International Boycott Reports, 2007 and 2008

by Melissa Costa

For Tax Year 2007, 120 "U.S. persons"[1] received about 4,800 requests to participate in boycotts unsanctioned by the United States, while, for Tax Year 2008, 138 U.S. persons received about 3,700 requests. Those receiving requests composed about 7.9 percent of the 1,509 U.S. persons who reported operations in, with, or related to countries known to participate in unsanctioned boycotts for Tax Year 2007 and about 8.6 percent of the 1,596 reporting such operations for Tax Year 2008. Of those receiving requests, 26 agreed to participate for Tax Year 2007 and 33 for Tax Year 2008. Roughly 1 percent of those with operations in countries known to participate in unsanctioned boycotts reported tax consequences for both years.

Operations

Most taxpayers file Form 5713, *International Boycott Report*, with their Federal income tax return to report operations in countries known to participate in boycotts not condoned by the United States. For both Tax Years 2007 and 2008, approximately 90 percent of filers were corporations, while partnerships accounted for another 8 percent. Trusts, estates, and individuals filed most of the remainder.

About 98 percent of Form 5713 filers for both Tax Years 2007 and 2008 reported operations in countries on the list of known boycotting countries maintained by the U.S. Department of Treasury. For 2007 and 2008, that list included Kuwait, Lebanon, Libya, Qatar, Saudi Arabia, Syria, the United Arab Emirates, and Yemen. These countries are known to participate in boycotts of Israel. While the antiboycott laws target any boycotts not sanctioned by the United States, less than 1 percent of filers reported operations in countries known to participate in boycotts of a country other than Israel for Tax Year 2007, and just 3.8 percent did so for Tax Year 2008.

Types of Boycotts

Because the United States does not wish to infringe upon the right of any country to choose its own trading partners, the antiboycott laws do not target primary boycotts, i.e., restrictions on the importation of goods and services originating in the boycotted country into the boycotting countries. Instead, laws are directed against secondary and tertiary boycotts.

Specifically, Internal Revenue Code section 999(b)(3) classifies the disallowed boycotts into the five types below:

1) A person agrees, as a condition of doing business directly or indirectly within a country or with the government, a company, or a national of the country:
   a) to refrain from doing business with or in a country that is the object of the boycott or with the government, companies, or nationals of that country [Type 1 request, as shown in Figure A]; or
   b) to refrain from doing business with any U.S. person engaged in trade in a country that is the object of the boycott or with the government, companies, or nationals of that country [Type 2]; or
   c) to refrain from doing business with any company whose ownership or management is made up, all or in part, of individuals of a particular nationality, race, or religion [Type 3]; or
   d) to refrain from employing individuals of a particular nationality, race, or religion [Type 4]; or
2) A person agrees, as a condition of the sale of a product to the government, a company, or a national of a country, to refrain from shipping or insuring the product(s) on a carrier owned, leased, or operated by a person who does not participate in, or cooperate with, a boycott [Type 5].

Figure A includes the number of persons receiving requests and the number of requests received, by type of boycott. Most of the boycott requests for both Tax Years 2007 and 2008 were either Type 1 or Type 5 requests.

Country of Requests

Table 1 displays the number of persons receiving requests, number of requests received, and number

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[1] As defined in Internal Revenue (IR) Code section 7701(a)(30), U.S. persons are U.S. citizens or residents, domestic partnerships, domestic corporations, and estates or trusts. This excludes foreign trusts or estates whose income from sources outside the United States is not includible in the income of their beneficiaries.

Figure A

International Boycott Reports: Number of Persons Receiving Requests and Number of Requests Received, by Type of Request, Tax Years 2007–2008

Type of boycott request	Number of U.S. persons receiving requests [1]		Number of boycott requests received [2]	
	2007	2008	2007	2008
	(1)	(2)	(3)	(4)
Total	**120**	**138**	**4,823**	**3,716**
Type 1	76	88	2,061	1,824
Type 2	8	8	65	51
Type 3	10	10	75	77
Type 4	9	7	50	34
Type 5	66	69	2,572	1,730

[1] Data in these columns may not add to totals because a person could have received requests of more than one type.
[2] The number of requests are undercounted to the extent that many taxpayers do not specify the number of requests they received. This figure counts an unknown number of requests as one request.
NOTE: For an explanation of each of the five types of international boycott requests, see article text.

of agreements, by boycotting country, for Tax Years 2007 and 2008.

About 90 percent of the requests received for Tax Year 2007, and almost 82 percent of those received in Tax Year 2008, were from persons in Treasury list nations. Entities from the United Arab Emirates accounted for the largest percentage of requests for both years, with 35.7 percent for Tax Year 2008 and 37.8 percent for Tax Year 2007.

Overall, the number of persons receiving requests rose about 15 percent from Tax Year 2007, while the number of requests dropped 23.0 percent, from 4,823 to 3,716. Requests from persons in Saudi Arabia had the largest change, with a drop of nearly 62 percent, from 522 to 199 requests. Requests from Kuwaiti persons fell from 471 to 221, or 53.1 percent. However, requests from Libyans rose 42.9 percent, from 231 to 330. See Figure B.

Tax Penalties

U.S. taxpayers who participated in the boycotts listed may lose their right to claim the foreign tax credit, as well as the tax deferral available to U.S. shareholders of controlled foreign corporations (CFCs) and to shareholders of Interest Charge Domestic International Sales Corporations (IC-DISCs).[2, 3] Taxpayers who had operations in a boycotting country were required to reduce foreign trade income qualifying for the extraterritorial income exclusion, even if they did not participate in a boycott.[4] For both Tax Years 2007 and 2008, just 15 taxpayers reported a loss of this tax benefit.

Taxpayers compute the loss of their extraterritorial income exclusion using the international boycott factor method. Under this method, the loss of tax benefit is determined by the taxpayer's ratio of purchases, sales, and payroll in boycotting countries to the taxpayer's total foreign purchases, sales, and payroll. The amount of foreign trade income qualifying for the exclusion is reduced by the same proportion as the international boycott factor. The boycott reduction in the extraterritorial income exclusion has dropped from the peak of $1,656,910 (in constant 2008 dollars) for Tax Year 2005 due to the gradual repeal of this provision included in the American Jobs Act of 2004. The total reduction fell to $190,786 for Tax Year in 2007 and $6,871 for Tax Year 2008. (Table 2 shows the tax consequences reported for the past 11 years, in constant 2008 dollars, by method of computation.)

For the denial of other tax benefits, taxpayers may use either the international boycott factor method or the specifically attributable method. Under the specifically attributable method, taxpayers reduce each benefit by the foreign taxes paid or foreign income earned that is associated with the operation in the boycotting countries with whom the agreement was made and that would otherwise be eligible for the tax benefits.

[2] A foreign corporation is considered to be a CFC if (on any day during the foreign corporation's tax year) U.S. shareholders own more than 50 percent of its outstanding voting stock or more than 50 percent of the value of all its outstanding stock. For more information on CFCs, see Mahony, Lee and Randy Miller, "Controlled Foreign Corporations, 2004," *Statistics of Income Bulletin*, Summer 2008, Volume 27, Number 1, pp. 49–110.

[3] To elect I-C DISC status, a domestic corporation must have "qualified export receipts" that constitute at least 95 percent of its gross receipts and must be able to classify at least 95 percent of its assets as "qualified export assets." Qualified export receipts are gross receipts from the sale of qualified export assets and other types of income related to exporting. Qualified export assets consist of property related to exporting. For more information on IC-DISCs, see Holik, Daniel, "Interest-Charge Domestic International Sales Corporations, Tax Years 2004, 2005, 2006," *Statistics of Income Bulletin*, Winter 2010, Volume 29, Number 3, pp. 173–212.

[4] This exclusion allowed businesses to deduct qualifying foreign trade income from their U.S. gross incomes. Qualifying foreign trade income was defined as the greatest of the following income amounts, that when excluded would reduce taxable income by (1) 1.2 percent of foreign trading gross receipts, (2) 15 percent of foreign trade income, or (3) 30 percent of foreign sales and leasing income.

Figure B

Changes in Boycott Requests and Agreements, by Boycotting Country, Tax Years 2007–2008

Country	Number of boycott requests received [1] 2007	Number of boycott requests received [1] 2008	Percentage change in number of requests from 2007 to 2008	Number of boycott agreements received 2007	Number of boycott agreements received 2008	Percentage change in number of agreements from 2007 to 2008
	(1)	(2)	(3)	(4)	(5)	(6)
All countries	**4,823**	**3,716**	**-23.0**	**1,980**	**889**	**-55.1**
Treasury-listed countries	**4,356**	**3,045**	**-30.1**	**1,962**	**852**	**-56.6**
Kuwait	471	221	-53.1	315	67	-78.7
Lebanon	408	400	-2.0	81	94	16.0
Libya	231	330	42.9	39	36	-7.7
Qatar	377	223	-40.8	211	13	-93.8
Saudi Arabia	522	199	-61.9	367	80	-78.2
Syria	282	210	-25.5	158	95	-39.9
United Arab Emirates	1,823	1,326	-27.3	652	442	-32.2
Yemen, Republic of	242	136	-43.8	139	25	-82.0
Non-listed countries	**467**	**671**	**43.7**	**18**	**37**	**105.6**

[1] Requests are undercounted to the extent that many taxpayers do not specify the number of requests they received. This figure counts an unknown number of requests as one request.

Taxpayers who use the international boycott factor reduce their foreign tax credit by the same proportion as the boycott factor. Those who use the specifically attributable method subtract the foreign taxes paid to the boycotting countries with whom they established agreements from the total amount of taxes eligible for credit. Regardless of the method selected, taxpayers may elect to treat the amount of taxes ineligible for the credit under the boycott provisions as a deduction from their U.S. gross incomes for the purpose of calculating their U.S. tax liabilities.

For Tax Year 2007, taxpayers reduced their U.S. foreign tax credit by a total of $70,994 (in constant 2008 dollars) using the international boycott factor and reduced their foreign taxes eligible for the foreign tax credit by $1,468,340 using the specifically attributable method. For 2008, taxpayers lowered their total foreign tax credit by $16,794 and decreased their eligible taxes by $2,010,545. For comparison, the total foreign tax credit for corporations filing for 2008 was more than $100 billion.

Under both the international boycott factor and specifically attributable methods, shareholders of CFCs or IC-DISCs must convert some of the earnings of the CFC or IC-DISC into a "deemed distribution," thereby subjecting the earnings to U.S. tax. Taxpayers who participated in a boycott reported a total increase of $3,750,233 (in constant 2008 dollars) to their taxable incomes from CFCs for Tax Year 2007. By comparison, includable income for all CFCs on corporate returns for Tax Year 2007 (in constant 2008 dollars) was more than $68 billion. Income from CFCs deemed taxable due to boycott participation rose to $7,973,026 for Tax Year 2008.

Summary

For both Tax Years 2007 and 2008, approximately 8 percent of taxpayers reporting operations in countries known to participate in an international boycott received boycott requests. More than a third of the requests received originated from persons in the United Arab Emirates. Less than 3 percent of taxpayers who had operations in countries known to participate in a boycott not sanctioned by the U.S. agreed to participate in such a boycott for both tax years, and only 15 persons lost tax benefits for both years. The total loss of tax benefits remains a very small percentage of the total tax benefits claimed by all filers.

Data Sources and Limitations

Data for the 2007 and 2008 studies were based on the population of Forms 5713, *International Boycott Report*, attached to U.S income tax returns with accounting periods ending between June 30 of the study year and June 30 of the subsequent year.

Table 1. International Boycott Reports: Number of Persons Receiving Requests, Number of Requests Received, and Number of Agreements, by Boycotting Country, Tax Years 2007–2008

Country	Number of U.S. persons receiving requests [1]		Number of boycott requests received [2]		Number of boycott agreements received		Boycott agreements as a percentage of requests received	
	2007	2008	2007	2008	2007	2008	2007	2008
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
All countries	**120**	**138**	**4,823**	**3,716**	**1,980**	**889**	**41.1**	**23.9**
Treasury-listed countries	**100**	**121**	**4,356**	**3,045**	**1,962**	**852**	**45.0**	**28.0**
Kuwait	32	43	471	221	315	67	66.9	30.3
Lebanon	22	21	408	400	81	94	19.9	23.5
Libya	33	30	231	330	39	36	16.9	10.9
Qatar	26	31	377	223	211	13	56.0	5.8
Saudi Arabia	33	33	522	199	367	80	70.3	40.2
Syria	25	16	282	210	158	95	56.0	45.2
United Arab Emirates	70	82	1,823	1,326	652	442	35.8	33.3
Yemen, Republic of	18	14	242	136	139	25	57.4	18.4
Non-listed countries	**53**	**76**	**467**	**671**	**18**	**37**	**3.9**	**5.5**
Bahrain	13	22	18	72	4	14	22.2	19.4
Iraq	11	7	43	45	0	0	0.0	0.0
Pakistan	24	23	159	228	0	0	0.0	0.0
Other non-listed countries	48	70	247	326	14	23	5.6	7.1

[1] Data in these columns may not add to totals because a person could have received requests from more than one country.
[2] The number of requests are undercounted to the extent that many taxpayers do not specify the number of requests they received. This table counts an unknown number of requests as one request.

Table 2. International Boycott Reports: Lost Tax Benefits, by Type and Method of Computation, 1998–2008

[Money amounts are in whole dollars]

Method and calendar or tax year [1]	Reduction of foreign taxes or foreign tax credit	Increase of subpart F income	Denial of IC-DISC benefits	Denial of foreign sales corporation benefits	Reduction of extraterritorial income exclusion [2]
	(1)	(2)	(3)	(4)	(5)
Boycott factor method:					
1998	0	0	0	5,869	0
1999	0	0	0	0	0
2000	0	7,453	0	0	0
2001	0	0	0	0	0
2002	6,754	399,389	0	0	311,659
2003	4,706	41,498	0	0	339,796
2004	11,407	216,923	0	0	603,560
2005	8,335	251,983	0	0	1,656,910
2006	6,066,332	244,607	0	0	588,384
2007	70,994	100,536	0	0	190,786
2008	16,794	53,038	0	0	6,871
Specifically attributable taxes and income method:					
1998	0	934,716	0	432,390	0
1999	38,954	1,014,279	0	0	0
2000	25,604	1,944,337	0	0	0
2001	10,460	2,355,337	0	0	0
2002	827,346	6,142,273	0	0	0
2003	622,765	2,074,173	0	0	0
2004	739,500	3,425,808	0	0	0
2005	900,154	3,240,143	0	0	0
2006	782,905	12,501,384	0	0	0
2007	1,468,340	3,649,697	d	0	0
2008	2,010,545	7,919,988	d	0	0

d—Data eliminated to avoid disclosure of information about specific taxpayers.

[1] Calendar year for 1998-2006, tax year for 2007-2008. Tax years run from June 30 to July 1 of the following year. Data for the gap between Calendar Year 2006 and Tax Year 2007 is not shown in order to avoid disclosure.

[2] Extraterritorial exclusion was added to the tax code in 2000 and repealed with some exceptions in 2004. Further repeal ended the exceptions for tax years beginning after May 18, 2006.

NOTE: For comparability, amounts have been adjusted for inflation to 2008 constant dollars.