October 15, 2024

The Honorable Jason Smith
Chairman
House Ways and Means Committee
U.S. House of Representatives
Washington, DC 20515

The Honorable Mike Kelly
Chairman
Tax Subcommittee
U.S. House of Representatives
Washington, DC 20515

The Honorable Kevin Hern
Chairman
Global Competitiveness Tax Team
U.S. House of Representatives
Washington, DC 20515

The Honorable Blake Moore
Vice Chairman
Global Competitiveness Tax Team
U.S. House of Representatives
Washington, DC 20515

By email: RepublicanTaxTeams@mail.house.gov

Re: Tax Teams Comment on Global Competitiveness

Dear Chairmen Smith, Kelly, and Hern, and Vice Chairman Moore,

The Financial Accountability and Corporate Transparency, or FACT Coalition is a nonpartisan alliance of more than 100 business, civil society, and labor organizations working toward a fair tax system that addresses the challenges of a global economy and promotes policies to combat the harmful impacts of corrupt financial practices.[1]

FACT commends the international reform provisions of the 2017 Tax Cuts and Jobs Act (TCJA) as an important step in the right direction, and an example of U.S. thought leadership on international tax policy. The framework has served as a model for our allies to adopt a global version of the minimum tax, now in force in dozens of countries.

Congress now has an opportunity to revisit and strengthen these provisions to ensure a level playing field for all American businesses, including small domestic businesses, while raising significant additional revenues needed to address other fiscal priorities.

[1] To learn more about the FACT Coalition and its members, see https://thefactcoalition.org/about-us. The views presented in this comment are not necessarily endorsed by every member of the Coalition.

U.S. Economy and U.S. Tax Policies Are Already Competitive

The United States is a proud home to many of the world's most competitive and successful companies. Their success is neither because, nor in spite, of our tax policy, but first and foremost thanks to the extraordinary ingenuity and hard work of American entrepreneurs and workers. Tax considerations can play a role in, but do not ultimately determine, international business competitiveness. To the extent that taxes are relevant to global competitiveness, that relevance goes beyond the headline statutory rates. Congress should instead consider the effective tax rates that companies actually pay.

By that measure, the U.S. has a far lower effective marginal tax rate on normal corporations than its main global competitors (see table below). A Reuters analysis has confirmed that the average effective tax rate for U.S. corporations is below the average for their foreign counterparts and that this would continue to be the case if the headline rate were raised to 28 percent. **Consequently, there is no reason to consider further reductions to the corporate statutory rate; and conversely, a rate increase would not necessarily make U.S. companies any less competitive.** A corporate rate increase also would not be too costly for U.S. workers: according to an estimate by the Alliance for Competitive Taxation and the Tax Foundation, increasing the corporate tax rate to 28 percent would reduce average wages by $5-11 per week.

Effective tax rates - Corporate tax statistics

Measure: Effective marginal tax rate ● ***Scenario:*** Fixed interest and inflation rates ● ***Tax type:*** Composite

Combined unit of measure: Percentage of taxable income

Time period		2019	2020	2021	2022	2023
Reference area						
Canada		14.08	13.75	17.04	13.75	13.79
France		25.24	22.64	17.51	15.38	15.38
Germany		27.68	24.92	9.18	9.18	11.01
Japan		29.26	29.26	29.26	29.26	29.26
Korea		24.83	24.83	24.83	23.26	22.11
United Kingdom		8.82	7.38	-27.28	-27.28	11.51
United States		3.75	3.72	3.71	3.73	7.03
China (People's Republic of)		14.22	14.22	14.22	15.59	15.59

Our Tax Laws Should Prioritize American Workers and Small Businesses

As Congress considers business competitiveness, it should take into account not only large multinational corporations but also the interests of American workers and small businesses, which form the backbone of the U.S. economy. Purely domestic companies account for the vast majority – more than 80 percent – of U.S. jobs, and are critical for economic stability and job creation.

Right now, U.S. tax policy puts small businesses on the back foot, and they know it. According to a recent poll by Small Business Majority, a FACT Coalition member, 82 percent of small business owners feel disadvantaged compared to large corporations under the current tax system. Poll after

poll shows that an overwhelming majority of Americans agree that big corporations pay too little in taxes. They believe that large corporations are exploiting loopholes to avoid taxes that small businesses have to pay, particularly by shifting jobs and profits overseas.

Likewise, tax policies that benefit multinational corporations and disadvantage workers can impact national confidence in ways that undermine U.S. geopolitical competitiveness. During a recent summit on conservative grand strategy, former chair of the U.S.-China Economic and Security Review Commission Alex Wong made the point that work without clear economic benefit can damage American social cohesion in ways easily exploited by U.S. adversaries like China. He noted, "When you have employment displacement, when you have people unable to find the same meaning in work that they did before: that does diminish social cohesion, and it does therefore diminish an element of our national power." Our tax policies should not weaken our position vis-a-vis our adversaries, and should instead encourage Americans to see themselves as stakeholders in our society.

International Tax Reforms Can Pay for Real Policy Priorities

Looking ahead, we face long-term fiscal challenges. The looming expiration of individual tax cuts in 2025 could lead to either tax increases for many Americans or further strain on the federal budget if these cuts are extended without offsetting revenue measures. As Congress evaluates potential revenue-raising options to address these challenges, **FACT Coalition strongly recommends that international tax reforms be prioritized as a way to generate much-needed revenue while also addressing some of the shortcomings in the current U.S. international tax framework.**

Policy Recommendations

1. **End America-last tax policy by harmonizing the rates on foreign and domestic income, to prevent offshoring of American profits and jobs**

The international provisions of the 2017 tax law were intended to curb profit shifting, but they have instead produced mixed results. U.S. multinationals continue to report around half of their total profits in low-tax jurisdictions as of 2020, according to official statistics from the Bureau of Economic Advisors and companies' own tax reporting to the IRS. In particular, U.S. pharmaceutical companies report much of their considerable profit offshore, despite having significant U.S. sales and high prices in the domestic market. Our tax policy should reduce incentives for the products of American innovation – like life-saving medications that generate hundreds of billions in sales to U.S. consumers every year – to be manufactured offshore.

Of course, domestic small and midsize businesses do not have access to complex international tax schemes, nor do even relatively large, wholly domestic businesses like CVS Health. As CVS Health said in a statement for the record to the Senate Budget Committee, "Retailers are generally subject to the highest level of federal corporate tax…Yet not all retailers, including companies

providing retail pharmacy services, pay the top rate due to their international structures."[2] **Congress must act to reclaim the corporate tax base that rightfully belongs in the U.S., and to level the playing field for domestic businesses with regard to their multinational competitors**.

The Global Intangible Low-Taxed Income regime (GILTI) offers a good starting point in this regard, as a groundbreaking global minimum tax intended to end the indefinite offshore deferral of U.S. profits that predated the TCJA. **However, while GILTI was intended to stop offshoring, it has created incentives that reward it: GILTI's discounted tax rate for foreign income compared to domestic income perversely encourages U.S. companies to locate production abroad, potentially leading to job losses and reduced domestic manufacturing capacity.**

To help GILTI accomplish its intended goal, the Ways and Means Committee should consider changes to:

> (1) Equalize the domestic and GILTI rates;
>
> (2) Eliminate the offshoring incentive offered by the exemption of the first 10 percent return on foreign tangible assets from U.S. taxation; and
>
> (3) End the loophole that allows for blending of income from tax havens and high-tax foreign jurisdictions.

These improvements would not place domestic multinationals at any meaningful disadvantage or impose significant compliance costs. U.S. and foreign companies alike are already performing similar analyses for purposes of complying with tax laws in other countries that have adopted their own versions of GILTI, but at a higher rate and calculated on a country-by-country basis. Conversely, if Congress fails to act to improve GILTI as outlined above, there would be no net benefit for U.S. companies, as they would be exposed to top-up taxes in dozens of countries around the world that have adopted the undertaxed profits rule (UTPR). **This loss of U.S. revenues to other countries is entirely avoidable if Congress acts promptly, as the effective date of the UTPR has been suspended until 2026, coinciding with TCJA expiration.**

As a fallback, Congress could at least move to counter incentives for companies to engage in the most egregious forms of international tax planning, including so-called "roundtripping," whereby intellectual property developed in the U.S. is first exported to a low-tax foreign jurisdiction, and then used to manufacture goods that are sold back into U.S. markets. According to George Callas, one of the architects of the TCJA, "ending this practice would make the code more neutral between Main Street businesses and global corporations." Proposals to address round-tripping include taxing GILTI derived from sales to U.S. markets as domestic income, at the full statutory corporate rate. Ultimately, however, the incentive to roundtrip – like most offshoring incentives – would be best addressed by simply harmonizing the GILTI rate with the statutory domestic rate, as recommended above.

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[2] CVS Health, Statement for the Record, Senate Budget Committee Hearing, ""The Great Tax Escape: Closing Corporate Loopholes that Reward Offshoring Jobs and Profits," January 17, 2024. p. 104 https://www.congress.gov/118/chrg/CHRG-118shrg54922/CHRG-118shrg54922.pdf

2. Repeal wasteful tax handouts for special interests

Tax breaks that favor specific sectors are economically inefficient and fiscally irresponsible. In the context of U.S. international corporate tax, two targeted tax breaks in the TCJA stand out as particularly harmful: the Foreign-Derived Intangible Income (FDII) deduction that predominantly benefits Big Tech companies, and the Foreign Oil and Gas Extraction Income (FOGEI) exclusion, which favors oil and gas extraction abroad.

FDII is a category of income defined as excess profits derived from sales by U.S. firms to foreign markets. Income that qualifies as FDII is subject to a 37.5 percent deduction for tax purposes, resulting in an effective tax rate of 13.125 percent. The harms of FDII are numerous:

- **An expensive handout to a small handful of firms**: The FDII deduction provides a massive tax break for companies already enjoying above-average returns on export sales. FDII costs the U.S. tens of billions of dollars every year, while meaningfully benefiting only a small handful of the largest firms, particularly in the tech sector.
- **Perverse incentives to offshore American manufacturing**: Further, while FDII was originally conceived as "a carrot" for U.S. multinationals to repatriate valuable intellectual property and other intangible assets, there is no evidence that the policy was a substantial driver of repatriation[3], let alone that it spurred domestic innovation or job creation. What is clear is that this handout perversely incentivizes U.S. companies, especially Big Tech firms, to shift valuable assets and jobs overseas. This is because FDII, like GILTI, is defined as qualifying income above a fixed rate of return on tangible assets, like factories and machinery. To maximize their FDII benefit, U.S. multinationals are encouraged to minimize the value of their real U.S. operations, including production plants and offices that create good paying American jobs.
- **Disadvantages for American entrepreneurs and consumers**: In addition to harming American workers, FDII also comes at the expense of Main Street businesses (that are not exporters and therefore cannot claim the deduction), and American consumers (by incentivizing foreign over domestic sales).
- **Massive revenue losses**: The fiscal cost of FDII has been so large that it has negated initial expectations that the international reform provisions of TCJA would help to offset the overall revenue losses from the corporate rate cut and the shift to a territorial system. While FDII was initially projected to cost $63 billion, a recent review of public company filings shows that just 15 corporate taxpayers claimed more than $50 billion in FDII benefit since the passage of the TCJA.

By repealing FDII, Congress now has an opportunity to raise significant revenues – up to $224 billion over ten years according to the JCT – while removing these harmful incentives and building a more neutral tax system that does not favor offshoring.

Another example of a wasteful handout that is against U.S. interests is a tax exemption for foreign oil and gas extraction. Such preferential treatment is not awarded to any other specific

[3] Research by the Penn-Wharton Budget Model team suggests that changes in Irish law played a significant role.

category of income or sector under GILTI. The policy does nothing for our energy security, and arguably undermines it by favoring drilling abroad, subsidized by our government. Such an America-last approach is indefensible, particularly when we know that big U.S. oil and gas companies are paying far more in taxes to foreign governments than here at home. Tens of billions could be saved over the next decade by repealing this baseless carveout.

3. **Hold foreign competitors accountable by adopting the undertaxed profits rule**

We urge Congress to consider adopting the UTPR as a way to pay for other reforms while also leveling the playing field with our key global competitors, in particular China. The rise of China's digital giants (Baidu, Alibaba, Tencent, Xiaomi) poses a challenge for national security as well as economic policy. International tax reform can be a part of the solution. While others advocate for a further erosion of U.S. revenues to address tax competition with China, such a trade-off is unnecessary. A better and more fiscally prudent policy response is to raise U.S. revenue from Chinese companies. To the extent that Chinese companies use tax havens to reduce their tax liabilities, as research suggests, Congress can counter and raise U.S. revenue by imposing a top-up tax on any Chinese or other foreign companies paying less than the globally agreed 15 percent minimum rate. Such reform is estimated to bring in tens of billions of dollars.

4. **Protect American investors by strengthening tax transparency**

In addition to direct revenue measures, Congress should also consider other ways to change the tax behavior of large multinational taxpayers. In particular, improving tax transparency will protect American investors from significant material tax risks that companies in their portfolios increasingly face.

Tax risks are most acute from cross-border tax structures, as demonstrated by large transfer pricing disputes such as the potential $16 billion tax liability for Coca-Cola and Microsoft's $29 billion tax bill. With improved tax transparency, such risky tax structures might have been deterred. To this end, 87 investors with more than $2.3 trillion in assets have recently petitioned the U.S. Securities and Exchange Commission to require public companies to disclose country-level data, including profits, employee headcounts, and taxes paid. As other key markets, including the European Union and Australia, advance corporate tax transparency measures, the U.S. should keep pace to ensure that American investors and businesses do not face increased tax and compliance risks abroad.

Conclusion

The upcoming expiration of many provisions of the TCJA provides Congress with a generational opportunity to address long-standing deficiencies in the tax code. Perhaps nowhere is this more true than in the realm of international corporate tax. Pre-2017, there was widespread bipartisan consensus that the treatment of the foreign income of U.S. multinationals needlessly locked profits offshore, didn't raise adequate revenues, and disadvantaged Main Street businesses.

Congress must use the tools provided by the 2017 tax reform to once and for all remove the incentive for U.S. multinationals to ship jobs and profits offshore, raise much-needed revenues to pay for policy priorities and reduce deficits, and level the playing field for domestic businesses and workers. The policy recommendations made above would, if adopted, represent a transformational step toward achieving these goals.

Thank you for the opportunity to comment.

Sincerely,

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