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US professors advocate international tax reform before Senate Finance panel


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Witnesses at a Senate Finance Committee hearing held October 3 expressed discontent with the current US international tax system and agreed that American companies are treated unfairly in comparison to foreign companies operating in the US.

There was also consensus that the US tax base should be broadened but accompanied by appropriate and enforceable anti-base erosion rules.

The hearing, which featured testimony of four US tax professors, focused on proposed reform of the US international tax system, presented in a framework unveiled September 27. The framework, offered by Republican leaders, proposes a move to a territorial tax system coupled with a global minimum tax and deemed repatriation of US multinationals’ foreign earnings accumulated overseas.

Bret Wells, Professor of Law and George Butler Research Professor of Law, Law Center, University of Houston, testified that US companies are competitive internationally. Within US borders, though, the tax rate applied to US companies is significantly higher than that of foreign companies, Wells said.

Stephen E. Shay, Senior Lecturer on Law, Harvard Law School, reminded the committee that US companies are vigorous in taking advantage of favorable tax rates in other countries. As the committee takes steps to strengthen the US source tax rules, it must be mindful that other countries may do the same, Shay warned.

Witnesses concluded that foreign businesses should be subject to balanced, not discriminatory, taxation to preserve foreign investment while reducing incentives for corporate inversion.

Senator Rob Portman (R-Ohio), reminded the committee that foreign acquisitions are another symptom of our current tax system. Chairman Orrin Hatch (R-UT) expressed a similar sentiment, saying “perhaps even worse than an inversion is when a larger foreign corporation simply acquires a smaller American corporation.”

Headquarters companies
Itai Grinberg, Professor of Law at Georgetown University Law Center, said that multinational corporations produce jobs that pay a third higher than non-multinational corporations and that multinational corporations produce the most jobs in their home countries.

The cost of failing to produce international tax reform is the whittling away of the corporate tax base and job loss, confirmed by the Congressional Budget Office, Ginberg said.

Senator Portman, citing Ernst and Young, observed that 4,700 more companies would be based in the United States if there were a 20% corporate rate and a territorial tax system.

Professor Grinberg also said that foreign direct investment creates jobs and advised against protectionist rates. He advocated for a principled and level approach with an inbound minimum tax that would defend the tax base consisting of income earned in the United States from American citizens and consumers.

Kimberly Clausing, a Thormund A. Miller and Walter Mintz Professor of Economics at Reed College, testified that US tax reform should include a per-country minimum tax to reduce profit shifting, because some countries will always have rock bottom rates. Professor Shay agreed, adding that a territorial system is toothless without a per-country minimum tax.

Professor Wells cautioned against double taxation but reinforced the advantages of a level playing field for businesses competing in the United States.

Professor Grinberg cautioned the committee that territorial systems often have rules for base protection, and the active business exception rule in the European Union is narrow. A higher level of substance for an active business exception would move jobs offshore, he said.

Professor Clausing told the committee the tax reform framework contains no language to prevent base erosion and warned that such language might get lost in the legislative shuffle if the process is rushed.

**Repatriation rates**

Professor Shay said the tax reform framework language proposing different repatriation rates on cash than illiquid assets should be replaced with a single rate because tax planners will redraw the line between cash equivalents and illiquid assets. Professor Wells agreed, saying that all businesses will find ways to minimize the outbound tax.

Senator Stabenow (D-MI) asked witnesses if they would support eliminating the business expense deduction for companies that move their jobs overseas. Professors Wells and Clausing said the problem is larger than that. Professor Shay was reluctant to pick out certain pieces, and Professor Grinberg said a far more comprehensive solution is required.
Revenue neutrality

Ranking Member Ron Wyden (D-OR) asked witnesses if tax cuts pay for themselves. Professors Shay and Clausing said no. **Professor Wells said there need to be offsets to tax cuts and Professor Grinberg said that appropriate cuts can increase revenues, but only by a certain amount.**

Senator Toomey (R-PA) reminded the committee that the ongoing process is not moving towards tax cuts, rather tax reform, and it cannot be scored as revenue-losing until the legislation is further defined.

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