NATIONAL TAXPAYERS UNION

September 3, 2021

The Honorable Ron Wyden
Chair, Senate Committee on Finance
219 Dirksen Senate Office Building
Washington, D.C. 20510

The Honorable Sherrod Brown
503 Hart Senate Office Building
Washington, D.C. 20510

The Honorable Mark Warner
703 Hart Senate Office Building
Washington, D.C. 20510

Dear Chair Wyden, Senator Brown, and Senator Warner:

On behalf of National Taxpayers Union (NTU), the nation's oldest taxpayer advocacy organization, I wish to offer comments on your discussion draft for overhauling the international tax system, which you released on August 25.[1] Though we may differ over several distinct parts of your latest proposal, we appreciate your willingness to examine what is and is not working in a very complicated part of the U.S. tax code that is still far from perfect in terms of maximizing simplicity, certainty, and growth potential for U.S. multinational companies (MNCs) and their U.S. workers.

NTU has engaged extensively with both domestic and international stakeholders on the years-long efforts to reform and overhaul international corporate tax provisions. Along with our sister organization, NTU Foundation, we have weighed in on the debate and passage of international tax provisions in the Tax Cuts and Jobs Act (TCJA) in 2017,[2] the subsequent implementation of such provisions by the Treasury Department in 2018 and 2019,[3] the OECD's consideration of stakeholder views for its Pillar One and Pillar Two blueprints in 2020,[4] and the Biden administration's proposals to overhaul the international tax system and achieve a global tax agreement in 2021.[5] As you know, we also weighed in on your framework for "Overhauling International Taxation" in April,[6] and we appreciate your willingness to engage with stakeholders from all corners of the tax policy community.

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[1] United States Senate Committee on Finance. "Wyden, Brown, Warner Unveil International Taxation Overhaul Discussion Draft." August 25, 2021. Retrieved from: https://www.finance.senate.gov/chairmans-news/wyden-brown-warner-unveil-international-taxation-overhaul-discussion-draft (Accessed August 25, 2021.)

[2] Wilford, Andrew; Woody, Spencer; and Brady, Demian. "What's the Deal with Base Erosion?" NTU Foundation, September 14, 2017. Retrieved from: https://www.ntu.org/library/doclib/NTUF-PP-179-Tax-Base-Erosion.pdf

[3] Sepp, Pete. "Treasury Can Keep GILTI from Harming Innocent Taxpayers." National Taxpayers Union, March 15, 2019. Retrieved from: https://www.ntu.org/publications/detail/treasury-can-keep-gilti-from-harming-innocent-taxpayers

[4] Sepp, Pete. "Comments to the OECD Centre for Tax Policy and Administration." National Taxpayers Union, December 14, 2020. Retrieved from: https://www.ntu.org/publications/detail/comments-to-the-oecd-centre-for-tax-policy-and-administration

[5] Lautz, Andrew. "Treasury, Congress Should Keep U.S. Businesses and Workers at Front of Global Tax Talks." National Taxpayers Union, August 24, 2021. Retrieved from: https://www.ntu.org/publications/detail/treasury-congress-should-keep-us-businesses-and-workers-at-front-of-global-tax-talks

[6] Lautz, Andrew. "Senate Finance Should Mind U.S. Competitiveness When Reforming the International Tax System." National Taxpayers Union, April 16, 2021. Retrieved from: https://www.ntu.org/publications/detail/senate-finance-should-mind-us-competitiveness-when-reforming-the-international-tax-system

Key Principles for International Tax Reform

Building off our prior work, and especially our comments to the OECD Centre for Tax Policy and Administration in December 2020, we wish to share a few key principles NTU urges policymakers to consider when designing changes to the tax treatment of U.S. business income earned abroad:

- **Maintain or improve America's ability to retain and attract both tangible and intangible assets**: As you know, a number of factors will motivate an MNC's decisions on where to locate tangible assets (like factories and equipment) and intangible assets (like intellectual property, or IP). Possible motivating factors include a jurisdiction's regulatory regime, its IP protections, its labor costs and quality, its market size, and its customer base.[7] Of course, tax rates and tax incentives play a significant role in these decisions, too.[8] To the extent that proposed changes to the U.S. code make the U.S. a less tax-competitive jurisdiction relative to economic peers with similar non-tax features as the U.S. (such as regulatory regimes and labor force quality), policymakers proposing such domestic changes risk incentivizing the offshoring of assets, jobs, and profits abroad.[9] Instead, lawmakers should be designing tax policy so that the code incentivizes companies to not only ***retain*** assets, jobs, and profits in the U.S. but to actually ***move*** assets, jobs, and profits currently located overseas to the U.S.
- **Design tax policy with simplicity and certainty first in mind, and potential tax revenue gains last**: As NTU President Pete Sepp put it in December, "No international tax framework can function with simplicity and certainty for long if it is designed with the overriding goal of merely raising additional revenues. Over time, the urge to 'trap' various forms of income, sales, and cross-border business activity for tax purposes will invariably lead to more arcane, complex laws and rulemakings that trigger heavier compliance burdens for taxpayers and heavier administrative burdens for governments."[10] We understand supporters of President Biden's "Build Back Better" agenda are eager to offset the President's proposed $3.5 trillion in new spending,[11] but tax policy designed solely to maximize revenues will ultimately harm low-income and middle-class taxpayers, and/or increase tax complexity and uncertainty. NTU's analysis of how a 28-percent corporate rate would hit taxpayers making less than six figures -- a $100 billion tax increase over 10 years, according to our estimates[12] -- should serve as a cautionary note to policymakers hoping for increased U.S. corporate tax rates.

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[7] For more, see "III. Economic Analysis" in: Joint Committee on Taxation (JCT). "U.S. International Tax Policy: Overview And Analysis." JCTX-16R-21, April 19, 2021. Retrieved from: https://www.jct.gov/publications/2021/jcx-16r-21/ (Accessed August 25, 2021.)

[8] For more, see "III.C. Location of Tangible Investment" and "III.D. Location of Intangible Property and the Returns to Intangible Investment, and Research Activity" in: *Ibid*.

[9] Kallen, Cody. "International Tax Proposals and Profit Shifting." Tax Foundation, August 24, 2021. Retrieved from: https://taxfoundation.org/international-tax-proposals-profit-shifting/ (Accessed August 25, 2021.)

[10] Sepp, Pete. "Comments to the OECD Centre for Tax Policy and Administration." National Taxpayers Union, December 14, 2020. Retrieved from: https://www.ntu.org/publications/detail/comments-to-the-oecd-centre-for-tax-policy-and-administration

[11] Scholtes, Jennifer, and Faler, Brian. "Democrats scramble for cash to cover Biden's $3.5T plan." *Politico*, August 3, 2021. Retrieved from: https://www.politico.com/news/2021/08/03/democrats-cash-cover-biden-plan-502187 (Accessed August 25, 2021.)

[12] Lautz, Andrew. "Biden's Corporate Tax Increase Could Be a $100 Billion Tax Hike on Taxpayers Making Less Than $100K." National Taxpayers Union, August 12, 2021. Retrieved from: https://www.ntu.org/publications/detail/bidens-corporate-tax-increase-could-be-a-100-billion-tax-hike-on-taxpayers-making-less-than-100k

- **Recognize the economic realities of operating multinational businesses in the 21st century**: We wrote to you in April that we were worried "some proposed changes in this framework … would punish companies for any number of legitimate reasons that they would have a facility, or workers, or tangible assets overseas."[13] While policymakers have a legitimate interest in ensuring that multinational profits are booked in jurisdictions with sufficient links to substantive economic activity, it is our firm belief that to deny companies some kind of substance-based carve-out would be to deny the economic realities of operating an MNC in 2021. The principle also applies to the risks policymakers take when they make the U.S. tax climate too inhospitable for MNCs in a highly mobile, digitalizing, and globalizing world.

NTU Feedback on the Discussion Draft

Unfortunately, we believe several aspects of your discussion draft stray from the principles outlined above:

- **Increasing the Global Intangible Low-Taxed Income (GILTI) rate**, depending on the final rate lawmakers settle on, and **repealing the Qualified Business Asset Investment (QBAI) substance-based carve-out** would hurt U.S. tax competitiveness, and in turn could incentivize the offshoring of U.S.-based assets, jobs, and profits abroad;
- **Moving to country-by-country GILTI calculations** and **adding a second bracket to the Base Erosion and Anti-Abuse Tax (BEAT)** would make the tax code more complex and create additional uncertainty for U.S. businesses, and appear to be designed with revenue gains and/or spending offsets foremost in mind;[14] and
- **Maintaining a foreign tax credit (FTC) haircut** (especially combined with the higher GILTI rate and the repeal of QBAI) and **equalizing the GILTI and Foreign Derived Intangible Income (FDII) deduction rates** (especially if GILTI retains an FTC haircut) would fail to recognize the economic realities of operating a U.S. MNC in the 21st century.

We consider each of these proposals in turn.

Increasing the GILTI rate

While the Biden administration envisions a doubling of the GILTI rate, from its current 10.5 percent to 21 percent,[15] your discussion draft does not specify a new GILTI rate other than to say the GILTI rate will be higher than it currently is.[16] We reiterate our significant concern with the Biden administration GILTI proposal and our opposition to increasing the rate. Should you increase the GILTI rate, we urge you to only do so to the extent

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[13] Lautz, Andrew. "Senate Finance Should Mind U.S. Competitiveness When Reforming the International Tax System." National Taxpayers Union, April 16, 2021. Retrieved from: https://www.ntu.org/publications/detail/senate-finance-should-mind-us-competitiveness-when-reforming-the-international-tax-system

[14] United States Senate Committee on Finance. "Wyden, Brown, Warner Unveil International Taxation Overhaul Discussion Draft." August 25, 2021. Retrieved from: https://www.finance.senate.gov/chairmans-news/wyden-brown-warner-unveil-international-taxation-overhaul-discussion-draft (Accessed August 25, 2021.)

[15] Department of the Treasury. "General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals." May 2021. Retrieved from: https://home.treasury.gov/system/files/131/General-Explanations-FY2022.pdf#page=10 (Accessed August 31, 2021.)

[16] Future references to the Wyden framework in this letter are sourced from the following section-by-section: Senate Committee on Finance. "International Tax Reform Framework Discussion Draft: Section-by-section description." August 2021. Retrieved from: https://www.finance.senate.gov/imo/media/doc/section%20by%20section%20-%20WBW%20Framework%20discussion%20draft%208.20.21%20FINAL.pdf (Accessed August 31, 2021.)

required by our international commitments under Pillar Two -- and only if Inclusive Framework (IF) members successfully implement the global tax agreement.

Very few OECD members currently operate "fully worldwide" tax systems, according to the nonpartisan Tax Foundation.[17] While this may change under the Pillar Two agreement, such a regime is contingent on dozens and dozens of countries agreeing to and implementing specific Pillar Two-compliant regimes in the next 14 months -- a herculean task, to put it mildly. If the U.S. were to significantly raise its GILTI rate without corresponding implementation of Pillar Two regimes in economic- and/or tax-competitive countries, or if the U.S. were to raise its GILTI rate well beyond what is needed to comply with Pillar Two, as President Biden has proposed, then policymakers could, in combination with other proposals to increase U.S taxation of business profits, incentivize the offshoring of jobs and profits overseas.

As we noted in our recent correspondence with the Treasury Department,[18] Tax Foundation analysis confirms that Biden administration proposals would increase profit shifting from the U.S., on net. The proposed rise in the domestic corporate rate (from 21 percent to 28 percent) and the repeal of FDII (which we acknowledge your discussion draft does ***not*** include) would more than outweigh any increased U.S. tax revenue from raising the GILTI rate:

> "[T]he full Biden administration proposal would raise the average tax rate on CFC activity by 4.9 percentage points, but a 28 percent corporate tax rate and repeal of the FDII deduction raise the average tax rate on U.S. activity by more than 7 percentage points. On net, this would increase profit shifting out of the U.S."[19]

We further note that President Biden's proposed GILTI rate is 40 percent higher than it might need to be under Pillar Two, given the current global agreement provides for a 15-percent minimum rate and President Biden has proposed 21 percent. Further, we remain concerned that without the repeal of the foreign tax credit (FTC) haircut the effective GILTI rates on U.S. companies could be several points higher than the statutory rate -- up to 13.125 percent under current law and up to 26.25 percent under the Biden proposal. More on that below. All of this adds up to a tax code that is less able to compete for future assets, jobs, and taxable profits than jurisdictions with, say, a 15-percent GILTI rate, a substance-based carve-out, and no haircut on FTCs.

Repealing QBAI

Both the Biden administration and your framework envision repealing the substance-based carve-out in the current U.S. regime, called qualified business asset investment (QBAI). When lawmakers created the GILTI regime, they intended to focus domestic taxation of foreign business income on returns from highly mobile and highly profitable intangible assets. This is why GILTI includes the 10-percent QBAI carve-out. This carve-out is hardly a policy unique to the U.S. or even to Republican lawmakers' preferences, given the July Pillar Two agreement envisions a carve-out equal to five percent (or 7.5 percent, in the first five years) of payroll and tangible assets.

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[17] Tax Foundation. "Worldwide Tax System." 2021. Retrieved from: https://taxfoundation.org/tax-basics/worldwide-taxation/ (Accessed August 31, 2021.)

[18] Lautz, Andrew. "Treasury, Congress Should Keep U.S. Businesses and Workers at Front of Global Tax Talks." National Taxpayers Union, August 24, 2021. Retrieved from: https://www.ntu.org/publications/detail/treasury-congress-should-keep-us-businesses-and-workers-at-front-of-global-tax-talks

[19] Kallen, Cody. "Options for Reforming the Taxation of U.S. Multinationals." Tax Foundation, August 12, 2021. Retrieved from: https://taxfoundation.org/us-multinational-tax-reform-options-gilti/ (Accessed August 19, 2021.)

Repealing QBAI would subject *all* returns from a U.S. business's foreign-derived income to the minimum GILTI rate (whatever that rate is), and in turn would punish businesses merely for having tangible assets located around the world. Repealing QBAI while the rest of the world enacts a substance-based carve-out would also put U.S. MNCs at a significant disadvantage relative to MNCs based in other countries.

Moving from global to country-by-country calculations under GILTI

As you know, the July Pillar Two agreement envisions country-by-country calculations of multinational companies' tax liabilities. One cold comfort for U.S. taxpayers and their advocates is that country-by-country calculations of top-up tax liability in every IF member country ***could*** ensure that there is at least a level playing field between the U.S. and its economic competitors.

Unfortunately, by insisting on country-by-country calculations of tax liability in global tax negotiations, the Biden administration has put U.S. policymakers in a bind that will significantly increase complexity for U.S.-based MNCs. Your discussion draft envisions a Pillar Two-compliant country-by-country calculation of tax liability that nonetheless excludes high-tax countries from GILTI liability. While we acknowledge that your discussion draft may be slightly less burdensome than the Biden administration's proposal for country-by-country calculations in high- and low-tax jurisdictions, we still believe that lawmakers and the Biden administration must agree on simplification measures for U.S. MNCs and the IRS -- much like the ones envisioned in the October 2020 OECD Pillar Two blueprint.

As we wrote in an August 2021 post on your discussion draft:

> "Absent the administration's willingness (or lawmakers' willingness) to push back on country-by-country calculations at this late stage of global negotiations, lawmakers should contemplate safe harbors, de minimis thresholds, or other simplification measures that would ease the reporting burden on U.S. MNCs and the administrative burdens on an already-overburdened IRS. The OECD envisions such simplification options in the global agreement, and all center somewhat on the country-by-country quandary."[20]

To specify a bit further, a safe harbor for GILTI tax liability calculations could apply to U.S. MNCs operating in jurisdictions with a minimum statutory or effective tax rate. For example, U.S. policymakers can be confident that a U.S. MNC paying an effective tax rate of 20 percent or more (according to already-existing requirements for MNCs to file country-by-country reports under OECD agreements) in a given country has complied with the global minimum, and does not need to do any further tax calculation work. Or the U.S. could include a profits de minimis threshold for top-up liability, so long as such a threshold is OECD-compliant, that suspends requirements to calculate tax liability in countries where a U.S. MNC is booking a minimal amount of total global pre-tax profits, such as 2.5 percent.[21] We encourage lawmakers to pursue simplification options that will reduce compliance burdens for U.S. MNCs and administrative burdens for an already-overburdened IRS.

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[20] Lautz, Andrew. "Early Reactions to Wyden's International Tax Draft." National Taxpayers Union, August 26, 2021. Retrieved from: https://www.ntu.org/publications/detail/early-reactions-to-wydens-international-tax-draft

[21] This is the threshold suggested by OECD in their "Simplification Options" under the October 2020 Pillar Two Blueprint: OECD. "Tax Challenges Arising from Digitalisation - Report on the Pillar Two Blueprint." October 2020. Retrieved from: https://www.oecd.org/tax/beps/tax-challenges-arising-from-digitalisation-report-on-pillar-two-blueprint.pdf (Accessed August 18, 2021.)

Adding a second bracket to BEAT

NTU has its fair share of concerns with the Biden administration's proposal to replace the Base Erosion and Anti-Abuse Tax (BEAT) with a Stopping Harmful Inversions and Ending Low-tax Developments (SHIELD) regime, especially the fact that SHIELD would apply to companies with annual global revenues above $500 million while the July Pillar Two agreement envisions a much higher threshold of around $877 million.[22] While your discussion draft does not carry many specifics on SHIELD, we are concerned that adding a second tax bracket to the existing BEAT regime will increase complexity and uncertainty for U.S. businesses, complicating an already complex TCJA-era tax as administration mulls completely replacing BEAT.

Your draft legislation would add a second tax bracket applying to base erosion income for MNCs, at an unspecified but higher rate than the 10-percent rate applied to regular taxable income under BEAT. The apparent motivation for this second bracket is to pay for "restoring the full value of tax credits for domestic investment" in BEAT.[23] Lawmakers should design tax policy with simplicity, certainty, and administrability in mind first and foremost, with potential revenue gains as a secondary consideration. Unfortunately, it seems these higher taxes are designed as an offset and/or pay-for first and foremost.

Maintaining the FTC haircut

Your discussion draft envisions either repealing the FTC haircut or maintaining some haircut (between just above zero percent and the 20 percent haircut that is effective under current law). We would strongly urge you to repeal the FTC haircut, given it raises effective GILTI rates above the statutory GILTI rate in many cases. As we wrote in our August 2021 post on the draft legislation:

> "One of the flaws of the current-law GILTI regime is that it limits the amount of foreign taxes a U.S. MNC can use to offset their GILTI liability; the so-called FTC haircut. Specifically, it allows a U.S. MNC to only apply 80 percent of their foreign taxes to offset GILTI. This means effective tax rates in some jurisdictions are higher than GILTI's 10.5-percent statutory rate, and can go as high as 13.125 percent. Chair Wyden's discussion draft envisions possibly leaving the 20-percent FTC haircut in place, or possibly eliminating the FTC haircut altogether, or possibly having some FTC haircut smaller than 20 percent. Lawmakers should repeal the FTC haircut; otherwise, the effective GILTI rate will actually be higher than the statutory rate in many cases. As noted above, under the Biden proposal GILTI rates could go as high as 26.25 percent in some jurisdictions, exacerbating the tax hike (especially in combination with the repeal of QBAI without a replacement)."[24]

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[22] Lautz, Andrew. "Treasury, Congress Should Keep U.S. Businesses and Workers at Front of Global Tax Talks." National Taxpayers Union, August 24, 2021. Retrieved from: https://www.ntu.org/publications/detail/treasury-congress-should-keep-us-businesses-and-workers-at-front-of-global-tax-talks

[23] United States Senate Committee on Finance. "Wyden, Brown, Warner Unveil International Taxation Overhaul Discussion Draft." August 25, 2021. Retrieved from: https://www.finance.senate.gov/chairmans-news/wyden-brown-warner-unveil-international-taxation-overhaul-discussion-draft (Accessed August 25, 2021.)

[24] Lautz, Andrew. "Early Reactions to Wyden's International Tax Draft." National Taxpayers Union, August 26, 2021. Retrieved from: https://www.ntu.org/publications/detail/early-reactions-to-wydens-international-tax-draft

We understand and appreciate that lawmakers included the FTC haircut to "protect against foreign soak-up taxes" on the foreign income of U.S. MNCs,[25] but the soak-up matter will be less of a relevant concern in a world where over 130 countries implement the global tax agreement. Furthermore, repealing the FTC haircut would better and more fully prevent double taxation of U.S. businesses' foreign-source income -- reflecting the reality that U.S. MNCs operate in several countries, pay taxes in those countries, and should receive full credit for foreign taxes paid. Repealing the haircut will also prevent effective GILTI rates from unnecessarily exceeding the statutory minimum.

Equalizing GILTI and FDII deduction rates

Your draft legislation also envisions equalizing the tax rates on GILTI and on the new "foreign-derived innovation income" deduction (which is meant to replace the current foreign-derived intangible income deduction enacted under TCJA).[26] Unfortunately, the equalization of GILTI and FDII deduction rates does not actually represent equalization so long as an FTC haircut remains in place, since the effective GILTI rates that U.S. MNCs will pay for some countries will be higher than the statutory minimum. Take, for example, a theoretical equalization of GILTI and the new FDII rate at 15 percent. Assuming an FTC haircut of 20 percent remains in place, a U.S. MNC with a subsidiary in a country where the MNC pays a 10-percent effective tax rate and has $100 worth of GILTI in that country would pay $10 in foreign taxes (with no substance-based carve-out) but only receive credit for $8 in foreign taxes paid, and would owe $7 in the GILTI top-up tax. Given the FTC haircut, the MNC would effectively pay $17 in total taxes ($10 in foreign taxes plus the $7 in GITLI top-up tax) for an effective GILTI rate of 17 percent.

We also have concerns about the draft's proposal for replacing the current FDII regime with a new, "innovation" income regime. In particular, the lack of specificity on the potential new FDII rate is of concern, especially if it differs drastically from the current 37.5-percent deduction (or effective 13.125 percent preferential tax rate) on foreign-derived deemed intangible income under the current FDII. We believe this proposal requires more explanation and work from lawmakers before the entire Senate Finance Committee (or the entire Senate) votes on your legislation.

NTU Recommendations for Future International Tax Work in Congress

In conclusion, we would like to re-share some of the international tax reform recommendations we shared with the Treasury Department as they continue negotiations over implementation of the July global tax agreement. We believe several of these recommendations are relevant to your policy work in the weeks and months ahead. Relevant recommendations include:

- **Maintaining a 21-percent domestic corporate tax rate**: A 28-percent rate will make the U.S. significantly less tax-competitive than other countries. Additionally, some of the burden of the corporate tax increase will fall on workers and/or on middle-class households.
- **Keeping the GILTI rate as low as possible.** There is no policy justification for raising it higher than what is needed to comply with Pillar Two. A 15-percent GILTI rate, assuming global implementation of Pillar Two, would be much more appropriate than President Biden's proposed 21-percent GILTI rate.

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[25] See page 390 (PDF page 402): House Committee on Ways and Means. "Tax Cuts and Jobs Act: Report of the Committee on Ways and Means." November 13, 2017. Retrieved from: https://www.congress.gov/115/crpt/hrpt409/CRPT-115hrpt409.pdf (Accessed August 31, 2021.)

[26] We use the acronym FDII for both, distinguishing the proposed "foreign derived innovation income" as the "new FDII."

- **Maintaining a substance-based carve out**: We strongly urge you to reverse your plans to completely repeal the QBAI carve-out without a replacement. At minimum, the U.S. should have a carve-out that is at least as robust as a globally-implemented Pillar Two agreement allows.
- **Adding simplification options to country-by-country calculation under a revised GILTI regime**: A safe harbor threshold for countries with high ETRs, or a de minimis profits threshold for MNCs, could significantly reduce compliance and administrative burdens for both U.S. MNCs and the IRS.

Above all, we urge you to proceed with care and caution as you consider policies that will bring the U.S. into Pillar Two compliance. While we maintain grave concerns about the global tax agreement and its impact on American taxpayers, we are further concerned that rushed work may increase tax, compliance, and administrative burdens on U.S. business taxpayers, and may increase uncertainty in the domestic tax policy and planning communities. Lawmakers should not adhere to arbitrary deadlines that would shackle international tax reform to the need for revenue that pays for significant proposed new spending. Simplicity, certainty, administrability, and an environment that encourages U.S. economic, job, and wage growth should be front and center.

Should you have any questions or feedback, I am at your disposal.

Sincerely,

Andrew Lautz
Director of Federal Policy