

International Boycott Reports, 2005 and 2006

by Melissa Costa

For Calendar Year 2006, 112 “U.S. persons” reported receiving almost 2,300 requests to participate in boycotts unsanctioned by the United States.¹ Most of these (91 percent) were requests from Arab League Countries to participate in some form of a boycott against Israel. While the number of U.S. persons receiving requests decreased by only three persons from 2005, the number of requests dropped by nearly 40 percent. About 30 percent of those receiving requests agreed to participate in a boycott. Less than 3 percent of all taxpayers filing Form 5713, however, reported tax consequences.

The Antiboycott Laws

The Arab League organization was founded in 1944 and currently contains 23 countries and entities. After Israel became independent in 1948, the Arab League instituted a formalized boycott of the state of Israel and anyone who does business with Israel.

In the 1970s, the United States Congress enacted laws to combat this boycott.² One law, the 1977 amendments to the Export Administration Act of 1969, requires U.S. persons to report quarterly to the Commerce Department the requests they have received to participate in, support, or further a prohibited boycott. Those U.S. persons who agree to participate in such boycotts are subject to criminal and civil penalties.

The other antiboycott law is the Ribicoff Amendment to the Tax Reform Act of 1976 (TRA76). It requires all U.S. taxpayers and their related persons to report operations in, with, or related to, boycotting countries or their nationals to the Internal Revenue Service. Operations include any business or commercial transactions, even if they do not generate income. Per Internal Revenue Code section 999(a), taxpayers report these operations on Form 5713, *International Boycott Report*, filed annually with

their Federal income tax returns. Although Congress intended these laws to dissuade boycotts of Israel, they cover any boycott not sanctioned by the United States.

Operations

For Calendar Year 2005, taxpayers filed 1,402 Forms 5713, while 1,412 forms were filed for 2006. Corporations filed approximately 90 percent of Forms 5713 for both years, while partnerships accounted for roughly 8 percent of the total. Trusts, estates, and individuals filed most of the remainder. The majority of Forms 5713 were filed to report the taxpayer’s operations in boycotting countries. For both years, 99 percent of taxpayers reported operations in Arab League nations known to participate in the boycott of Israel. Taxpayers listed Saudi Arabia and the United Arab Emirates more frequently than any other countries. Less than 3 percent of filers reported operations in countries known to participate in an unsanctioned boycott of a country other than Israel. Of the latter, the most frequently listed boycotting country for both years was Pakistan.³

Types of Boycotts

There are three tiers to the Arab League’s boycott of Israel. The primary boycott bans the importation of goods and services originating in Israel into member countries. Because the United States does not wish to infringe on the right of any country to choose its own trading partners, the antiboycott laws do not target such boycotts. They are directed instead against the secondary and tertiary boycotts. The secondary boycott bans entities in member states from doing any business with any entity that does business with Israel. A tertiary boycott bans entities in member countries from doing business with companies or individuals who have business with firms on the Arab League blacklist.

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

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¹ As defined in 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 its beneficiaries.

² Doernberg, Richard L. (1999), *International Taxation*, West Group, St. Paul, MN, p. 413.

³ Taxpayers do not report the country that their countries of operation were boycotting when it is not Israel.

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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 which 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 which 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].⁴

For both years, around 8 percent of filers reported receiving requests. Figure A includes the number of persons receiving requests and the number of requests received, by type. Most of the boycott requests for both 2005 and 2006 were either type 1 or type 5 requests.

Participation of Listed and Nonlisted Countries

Actual participation with the Arab League boycott has always varied greatly among its member states and with the ups and downs of the Israeli/Palestinian conflict.⁵ Over time, the number of persons receiving requests has remained relatively constant, but the number of requests received has fluctuated considerably. See Figure B.

Figure A

Number of Persons Receiving Boycott Requests and Number of Requests Received, by Type of Request, 2005-2006

Type of boycott request	Number of persons receiving boycott requests [1]		Number of boycott requests received [2]	
	2005 (1)	2006 (2)	2005 (3)	2006 (4)
Total	115	112	3,703	2,270
Type 1	64	67	1,513	1,143
Type 2	15	7	556	41
Type 3	18	13	240	47
Type 4	12	5	222	53
Type 5	74	59	1,172	986

[1] A person could receive more than one type of request.

[2] Many persons fail to report the total number of requests.

NOTE: This figure counts an unknown number of requests as one request.

Some nations, including Algeria, Egypt, Jordan, Mauritania, Morocco, the Palestinian Authority, and Tunisia, either formally ended the boycott long ago or never enforced it.⁶ Some, like Kuwait and Qatar, support only primary boycotts, and others continue to enforce all three levels of boycott activity. The U.S. Department of Treasury maintains a list, published quarterly, of those countries known to participate in unsanctioned boycotts.

For 2005, that list included Bahrain, Iraq, Kuwait, Lebanon, Libya, Oman, Qatar, Saudi Arabia, Syria, the United Arab Emirates, and Yemen. Bahrain and Oman stated they would not comply with the boycott of Israel during negotiations for their respective Free Trade Agreements with the United States and were removed from the Treasury List in 2006. Listed countries were responsible for 89 percent of the total requests for 2005 and 82 percent for 2006.

Figure C provides a comparison of the number of requests received, by selected country, for 2005 and 2006. Requests received from Lebanon experienced the most noticeable decline, with a fall of 69 percent, followed by the United Arab Emirates, with a fall of 62 percent. (The United Arab Emirates began negotiating for a free trade agreement with the

⁴ For a more detailed discussion of activities not permitted under the boycott provisions, see Doenberg, pp. 414-420.

⁵ Weiss, Michael, "Arab League Boycott of Israel," CRS Report for Congress, August 27, 2008, <http://www.usembassy.it/pdf/other/RL33961.pdf>.

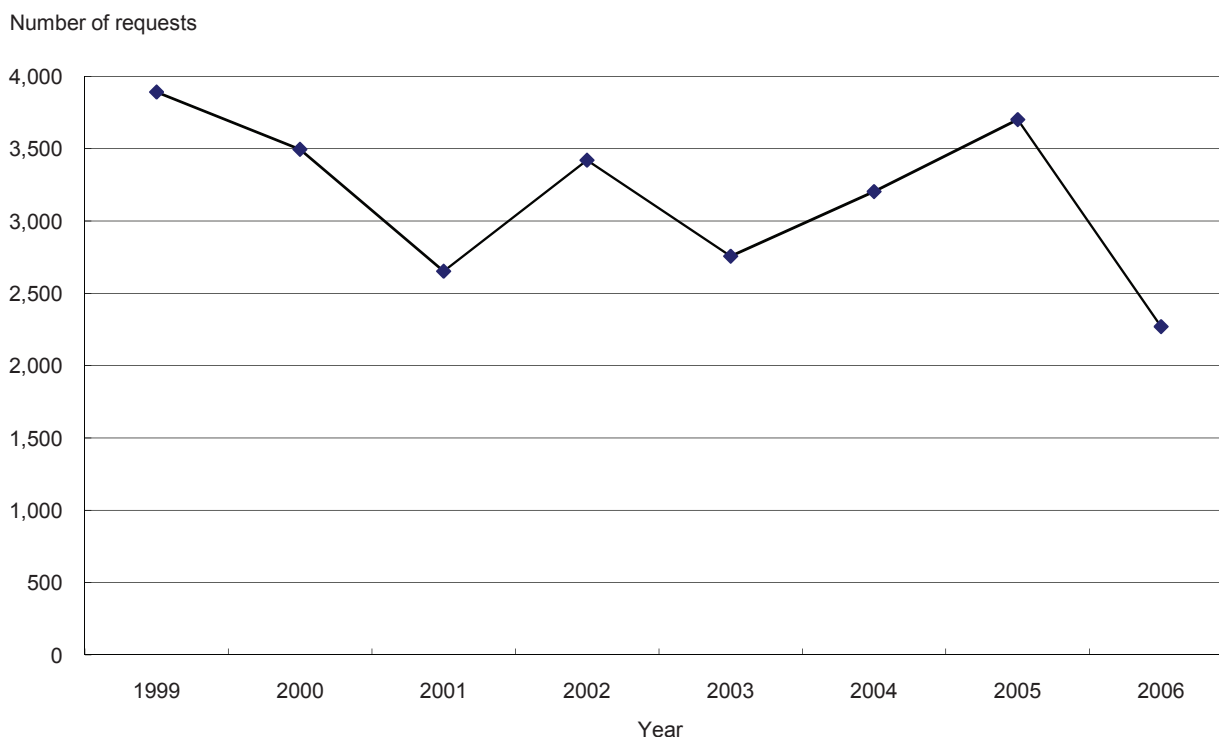
⁶ Ibid.

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Figure B

Number of Boycott Requests Received, 1999-2006



United States in 2005). Despite the dramatic drop in requests, the United Arab Emirates still accounted for the largest percentage of requests for both years, comprising 37 percent of the total for 2005 and 20 percent for 2006.

Approximately 18 percent of requests for 2006 originated from nonlisted countries, up from 11 percent for 2005. Requests from Pakistan comprised about one-quarter of the nonlisted requests for both 2005 and 2006. In 2006, another quarter of the nonlisted requests came from Oman. Nevertheless, overall requests from Oman fell by two-thirds, from 304 for 2005 to 104 for 2006. Non-Arab League countries accounted for approximately 6 percent of the total requests for 2005 and 9 percent for 2006.

Boycott Agreements

Approximately 2 percent of the filers in both study years agreed to participate in an unsanctioned boycott, 31 in 2005 and 32 in 2006. Table 1 provides the

number of persons receiving requests, the number of persons agreeing to participate, and the number of requests and agreements, by Treasury-listed country. Overall, boycott agreements fell almost 15 percent, from 494 in 2005 to 421 in 2006. In 2005, taxpayers agreed to participate with about 13 percent of the requests they received, while they agreed to about 19 percent of the requests received in 2006. They were most likely to comply with requests from Saudi Arabia, agreeing to 30 percent of its requests in 2005 and 55 percent in 2006.

Tax Penalties

U.S. taxpayers who participated in the boycotts listed may lose their right to claim certain tax benefits provided by U.S. tax law. For 2005 and 2006, taxpayers lost portions of the foreign tax credit, the exclusion of extraterritorial income, and the tax deferral available to U.S. shareholders of controlled foreign corporations (CFCs).^{7, 8} Not all taxpayers, of course, were

⁷ 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, that when excluded would reduce taxable income by (1) 1.2 percent of foreign trading gross receipts, or (2) 15 percent of foreign trade income, or (3) 30 percent of foreign sales and leasing income.

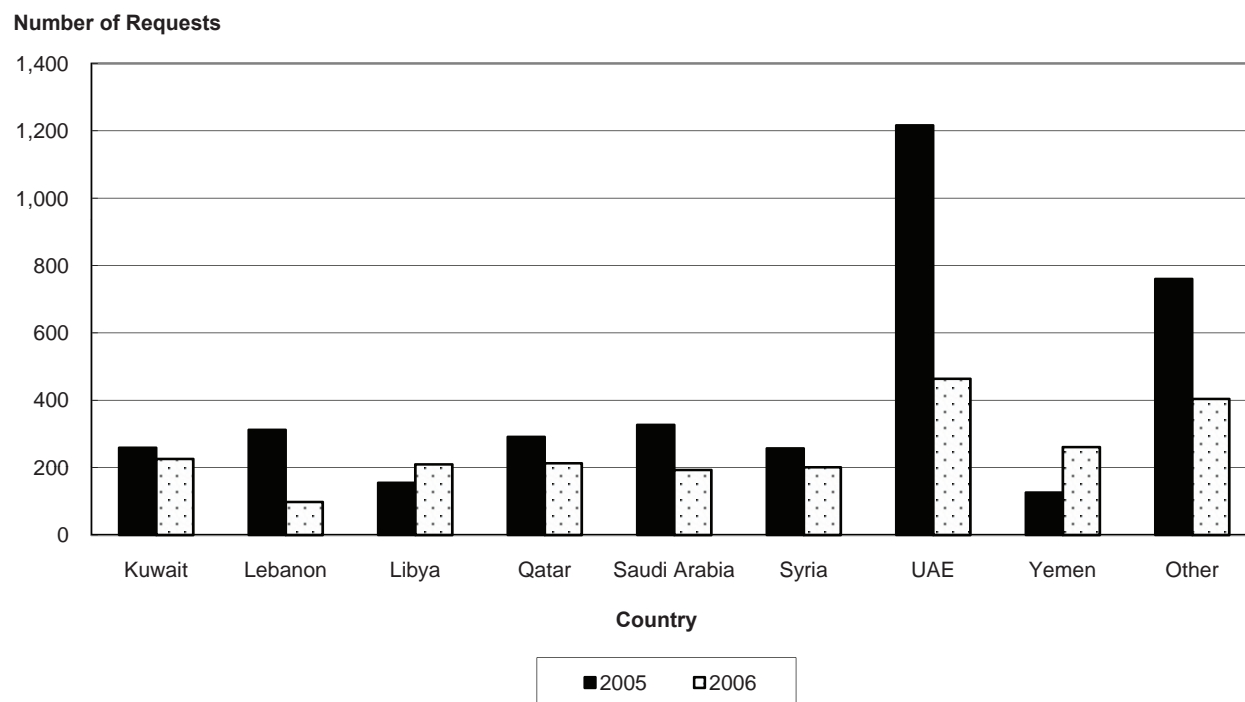
⁸ No taxpayer has reported a loss of tax deferral of Interest Charge Domestic International Sales Corporation or Foreign Sales Corporation benefits in recent years. Congress repealed the FSC provisions in November 2000. Exceptions that permitted certain FSCs to continue were repealed in May 2006.

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Figure C

Number of Boycott Requests Received, by Requesting Country, 2005-2006



eligible for the tax benefits subject to consequences. Of those taxpayers agreeing to participate, 19 lost tax benefits in 2005, and 9 lost tax benefits in 2006.

Taxpayers who had operations in a boycotting country were required to reduce foreign trade income qualifying for extraterritorial income exclusion, even if they did not receive any requests to participate in a boycott. There were 28 taxpayers for 2005 who lost part of their extraterritorial income exclusion although they did not participate in a boycott and 24 for 2006.

Taxpayers compute the loss of 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 exclusion is reduced by the same proportion as the international boycott factor. In all, taxpayers reduced the exclusion by \$1,551,456 in 2005 (in constant 2006 dollars) and \$550,936 in 2006. (Table 2 shows

the amount of tax consequences reported for the past 11 years, in constant 2006 dollars, by method of computation.)⁹

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 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 tax benefits.

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 foreign taxes paid to boycotting countries with whom they established agreements from the amount of taxes eligible for credit.

Regardless of the method selected, taxpayers may still deduct taxes ineligible for the credit under

⁹ In the American Jobs Act of 2004, Congress enacted a gradual repeal of the extraterritorial income exclusion. Taxpayers could claim 80 percent of their eligible exclusion for 2005 and 60 percent for 2006. No exclusion can be claimed for tax years after 2006.

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boycott provisions from their U.S. gross incomes. For 2005, taxpayers reduced their foreign tax credit by a total of \$7,805 (in constant 2006 dollars) using the first method and reduced their eligible foreign taxes by \$842,864 using the second method. For 2006, taxpayers lowered their total foreign tax credit by \$5,680,239 and decreased their total eligible foreign taxes by \$733,077.

Although the reduction in foreign tax credit due to boycott participation rose substantially for 2006, the boycott reduction remains a very small amount of the total foreign tax credit claimed by all U.S. persons. For comparison, the foreign tax credit for corporations filing for 2006 was over \$82 billion.

A CFC is any foreign corporation in which U.S. shareholders own directly, indirectly, or constructively more than 50 percent of either the total combined voting power or total value of all stock on any day of the taxable year of the corporation. Generally, earn-

ings from a CFC are not subject to tax in the United States until they are distributed to the U.S. parent.

Under both the international boycott factor and specifically attributable methods, shareholders of CFCs must convert some of their CFCs' undistributed incomes into a "deemed distribution," thereby subjecting the distribution to U.S. tax. Taxpayers who participated in a boycott reported a total increase of \$3,269,868 (in constant 2006 dollars) to their taxable incomes from CFCs for 2005 and \$14,644,844 for 2006.) As with the reduction of the foreign tax credit, the overall increase in taxable income from CFCs due to boycott participation is very small compared to total CFC income for all taxpayers.

Data Sources and Limitations

Data for the 2005 and 2006 studies were based on the population of Forms 5713, *International Boycott Report*, attached to U.S. income tax returns with accounting periods ending in those years.

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Table 1. International Boycott Reports: Number of Persons Receiving Requests, Number of Requests Received, and Number of Agreements, by Boycotting Country, 2005-2006

Country	Number of persons receiving requests [1]		Number of boycott requests received [2]		Number of persons with agreements [1]		Number of boycott agreements		Boycott agreements as a percentage of requests received	
	2005 (1)	2006 (2)	2005 (3)	2006 (4)	2005 (5)	2006 (6)	2005 (7)	2006 (8)	2005 (9)	2006 (10)
All countries	115	112	3,703	2,270	31	32	494	421	13.3	18.5
Treasury-listed countries	106	90	3,290	1,866	24	27	480	381	14.6	20.4
Bahrain	20	N/A	43	N/A	6	N/A	9	N/A	20.9	N/A
Kuwait	30	31	259	226	10	15	36	48	13.9	21.2
Lebanon	29	29	312	98	11	10	91	31	29.2	31.6
Libya	36	30	155	210	5	9	6	25	3.9	11.9
Oman	22	N/A	304	N/A	3	N/A	5	N/A	1.6	N/A
Qatar	34	22	291	213	3	**	11	4	3.8	1.9
Saudi Arabia	28	23	327	193	10	8	99	107	30.3	55.4
Syria	26	19	257	201	10	7	39	65	15.2	32.3
United Arab Emirates	64	58	1,216	464	17	18	174	81	14.3	17.5
Yemen, Republic of	9	14	126	261	4	3	10	20	7.9	7.7
Nonlisted countries	38	54	413	404	6	12	14	40	3.4	9.9

N/A—not applicable. Bahrain and Oman were not on the Treasury List for 2006.

**Data deleted to avoid disclosure of information about specific taxpayers. However, data are included in the appropriate totals.

[1] Data in these columns do not add to totals because persons could have received requests from, or made agreements with, 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.

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Table 2. International Boycott Reports: Lost Tax Benefits, by Method of Computation, 1997-2006

[Money amounts are in whole dollars]

Method and calendar year	Reduction of foreign taxes or foreign tax credit [1]	Increase of Subpart F income [1]	Denial of Foreign Sales Corporation benefits [1]	Reduction of extraterritorial income exclusion [1, 2]
	(1)	(2)	(3)	(4)
Boycott factor method				
1997	29,208	282,026	0	0
1998	0	0	5,495	0
1999	0	0	0	0
2000	0	6,979	0	0
2001	0	0	0	0
2002	6,324	373,970	0	291,824
2003	4,407	38,857	0	318,170
2004	10,681	203,117	0	565,146
2005	7,805	235,945	0	1,551,456
2006	5,680,239	229,039	0	550,936
Specifically attributable taxes and income method				
1997	146	1,868,514	368,133	0
1998	0	875,226	534,784	0
1999	36,474	949,725	0	0
2000	23,974	1,820,590	0	0
2001	**	2,205,431	0	0
2002	774,690	5,751,347	0	0
2003	583,129	1,942,162	0	0
2004	692,435	3,207,772	0	0
2005	842,864	3,033,923	0	0
2006	733,077	11,705,731	0	0

**Data deleted to avoid disclosure of information about specific taxpayers.

[1] Money amounts have been adjusted for inflation to constant 2006 dollars using the Consumer Price Index.

[2] The reduction of the extraterritorial income exclusion was added to the November 2001 Form 5713 revision.