



FOR IMMEDIATE RELEASE: February 4, 2005

CORPORATE TAX SHELTERS IN A GLOBAL ECONOMY

Why They Are a Problem and What We Can Do about It

By Daniel N. Shaviro

The complexity of our existing tax code encourages aggressive tax management or “evasion.” For example, Enron designed its Apache transactions to shelter interest income from taxation through complicated maneuvers involving foreign subsidiaries and foreign lenders. Tax reform proposals often include alterations to make the corporate tax code simpler and more transparent in an effort to eliminate “abuse” of corporate tax shelters—the exploitation of various tax rules in unintended ways solely for the purpose of obtaining favorable tax results with no or almost no other economic consequences. But can any tax system eliminate costly evasion activity?

In *Corporate Tax Shelters in a Global Economy: Why They Are a Problem and What We Can Do about It* (AEI Press, January 12, 2005), Daniel N. Shaviro, AEI visiting scholar and Wayne Perry Professor of Taxation at New York University Law School, provides a useful guide to the key economic and legal conceptual issues that must be addressed in order to design truly effective tax reform.

Shaviro attempts to identify the specific aspects of U.S. tax law that lead to extensive “paper pushing” in the interest of tax avoidance, as well as a metric by which a tax authority can establish whether a particular tax planning action should be considered abusive or wasteful. He then explores tax arbitrages that are common among U.S. multinationals and discusses their economic consequences.

The author discusses policies that can soften the economic blow from avoidance activities. For instance, tax sheltering opportunities that exploit the law for unintended purposes can be significantly discouraged by requiring taxpayers to accept at least a modicum of accompanying business risk. Shaviro recommends that the government, therefore, toughen economic substance standards, requiring that tax-motivated transactions have significant economic consequences beyond tax avoidance, including exposure to economic risk. These tough standards ought to be accompanied by specific black-letter rules that require a high level of economic substance in particular transactional settings where abuse is a problem.

Only fundamental tax reform, if even that, is likely to make unnecessary an economic substance approach. Any fundamental tax reform, Shaviro concludes, will require rules to ensure that taxpayers face the incentives that are intended by reformers. *Corporate Tax Shelters in a Global Economy* is a valuable guide for those who must establish these rules.

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