AMERICANS FOR TaxFairness

# PFIZER'S TAX DODGING Rx: STASH PROFITS OFFSHORE

The full report is available here.

## Key Findings

Pfizer, one of the world's largest pharmaceutical companies,[1] has announced that it has entered into preliminary discussions with the Irish corporation Allergan to effect a business combination, which most observers assume would be structured as an "inversion" transaction. An inversion would allow Pfizer to renounce its U.S. tax citizenship while retaining its current U.S. headquarters, management structure and facilities.

Pfizer executives have made no effort to hide that their latest inversion attempt is intended to dramatically cut its U.S. tax bill. The company's leaders say they believe that Pfizer's worldwide effective tax rate—which was reported as 25.5% in 2014—could be sharply reduced if the corporation's legal address is shifted to Ireland through an inversion with Allergan.

This report finds that Pfizer appears to be dramatically overstating its corporate tax rate, and that the company may be paying taxes on its worldwide profits that are effectively tax-haven rates. Thus, Pfizer does not appear to be at a competitive disadvantage operating under the U.S. tax system—if anything it is highly advantaged. An inversion would lock in these current advantages and extend them further.

With an inversion, Pfizer essentially would continue to enjoy all the benefits of being an American corporation but just not pay the taxes required for that privilege. Pfizer would not pay its fair share for its educated workforce; use of our transportation systems; the protections provided by our strong judicial, banking and regulatory systems; and so much more that makes America one of the top countries in the world in which to do business, ranking number three according to the World Economic Forum.[2]

Key findings in this report include:

- **ATF estimates that Pfizer's effective (i.e., economic) tax rate on its worldwide income was just 7.5% in 2014, compared with the 25.5% rate the company reported in its Securities and Exchange Commission (SEC) filings.** (This finding was also reported in The Wall Street Journal on Nov. 8, 2015.[3]) Moreover, **ATF estimates that Pfizer's effective tax rate on its worldwide income from 2010 to 2014 averaged just 6.4% when the company's filings reported a 24% tax rate.** Therefore, **up to 75% of Pfizer's reported taxes may be an accounting fiction.** The reason for the discrepancy in estimates is that Pfizer's numbers include very large provisions (reserves) for U.S. tax that will never actually be paid, unless Pfizer elects unilaterally in the future to incur the tax bill, which seems remote.

- **Pfizer had as much as $148 billion in profits parked offshore at the end of 2014, on which it has paid no U.S. income taxes.** Pfizer alone controls whether, when and how much of its foreign earnings might actually be repatriated and therefore taxed. This enormous sum is comprised of two piles of profits:

    - $74 billion in foreign “Permanently Reinvested Earnings” that Pfizer reports to the SEC —foreign profits on which Pfizer has neither paid U.S. tax nor provided a financial accounting liability for any ultimate U.S. tax due; and
    - Up to another $74 billion in “stealth” foreign profits (ATF estimate) on which Pfizer has not actually paid any U.S. tax, but has in its SEC reports created a tax reserve against any U.S. tax that would ultimately be due only if Pfizer should unilaterally choose to “repatriate” those earnings to the U.S., which appears to be unlikely.

- **The offshore stash of profits known as Permanently Reinvested Earnings alone has grown nearly three-fold since a repatriation tax holiday in 2004—from $27 billion in 2005 to $74 billion in 2014.** When the U.S. government gave companies the tax holiday, charging them just a 5.25% tax rate on offshore profits if they voluntarily brought them home and invested in job creation, Pfizer repatriated $37 billion (the most of any company), took $10 billion in tax savings and promptly laid off 10,000 American workers within two years. Pfizer is looking for a similar tax break on its current offshore profits.

- **Pfizer reported losing more than $16 billion in the United States from 2010 through 2014, while it earned $78 billion offshore.** This is a major feat that is likely attributable to profit shifting to tax havens, as the company had 38% of its sales and 48% of its assets in the U.S. in 2014. Pfizer has 151 subsidiaries in 10 tax havens. The engine of Pfizer’s profits—development of new drugs—is heavily concentrated in America, as are its patents.

- **Pfizer pocketed $5.3 billion in federal contracts between 2010 and 2014,** while benefitting from very low effective tax rates those years. About 5% of Pfizer’s $20 billion annual U.S. revenue is from the federal government. Yet, Pfizer does not come close to paying its fair share, and it may desert America for a tax haven through an inversion.

- **Pfizer’s R&D spending since 2002 has increased while its offshore stash of untaxed profits has skyrocketed, suggesting that the increase in Pfizer’s offshore profits and the U.S. corporate tax rate are not stifling new drug investments.** Pfizer’s R&D spending has climbed 1 percentage point since 2002, from 16% of revenue to 16.9% in 2014—while its offshore profits have nearly tripled, rising from $29 billion in 2002 to $74 billion in 2014. One would expect R&D to have plummeted during that time if these offshore profits were critical to financing new drug development.

- **The pay packages of Pfizer’s top five executives doubled between 2004 and 2006, the time period when the repatriation tax holiday kicked in.** A major criticism of the 2004 tax holiday is that much of the money was spent to buy back corporate stock to boost share prices, which provided a windfall for corporate executives, but did little in terms of creating new jobs. The same is likely to happen if Congress provides future tax breaks on repatriated profits, as it has considered doing.

- **Congress can pass legislation that would prevent Pfizer from doing an inversion with Allergan in order to take advantage of the low tax rates in the tax haven of Ireland.** Two remedies will take away the tax advantages of an inversion:

    - **Close the earnings stripping loophole:** This would eliminate the ability of Allergan (Pfizer’s new foreign parent under an inversion) to load up its new U.S. subsidiary (Pfizer) with excessive debt that would be owed to Allergan, debt that Pfizer could claim a hefty U.S. tax deduction on thereby reducing its U.S. tax bill and shifting taxable profits to Allergan in low-tax Ireland.

- **Enact the Stop Corporate Inversions Act (S. 198 and H.R. 415):** These bills would make it very difficult for corporations to desert America for a tax haven, and they would raise $33.6 billion over 10 years, according to the Joint Economic Committee. The bills would not allow for an inversion unless the new foreign parent company acquiring the U.S. company comprised more than 50% of the shareholders. Moreover, the new smaller foreign parent and its U.S. subsidiary would have to pay U.S. taxes if its headquarters remains here and it is managed and controlled from U.S. soil.

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[1] PMLive, "Top 25 pharma companies by global sales" (accessed November 9, 2015). http://www.pmlive.com/top_pharma_list/global_revenues

[2] World Economic Forum, The Global Competitiveness Report 2014–2015, Table 3, p. 13. http://www3.weforum.org/docs/WEF_GlobalCompetitivenessReport_2014-15.pdf

[3] *The Wall Street Journal* (WSJ), "Pfizer Piles Profits Abroad" (November 8, 2015) http://www.wsj.com/articles/pfizer-piles-profits-abroad-1447031546?alg=y