The Honorable Max Baucus  
Chairman  
Committee on Finance  
United States Senate  
219 Dirksen Senate Office Building  
Washington, D.C. 20510

The Honorable Orrin Hatch  
Ranking Member  
Committee on Finance  
United States Senate  
219 Dirksen Senate Office Building  
Washington, D.C. 20510

The Honorable Dave Camp  
Chairman  
Committee on Ways and Means  
United States House of Representatives  
1102 Longworth House Office Building  
Washington, D.C. 20515

The Honorable Sander Levin  
Ranking Member  
Committee on Ways and Means  
United States House of Representatives  
1102 Longworth House Office Building  
Washington, D.C. 20515

January 22, 2014

Dear Chairmen and Ranking Members,

We, the undersigned organizations ask that you refuse to extend two recently expired tax breaks that subsidize highly profitable corporations at the expense of ordinary Americans. Congress has routinely kept egregious and expensive corporate tax breaks in place for companies that shift profits and jobs offshore. These corporate tax breaks are not free. And taxpayers have routinely had to shoulder their cost through cuts to programs or higher taxes.

Two rules in the tax code that allow U.S. multinational corporations to park their earnings offshore and avoid paying tax on them expired at the end of 2013. These rules are known as the “active financing exception” and the “controlled foreign corporation (CFC) look-through rule.” If Congress refuses to extend these expired provisions, some U.S. companies will have much less incentive to send their profits and jobs offshore.

A U.S. multinational corporation generally cannot defer paying tax on the income of its foreign subsidiaries that is considered “passive” (even if it is not repatriated), such as interest, dividends, rents, and royalties. Congress has determined that deferral is not appropriate for this type of income because it is highly fungible and the entities that earn it are very mobile.

The “active financing exception” is an exception to this general rule that passive income earned by a foreign subsidiary must be recognized for tax purposes when earned. The “active financing exception” was repealed in the 1986 Tax Reform Act but reinstated in 1997 as a “temporary” measure after fierce lobbying by corporations. In 1998 it was expanded to include foreign captive insurance subsidiaries. These provisions have been extended every year since 1998, usually for only one or two years at a time.

The exception creates two harmful incentives. First it encourages American corporations to lend, invest and create jobs in foreign countries rather than in the U.S., because it provides a break from U.S. taxes on financial income generated offshore. Second, it encourages American corporations to engage in “financial engineering” to make their U.S. profits appear to be generated by a “captive” foreign financing subsidiary or other type of offshore subsidiaries, in order to avoid U.S. taxes.

The active financing exception is one of the primary reasons General Electric has paid, on average,
only a 1.8% effective U.S. federal income tax rate over the past ten years. G.E.’s federal tax bill is
lowered dramatically with the use of the active financing exception provision by its subsidiary, G.E.
Capital, which Forbes noted has an “uncanny ability to lose lots of money in the U.S. and make lots
of money overseas.”

In addition, this exception allows large U.S.-based financial institutions to pay low effective rates.
As a group, the financial industry has one of the lowest effective rates of all corporations,
averaging only 15.5% for the years 2008-2010.

The last two-year extension of the active financing exception was estimated by the Joint
Committee on Taxation to have cost taxpayers $11.2 billion.

Another exception to the general rules requiring taxation of passive income, the CFC look-
through rule, allows a U.S. multinational corporation to defer tax on passive income, such as royalties,
earned by a foreign subsidiary (a “controlled foreign corporation” or “CFC”) if it is paid to that
subsidiary by a related CFC and can be traced to the active income of the payer CFC. (The check-
the-box regulations allow similar tax planning with non-corporate entities.)

The CFC look-through rule allows multinationals to create transactions purely for “earnings
stripping” – to create dividends, interest, rents, and royalties to strip active income out of high-tax
countries and move it into low-tax or no-tax countries without incurring any U.S. tax liability (or
any tax liability anywhere).

The last two-year extension of the CFC look-through rule was estimated by the Joint Committee on
Taxation to have cost taxpayers $1.5 billion.

In summary, these rules allow U.S. multinationals to create “stateless income”: income that is
treated, for tax purposes, as earned in a (low- or no-tax) country instead of in the country where
the employees and assets are located.

Transactions enabled by these rules are a reason for the low effective tax rates of companies with
highly-valued intangibles. High-tech companies like Apple and Google and pharmaceutical
companies like Pfizer and Forest Laboratories are easily able to shift income from the U.S. (or
other countries with a meaningful corporate income tax) to low- or no-tax countries.

Public outcry against tax loopholes for large corporations has never been louder. News reports
about the way companies such as G.E., Apple, Pfizer and Facebook are able to legally game the
system continue to outrage your constituents and the country as a whole. These tax giveaways
come at the expense of critical programs and the fiscal health of our government. Congress needs
to stand up for ordinary taxpayers and stop giving these corporations a free pass.

Sincerely,

The Financial Accountability and Corporate Transparency (FACT) Coalition

Alliance for a Just Society

American Federation of Labor and Congress of Industrial Organizations (AFL-CIO)

Americans for Tax Fairness

Campaign for America’s Future
Center for Effective Government
Citizens for Tax Justice
Dominican Sisters of Hope
Fair Share
JPIC Ministry, Missionary Oblates
Jubilee USA Network
Main Street Alliance
Maryknoll Catholic Foreign Mission Society of America
National Peoples Action
National Priorities Project
New Rules for Global Finance
Public Citizen
Sisters of Charity Federation
Sisters of the Good Shepherd
Sisters of St Dominic of Caldwell NJ
School Sisters of Notre Dame Cooperative Investment Fund
Sisters of Notre Dame de Namur, NGO Representative at the United Nations
Tax Justice Network USA
Tri-State Coalition for Responsible Investment
U.S. Public Interest Research Group