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Dear Senator Warren:

We write regarding your proposal to impose a new corporate tax for U.S. companies with more than $100 million in global net income. The tax would be at a rate of 7% on the global net income of U.S. companies in excess of $100 million as reported by companies in their financial statements. The tax would be paid in addition to any existing corporate tax liability. We estimate that close to **1,200 public corporations would be liable for this tax and that it would raise $1.05 trillion on public companies alone over the ten-year budget window 2019-2028**. Our estimates only include public corporations (for which data is readily available) and should thus be seen as lower bounds. This tax would increase federal corporation income tax receipts from the projected $256 billion for fiscal year 2020 to about $340 billion.

Details on the estimation

Data sources:

We use Compustat data, which cover all publicly listed U.S. corporations.

Methodology:

1) The tax base is the global, consolidated net income of U.S. public companies, as reported in Compustat. The first $100 million in net income are exempted from the tax. The corresponding tax base adds up to a bit more than $1.3 trillion in 2018.

2) Since the tax is levied on the global consolidated income of U.S. companies, it cannot be avoided by shifting income to low-tax jurisdictions. Moreover, since the tax is based on income as reported in audited and certified financial accounts and does not allow for any deduction or credit, the possibilities of avoidance are limited. There are three ways to avoid the tax: inverting to a foreign country, splitting to reduce income below the $100 million exemption threshold, or manipulating global net income figures in financial statements by exploiting ambiguities in accounting rules. We discuss below how

regulations can address the first two issues. Based on the IRS estimated tax gap for the corporate income tax, we factor in a 15% tax avoidance rate.[1]

3) In 2019, there would be around 1,200 public companies liable for the tax. The tax base above $100 million would be $1.39tr (assuming 5.5% nominal growth over 2018-2019). A seven percent tax on this base would raise $97 billion in 2019. After reducing it by 15% to account for avoidance, tax revenue would be $83 billion.

4) To project tax revenues over a 10-year horizon, we assume that nominal taxable income would grow at the same pace as the U.S. economy, at 5.5% per year as in standard projections of the Congressional Budget Office or the Joint Committee on Taxation. This growth is decomposed into 2.5% price inflation, 1% population growth, and 2% of real growth per capita. This implies that tax revenue over the 10 years 2019-2028 is 13 times the revenue raised in 2019.[2] This uniform growth assumption is conservative as the income of large companies has been rising faster than U.S. GDP in recent years.

5) This 10-year projection implies that revenue raised by the new corporate surtax would be 13 * 83 = $1,075 billion, rounded to $1.05 trillion.

6) We emphasize that our computation is a lower bound since it is based only on public companies, despite the fact that private companies would also be subject to the tax.

Anti-avoidance measures

Regulations need to be designed to prevent corporations from artificially splitting to reduce income below the $100 million exemption threshold. The regulations should mandate that corporations that are for all intent and purpose part of a single group (e.g., because they have the same owners and take orders from the same persons) should be treated as such (i.e., consolidated) for tax purposes.

Treasury regulations regarding corporate inversions have been significantly strengthened in 2016 and since then corporate inversions have come to a halt. The higher the effective U.S. corporate tax rate, however, the more pressure there will be on that front. The solution to the problem of tax competition from low-tax countries involves greater international tax coordination (in particular, reaching an international agreement on minimum effective corporate tax rates) and the adoption of defensive measures against tax havens and multinationals headquartered in countries refusing international coordination.

Sincerely,

Emmanuel Saez and Gabriel Zucman

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[1] The tax gap estimate for years 2008-2010 is $28 billion for large corporations, equivalent to 15% of federal corporate income tax revenue.

[2] With r=5.5%, we have [1+(1+r)+..+(1+r)^9]=[(1+r)^10-1]/r=12.9, approximately 13.