

# How Big Business Evades Taxes

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Pacific News Service, Apr 09, 2004

*EDITOR'S NOTE: As states and municipalities reel from service cutbacks caused by lower tax earnings, big corporations pay virtually no taxes on huge profits. They do it though elaborate "shell" games.*

Were you stunned by the revelation, days before your taxes are due, that nearly two-thirds of companies operating in America reported owing no taxes from 1996 through 2000? That over 90 percent of large corporations -- with at least \$250 million in assets or \$50 million in gross receipts -- reported owing taxes of only under 5 percent?

The law requires firms to pay 35 percent tax on U.S. profits. Had big business complied, corporate income taxes in 2002 would have been \$308 billion instead of only an estimated \$136 billion. Do you wish you knew the corporate secret?

Is your town or state suffering from service cutbacks because tax revenues are down? Would you like to cut your tax bite from the current 15 to 35 percent to 5 percent or zero? How do corporations do it?

The General Accounting Office report, commissioned by Senators Carl Levin (D-MI) and Byron Dorgan (D-ND) and released April 5, gave a clue to how. It's called "transfer pricing," or improperly shifting income to lower-tax countries.

Firms set up offshore "subsidiaries" which, on their books, perform functions that let them cut onshore taxes. They may sell their own "logo" to the subsidiary and then pay a high price to "rent" it back, deducting "rent" as expense. They may move money to the subsidiary and "borrow" it back, deducting interest payments. If several of their subsidiaries are involved in a deal, the firms may grossly inflate profits assigned to those in offshore tax havens, which levy no or minimal taxes on "profits" claimed there.

The U.S. firm may "trade" with an offshore "shell" it owns -- a phony company set up in a tax haven -- pretending it's buying goods or services at a high price or selling its product low, to create deductions. Because the tax haven keeps owners' names secret, the IRS won't know the company is "trading" with itself.

Professors Simon J. Pak (Penn State University) and John S. Zdanowicz (Florida International University) examined the impact of over-invoiced imports and under-invoiced exports on 2001 U.S. tax revenues. Would you buy multiple vitamins bought from China at \$850 a pound, plastic buckets from the Czech Republic for \$973 each, tissues from China at \$1,874 a pound, a cotton dishtowel from Pakistan for \$154, and tweezers from Japan at \$4,896 each?

By contrast, U.S. companies, on paper, were getting very little for their exports. If you

were in business, would you sell multiple vitamins to Finland at 61 cents a pound, bus and truck tires to Britain for \$11.74 each, color video monitors to Pakistan for \$21.90, missile and rocket launchers to Israel for \$52.03 and prefabricated buildings to Trinidad for \$1.20 a unit?

Comparing claimed export and import prices to real world prices, the professors figured the 2001 U.S. tax loss at \$53.1 billion.

We all know that Enron cheated investors by using offshore firms to pretend that money it borrowed was money it earned. We later found it also used shells to hide income from the IRS. Enron had 881 offshore subsidiaries: 692 in the Cayman Islands; 119 in the Turks and Caicos; 43 in Mauritius and 8 in Bermuda. Enron had no office in the Cayman's, but Box 1350 there received mail for 500 affiliates. Enron's 1996 through 2000 pretax U.S. profits were \$1.8 billion, but it paid no tax in four of those five years. It even got a rebate! Because of fancy paperwork that invented tax losses even while it was boasting of profits to investors, Enron got back \$381 million from the IRS.

Bob McIntyre, who heads the Washington-based Citizens for Tax Justice, says that in 1996-2000, Goodyear's profits were \$442 million, but it paid no taxes and got a \$23-million rebate. Colgate-Palmolive made \$1.6 billion and got back \$21 million. Other companies that got rebates in 1998 included Texaco, Chevron, PepsiCo, Pfizer, J.P. Morgan, MCI Worldcom, General Motors, Phillips Petroleum and Northrop Grumman. Microsoft, run by the world's richest man, reported \$12.3 billion U.S. income in 1999 and paid zero federal taxes. In the past two years, Microsoft paid only 1.8 percent on \$21.9 billion pretax U.S. profits.

There are some 55 "offshore" zones, including legendary Switzerland; the Caribbean with money-laundries Grand Cayman, Antigua, Aruba and the British Virgin Islands; European favorites Luxembourg, Liechtenstein, Monaco, Austria, Cyprus; and British Channel Islands Jersey, Guernsey, Isle of Man. Many banks in "offshore" centers are subsidiaries of major international banks, including Citibank, Bank of New York and Credit Suisse.

Why does Washington tolerate the offshore tax evasion system? Because powerful people benefit. With President Bush on its board, Harken Energy set up an offshore network that cut its taxes. White House spokesman Dan Bartlett defended Harken for seeking "tax competitiveness," the preferred euphemism. When Vice President Cheney ran Halliburton, it increased its offshore subsidiaries from 9 to at least 44.

*Lucy Komisar is a freelance journalist who is writing a book about the offshore bank and corporate secrecy system.*