United States Senate
WASHINGTON, DC 20510–3905

September 3, 2021

The Honorable Ron Wyden
Chairman
Senate Finance Committee
219 Dirksen Senate Office Building
Washington DC, 20510

The Honorable Sherrod Brown
United States Senator
503 Hart Senate Office Building
Washington DC, 20510

The Honorable Mark Warner
United States Senator
703 Hart Senate Office Building
Washington DC, 20510

Dear Chairman Wyden, Senator Brown, and Senator Warner,

Thank you for your leadership in drafting legislation to reverse incentives in the Trump tax law to shift profits and outsource jobs overseas. We appreciate the opportunity to comment. This draft legislation makes great strides towards leveling the playing field for American workers and domestic businesses, large and small.

Fixing our international tax system will provide a major source of revenue to finance President Biden's Build Back Better plan to create an economy that works for everyone. President Biden's international tax reform proposal, from which the draft legislation draws, would raise over $1 trillion in revenue, according to the Department of Treasury.[1] But its importance goes beyond raising revenue. Strong international tax reform will make our tax code fairer for and improve the competitiveness of American workers and domestic businesses. We look forward to working with you to ensure this legislation fulfills its promise, and offer the comments below.

Reforms to the tax on offshore profits (GILTI):

The regime for taxing Global Intangible Low-Taxed Income (GILTI) created by the Trump tax law contains three significant flaws, each of which encourages companies to shift profits and outsource jobs overseas: 1) a rate on offshore profits that is half the domestic rate; 2) an exemption from that discounted rate for up to a 10 percent return on tangible investments like plants and equipment (QBAI); and 3) a global structure that allows companies to shrink their tax bill by blending streams of income from high-tax countries and tax havens.

The draft legislation currently does not specify a GILTI rate, a critical decision that will determine its effectiveness. We support fully eliminating the deduction for GILTI so that there is

[1] Department of the Treasury, General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals, May 2021, https://home.treasury.gov/system/files/131/General-Explanations-FY2022.pdf.

no longer a tax advantage for foreign profits over domestic profits. Short of fully equalizing the domestic and foreign rates, the GILTI rate should be no lower than the 21% President Biden has proposed.

We applaud the draft legislation for fully eliminating the tax break for QBAI. There is simply no justification for allowing a company to escape taxes entirely by building factories overseas. We also applaud the creation of a country-by-country system for GILTI, in which deductions or credits cannot be claimed for foreign taxes attributable to high-tax income that is excluded from the regime.

You note that the drafters are considering how to deal with losses. Under the GILTI structure created by the draft, carryforwards would add significant complexity and open the door to gamesmanship. Allowing carryforwards would likely require structuring the system as President Biden proposed, with a separate foreign tax credit limitation for each country, in order to prevent losses in one country from offsetting income in another.

You also note that the status of the foreign tax credit haircut remains under consideration. If the legislation does not equalize the GILTI rate with the domestic rate, we believe Congress should maintain the current haircut, rather than making it more generous than it already is under the Trump tax law. Currently, a multinational can write-off half of its GILTI and still claim a credit for 80 percent of its foreign taxes paid, allowing it to offset income that is exempt from U.S. tax.

Some have said that President Biden's reforms go too far because they are more ambitious than the minimum standards to which other countries have committed. In complying with the global minimum tax agreement, America should not let foreign countries that do the bare minimum dictate what is best for America. The Republican discussion of competitive advantage for big American corporations operating overseas ignores and obscures the disadvantage to domestic small businesses with only U.S. operations which must compete at a tax disadvantage against those big enough to operate overseas.

These reforms will make America a more attractive investment location for U.S. multinationals, reduce outsourcing incentives, level the playing field for domestic companies, and finance critical investments.

Reforms to the tax on base erosion payments

The Base Erosion and Anti-Abuse Tax (BEAT) created by the Trump tax law contains significant flaws that have substantially limited its effectiveness. The BEAT:

- *Exempts most large companies*. The tax only applies to companies with more than $500 million in gross receipts. Other anti-abuse measures in the tax code or in regulations apply to companies with more than $25 million to $50 million in gross receipts.[2]
- *Only applies to companies whose payments to offshore subsidiaries exceed three percent of their overall deductions*. This threshold is unnecessary, creates an arbitrary cliff, and incentivizes gamesmanship.

[2] E.g. section 163(j) ($25 million) and Treasury regulations under section 385 ($50 million).

- *Excludes many payments to offshore subsidiaries*. The Trump tax law exempts costs of goods sold (COGS) payments from the BEAT, which opens the door for significant profit shifting to escape the BEAT entirely.[3]

The drafters are considering the best way to incorporate the purposes and policies of President Biden's Stopping Harmful Inversions and Ending Low-Tax Developments (SHIELD) proposal into the BEAT. We support the SHIELD proposal, which would address the flaws noted above. It would also provide a powerful incentive for countries that have not joined the global tax deal to do so. For those that refuse, it would take away the main tax benefit a U.S. company would get if it chose to renounce its American citizenship by moving to such a country. At the very least, the legislation should apply the BEAT to companies with more than $100 million in gross receipts, eliminate the three percent threshold, and limit the exception for COGS.

Reforms to deduction for Foreign Derived Intangible Income (FDII)

The Trump tax law created a new tax break for so-called Foreign-Derived Intangible Income (FDII). Like the GILTI regime, the design of this provision encourages large multinationals to locate tangible assets like plants and equipment offshore. The more tangible assets a company locates here in the U.S., the smaller the tax break. Further, it provides a windfall to large companies earning excess profits which are benefiting from the returns on earlier investments.[4] Prior to the Trump tax law, many large multinationals could already avail themselves of numerous tax breaks to avoid paying tax entirely.[5] FDII provides an additional break to many of these same multinationals, the repeal of which JCT estimates would save $224 billion.[6]

The draft legislation would address a major problem with the FDII regime: the incentive it creates to locate fewer tangible assets in the U.S. We recommend repealing the FDII entirely, as proposed by President Biden. The benefits of the proposed tax break for domestic innovation income should be weighed against the opportunity cost of other options for deploying these funds to invest in R&D and American workers.

Allocation of stewardship expenses

Under current law, a portion of expenses incurred in the U.S. that give rise to foreign income must be allocated to that foreign income, which reduces the foreign tax credits companies can claim and prevents a subsidy for foreign taxes levied. This is sound policy.

Under the draft legislation, expenses for R&D and stewardship expenses would not have to be allocated to the foreign income to which they gave rise. This additional tax break for large multinationals is unnecessary, and especially problematic in the case of stewardship expenses

[3] Richard Phillips, "Understanding and Fixing the New International Corporate Tax System," *Institute on Taxation and Economic Policy,* July 2018, https://itep.sfo2.digitaloceanspaces.com/fixinginternationalsystem0718.pdf.
[4] Department of Treasury, The Made in America Tax Plan, April 2021, https://home.treasury.gov/system/files/136/MadeInAmericaTaxPlan_Report.pdf.
[5] Robert S. McIntyre, et al., "Sorry State of Corporate Taxes," *Citizens for Tax Justice,* February 2014, https://ctj.org/the-sorry-state-of-corporate-taxes/.
[6] Joint Committee on Taxation, March 2, 2021, https://www.sanders.senate.gov/wp-content/uploads/Corporate-Tax-Dodging-Prevention-Act-Score-of-offshore-portion.pdf.

which risk encompassing all headquarters expenses, including exorbitant executive salaries. If the legislation remains in its current form, it is especially important to extend the $1 million per-employee compensation deduction limit that exists for a company's top executives to all employees, as proposed in the Stop Subsidizing Multimillion Dollar Corporate Bonuses Act (S. 178).

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As you consider additional reforms to the international tax system, we urge you to consider the following:

Cracking Down on Inversions

President Biden's plan proposes reforms to make it harder for companies to "invert," a practice whereby companies renounce their U.S. citizenship to avoid taxes. These reforms are in line with those included in the Stop Corporate Inversions Act (S. 1501) and the No Tax Breaks for Outsourcing Act (S. 714). These bills would deem companies formed by certain mergers between U.S. companies and smaller foreign firms to be U.S. taxpayers, no matter where in the world the new companies claim to be headquartered. The combined company would continue to be treated as a domestic corporation if the historic shareholders of the U.S. company own more than 50 percent of the new entity. If the new entity is managed and controlled in the U.S. and continues to conduct significant business here, it would continue to be treated as a domestic company regardless of the percentage ownership.

Combating earnings stripping by restricting the interest deduction for multinational enterprises with excess domestic indebtedness

Some multinational corporations reduce or eliminate their U.S. tax bills by concentrating their worldwide debt, and the resulting interest deductions, in their U.S. subsidiaries. The No Tax Breaks for Outsourcing Act (S. 714) includes a provision to limit interest deductions for U.S. subsidiaries of a multination corporation in cases where a disproportionate share of the worldwide group's debt is located in the U.S. entity. Disallowed interest with respect to this provision and the existing limitation under section 163(j) could be carried forward for five years. This reform was included in the original version of the Trump tax law, but it was stripped out of the conference agreement after corporate lobbying.

Country-by-country corporate transparency

Under current law, companies must report basic information on profits, taxes, employees, and tangible assets, to the IRS. The Disclosure of Tax Havens and Offshoring Act (S. 1545) would require public disclosure, which would allow investors to access this important information and enable policymakers and the public to evaluate the efficacy of our international tax laws.

Disallowing deductions attributable to foreign income exempt from U.S. tax or taxed at preferential rates under GILTI

Under current law, deductions are disallowed for certain income that is determined to be wholly exempt from U.S. tax. Companies should not be entitled to a deduction from income that was never subject to U.S. tax in the first place. President Biden proposes to strengthen this provision to ensure that income taxed at lower tax rates cannot avoid this limitation entirely simply because only a portion of the income is wholly exempt from U.S. tax.[7] While we believe foreign income should be taxed at the same rates as domestic income, if there is a tax break for foreign income, companies should not be able to claim deductions against income that was never fully taxed.

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We thank you for the opportunity to comment on this draft legislation that proposes critical reforms that would make our international tax system fairer and help finance President Biden's Build Back Better plan.

Sincerely,

Sheldon Whitehouse
United States Senator
Chairman, Subcommittee on
Taxation & IRS Oversight

Richard J. Durbin
United States Senator

Jack Reed
United States Senator

Chris Van Hollen
United States Senator

Elizabeth Warren
United States Senator

[7] Treasury, General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals, https://home.treasury.gov/system/files/131/General-Explanations-FY2022.pdf.