLGATE PALMOLIVE	780	9%	7%
56	MICROSOFT	780	1%	2%
58	STRYKER	722	18%	17%
59	BMC SOFTWARE	709	23%	50%

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(105 companies total[1])

Rank	Company	Amount Repatriated	Amount Repatriated/ Total Assets[2]	Revenue[2]
60	LEXMARK INTERNATIONAL	684	17%	13%
61	ALLERGAN	674	30%	33%
62	IMS HEALTH	647	34%	41%
63	TOYS R US	607	6%	5%
64	C.R. BARD	600	30%	36%
64	TELLABS	600	17%	49%
66	H.J. HEINZ	588	6%	7%
67	MARSH & MCLENNAN	585	3%	5%
68	COMPUTER ASSOCIATES	584	5%	16%
69	EASTMAN KODAK	580	4%	4%
70	STARWOOD HOTELS & RESORTS	550	4%	10%
71	HERTZ	548	4%	8%
72	HASBRO	547	17%	18%
73	DEVON ENERGY	545	2%	6%
74	LOUISIANA PACIFIC	517	15%	18%
75	AUTODESK	512	45%	41%
76	ACE LTD	500	1%	4%
76	ADOBE SYSTEMS	500	26%	30%
76	ALTERA	500	29%	49%
76	AMERICAN POWER CONVERSION	500	27%	29%
76	AMERICAN STANDARD	500	7%	5%
76	AMGEN	500	2%	5%
76	ANADARKO PETROLEUM	500	2%	8%
76	BURLINGTON RESOURCES	500	3%	9%
76	CADENCE DESIGN SYSTEMS	500	17%	42%
76	CARDINAL HEALTH	500	2%	1%
76	CATERPILLAR	500	1%	2%
76	CITRIX SYSTEMS	500	39%	67%
76	DUKE ENERGY	500	1%	2%
76	ESTEE LAUDER	500	13%	9%

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Companies repatriating $500M or more
(105 companies total[1])

Rank	Company	Amount Repatriated	Amount Repatriated/ Total Assets[2]	Revenue[2]
76	GREAT ATLANTIC & PACIFIC	500	18%	5%
76	HARMAN INTERNATIONAL	500	25%	18%
76	KRAFT FOODS	500	1%	2%
76	LAM RESEARCH	500	42%	53%
76	MERCURY INTERACTIVE	500	25%	73%
76	MICROCHIP TECHNOLOGY	500	28%	59%
76	MILLIPORE	500	49%	57%
76	NIKE	500	6%	4%
76	QUALCOMM	500	5%	10%
76	SAFEWAY	500	3%	1%
76	SPX	500	7%	11%
76	ST. JUDE MEDICAL	500	15%	22%
76	SYMANTEC	500	9%	19%
76	WATERS	500	34%	45%
76	XILINX	500	16%	32%
76	YUM BRANDS	500	9%	6%

1. We estimate five additional companies repatriated more than $500 million, although they did not report exact amounts. Company names and their approximate ranks are: Gentek (#3), Chattem (#17), Hewitt (#22), Ford Motor (#53) and Apple Computer (#57).
2. Total assets and revenues are measured at the end of fiscal 2004.

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