

# The Impact of the Tax Cuts and Jobs Act on Foreign Investment in the United States

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Thomas Brosy

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**Prepared by Thornton Matheson, Alexander Klemm, Laura Power, and Thomas Brosy\***

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**ABSTRACT:** The 2017 Tax Cuts and Jobs Act (TCJA) sharply reduced effective corporate income tax rates on equity-financed US investment. This paper examines the reform’s impact on US inbound foreign direct investment (FDI) and investment in property, plant and equipment (PPE) by foreign-owned US companies. We first model effective marginal and average tax rates (EMTRs and EATRs) by country, industry, and method of finance, and then use those tax rates to calculate the tax semi-elasticities of inbound FDI and PPE investment. We find that both PPE investment and FDI financed with retained earnings responded positively to the TCJA reform, but FDI financed with new equity or debt did not. In country-level PPE regressions, inclusion of macroeconomic controls renders tax rate coefficients insignificant, suggesting that the increase in PPE investment after TCJA was driven by general economic growth. In regressions of FDI financed with retained earnings, however, tax coefficients were robust to inclusion of macroeconomic controls. As the literature predicts, EATRs have a greater impact on cross-border investment than EMTRs. Country-by-industry regressions showed a larger effect of taxes on PPE investment than aggregate country-level regressions, but industry-level tax rates appear to have no effect on earnings retention.

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WORKING PAPERS

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# Contents

<b>GLOSSARY</b>	<a href="#">3</a>
<b>1. INTRODUCTION</b>	<a href="#">4</a>
<b>2. LITERATURE REVIEW</b>	<a href="#">5</a>
<b>3. FOREIGN INVESTMENT</b>	<a href="#">7</a>
<b>4. EFFECTIVE TAX RATES</b>	<a href="#">10</a>
<b>5. MODELS AND DATA</b>	<a href="#">13</a>
<b>6. REGRESSION RESULTS</b>	<a href="#">16</a>
Country-level analysis	<a href="#">16</a>
Country-by-industry analysis	<a href="#">21</a>
<b>7. CONCLUSIONS</b>	<a href="#">23</a>
<b>REFERENCES</b>	<a href="#">26</a>
<b>FIGURES</b>	
1. Foreign Investment in the US	<a href="#">8</a>
2. US Inbound FDI Stock by Industry	<a href="#">9</a>
3. US Effective Tax Rates Before and After TCJA	<a href="#">11</a>
4. Change in Effective Tax Rates on Equity-Financed Inbound Investment by Country, 2017–18	<a href="#">12</a>
5. Change in Effective Tax Rates by Industry, 2017–18	<a href="#">13</a>
<b>TABLES</b>	
1. Descriptive Statistics of Country-Level Regression Variables	<a href="#">15</a>
2. Regressions of PPE Investment	<a href="#">16</a>
3. Regressions of Equity-Financed FDI by Country	<a href="#">17</a>
4. Regressions of Debt-Financed FDI by Country	<a href="#">18</a>
5. Regressions of Retained Earnings-Financed FDI by Country	<a href="#">19</a>
6. Additional Regressions of PPE Investment by Country	<a href="#">20</a>
7. Additional Regressions of Retained Earnings-Financed FDI by Country	<a href="#">21</a>
8. Regressions of PPE Investment, Country-by-Industry	<a href="#">22</a>
9. Regressions of Retained Earnings-Financed FDI, Country-by-Industry	<a href="#">23</a>
<b>APPENDIX</b>	
A. Countries	<a href="#">25</a>

## Glossary

ATR	Average Tax Rate
BEA	Bureau of Economic Analysis
BEAT	Base-erosion Anti-abuse Tax
BTT	Bilateral Tax Treaty
CBO	Congressional Budget Office
CIO	Country of Immediate Origin
CIT	Corporate Income Tax
EATR	Effective Average Tax Rate
EBIT	Earnings Before Interest and Taxes
EBITDA	Earnings Before Interest, Taxes, Depreciation and Amortization
EMTR	Effective Marginal Tax Rate
ETR	Effective Tax Rate
FDI	Foreign Direct Investment
FDII	Foreign-derived Intangible Income
GDP	Gross Domestic Product
GMM	Generalized Method of Moments
IICM	International Investment and Capital Model
IP	Intellectual Property
MACRS	Modified Accelerated Cost Recovery System
MNE	Multinational Enterprise
PPE	Property, Plant and Equipment
TCJA	Tax Cuts and Jobs Act
TPC	Tax Policy Center
UBO	Ultimate Beneficial Owner
US	United States
WHT	Withholding Tax