Business Roundtable Submission on Tax Reform
United States Senate Committee on Finance
July 17, 2017

In response to Chairman Hatch's June 16 request for recommendations for tax reform, this submission reaffirms Business Roundtable's support for pro-growth tax reform. The nation's tax system is in urgent need of reform to boost economic growth, global competitiveness for American companies, and bring about meaningful improvements in the incomes of American families through higher wages and more and better paying American jobs.

It has been over 30 years since Congress last undertook tax reform. Since that time, the world's economies have become significantly more competitive and the U.S. tax system has become an anti-competitive drag on the U.S. economy. A recent Business Roundtable survey found that CEOs believe that tax reform is the single most effective action that Congress can take to accelerate economic growth. Seventy-six percent of the CEOs said that they would increase hiring at their company if the U.S. tax system is reformed.

Comprehensive tax reform for both individuals and businesses — including more competitive rates for non-corporate businesses — is fundamental to strengthening the U.S. economy, enhancing job creation, increasing wage growth, and ensuring that American workers and American companies can successfully compete around the globe. Tax reform should also be used to give a targeted boost to lower- and middle-income workers by expanding programs such as the Earned Income Tax Credit (EITC), which already provides a helping hand to more than 29 million workers. A comprehensive approach is the best way to create a modern, competitive tax system for both businesses and individuals. Business Roundtable calls for the following corporate tax changes:

- A corporate tax rate set at an internationally competitive level, and
- A modern international tax system (territorial-like) that permanently removes the penalty for returning foreign earnings to the United States, thereby aligning the U.S. system with the tax systems of our major trading partners.

We believe that these reforms can be achieved in a fair and fiscally responsible manner. Business Roundtable companies are committed to putting all corporate tax credits and special deductions on the table in consideration of an internationally competitive corporate tax system.

Based on the knowledge and experience of most Business Roundtable CEOs, the remainder of this submission focuses on reform of the corporate income tax system.

The Need for U.S. Corporate Tax Reform

The U.S. corporate tax system was last reformed in 1986. It is outdated and fails to reflect the increased competition American companies face from their global competitors both at home and abroad. The U.S. corporate tax rate is the highest among industrialized countries. Including state taxes, the combined U.S. statutory corporate tax rate is 38.91 percent, more than 15 percentage points higher than the 23.75 percent average combined national and sub-national statutory corporate tax rate of the other 34 members of the Organization for Economic Cooperation and Development.[1]

While effective tax rates are typically lower than statutory tax rates, U.S. effective tax rates are consistently found to be among the highest of developed countries. A recent study conducted for the European Commission found the corporate effective marginal tax rate for investments in the United States to be 34.3 percent while the average of the other 34 surveyed countries (28 EU countries, plus four other European countries, Canada, and Japan) was 16.0 percent.[2] Many other developed countries also have special favorable tax rules for intellectual property, including so-called "patent boxes" or "innovation boxes," with effective tax rates on such income typically ranging from 5 to 15 percent.[3]

Further, the U.S. international tax system still is premised on rules first adopted in 1909 that tax the worldwide income of American corporations. Virtually all other advanced economies — including all other G7 countries and 29 of the other 34 OECD countries — have adopted territorial tax rules that ensure that their own companies are as competitive as possible in the global marketplace.

Together, the high U.S. corporate tax rate and antiquated international tax rules make the U.S. corporate tax system an outlier from the rest of the world, harming the ability of American companies and their workers to compete successfully.

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[1] OECD Tax Database, available at: http://stats.oecd.org/Index.aspx?DataSetCode=TABLE_II1. The average U.S. state corporate tax rate is 6.01 percent according to the OECD. Because state corporate income taxes are deductible against federal corporate income taxes, the combined federal and state statutory corporate tax rate is .35 + (1-.35)(.0601) = 38.91 percent. If tax reform lowered the U.S. federal corporate tax rate to 20 percent, it would result in a combined federal and state tax rate of 24.81 percent – still a full percentage point greater than the OECD average rate.

[2] Center for European Economic Research (ZEW), "Effective Tax Levels Using the Devereux/Griffith Methodology," Project for the EU Commission TAXUD/2013/CC/120, Intermediate Report, October 2015, available at: http://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/common/publications/studies/effective_tax_rates.pdf.

[3] Countries with patent or innovation boxes include Belgium, France, Hungary, Ireland, Israel, Italy, Korea, Luxembourg, Malta, Netherlands, Portugal, Spain, Switzerland, Turkey, and the United Kingdom. For details on qualifying income and tax rates see PwC, *Global Research & Development Incentives Group*, April 2017, available at: https://www.pwc.com/gx/en/services/tax/international-tax-services/global-research-and-development-incentives-group.html.

Creating a Competitive Advantage

Our trading partners use their corporate tax systems to achieve competitive advantage at the expense of the American worker. For example, Canada has aggressively lowered its combined federal and provincial corporate tax rate from 42.4 percent to 26.7 percent since 2000, with the federal rate now at 15 percent. As outlined by the Canadian government in a 2006 policy document, *Advantage Canada*, this was part of an explicit Canadian policy to obtain a competitive advantage over the United States:

> To create a Canadian tax advantage over the coming years, Canada's New Government will…[e]stablish a broader corporate tax advantage for Canada in the treatment of business investment. Step one is to create a meaningful tax advantage over the United States, our closest economic partner. Step two is to achieve the lowest tax rate on new business investment in G7 countries.[4]

Since 2000, average wages have grown 7 percent faster in Canada than in the United States.[5] And even with the substantially lower tax rate, Canada's federal corporate tax revenues as a share of GDP are greater than those of the United States and greater than in the 1980s when Canada's federal tax rate was twice as high.[6]

Perhaps not surprisingly, Canada understands U.S. tax reform can end Canada's tax advantage and attract greater investment to the United States.[7]

The problem for the United States has been that nearly every developed country has explicitly or implicitly sought to achieve a tax advantage over the United States. Of the other 34 OECD countries, all but one have lowered their statutory corporate tax rate since the last U.S. tax reform — and all have set their corporate tax rate below that of the United States.

At the same time, territorial tax systems — under which a company pays tax in the country in which profits are earned but not a second time when earnings are brought home to the company's home country — have become the norm among developed countries. Since

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[4] *Advantage Canada: Building a Strong Economy for Canadians*, Department of Finance Canada, p. 33, available at: https://www.fin.gc.ca/ec2006/pdf/plane.pdf.

[5] OECD statistics, available at: https://stats.oecd.org/Index.aspx?DataSetCode=AV_AN_WAGE.

[6] See, *Fiscal References,* Table 4, providing historical data on Canadian federal tax revenues, available at: http://www.fin.gc.ca/frt-trf/2016/frt-trf-16-eng.pdf.

[7] See recent articles in the Canadian press describing the potentially adverse impact of U.S. corporate tax reform on Canada's current tax advantage as well as the benefits to the United States: "Donald Trump's 'big, big' corporate tax cut could 'erase Canada's advantage'," *Global News*, March 1, 2017; (http://globalnews.ca/news/3279987/donald-trump-corporate-tax-cut-canada/); "Trump's corporate tax cut could end Canada's advantage," *Toronto Star*, April 26, 2017 (https://www.thestar.com/business/2017/04/26/trumps-corporate-tax-cut-could-end-canadas-advantage.html); "'A real negative for Canada': Businesses warn Trump's tax plan would hurt competitiveness," *National Post*, April 27, 2017 (http://business.financialpost.com/news/economy/a-real-negative-for-canada-businesses-warns-trumps-tax-cut-plan-would-hurt-competitiveness/wcm/c0ddad77-5698-44b4-8f15-5ac67c9bb059).

1990, the number of OECD countries with territorial tax systems has grown from 9 to 29.[8] Of the 29 countries, 21 provide 100 percent exemption for foreign qualifying dividends and the other 8 exempt 95 to 97 percent of such income, resulting in a home-country tax rate of approximately 1 percent on the foreign dividend.

U.S. companies operate in an increasingly competitive global marketplace. Among companies listed in the Global Fortune 500, the number of U.S.-headquartered companies declined by 25 percent between 2000 and 2015. U.S. companies competing abroad are virtually certain to be facing competition from a company headquartered in a territorial country in addition to locally headquartered companies that face only the local country tax.

Both a competitive U.S. corporate tax rate and adoption of a modern international tax system can turn the current U.S. tax disadvantage into a U.S. tax advantage. One study estimates that if the United States had provided a 25 percent U.S. federal corporate tax rate over the past 10 years, this reform would have increased U.S. acquisitions of foreign companies and reduced foreign acquisitions of U.S. companies by a net $769 billion and resulted in the creation and retention of 1,300 U.S.-headquartered companies.[9]

The Framework for a Competitive U.S. Corporate Tax System

Current high tax rates discourage investment and job creation in the United States by both U.S. and non-U.S. companies. Further, the current U.S. international tax rules hinder American companies in foreign markets and discourage them from bringing their earnings home for reinvestment.

Business Roundtable believes that reform should include reduction of the corporate tax rate to a competitive level, taking into consideration both federal and state corporate tax rates. Additionally, tax reform should include adoption of a modern international tax system, consistent with the territorial tax systems of our major trading partners, to allow U.S. companies to compete on a level playing field with their foreign competitors and return their foreign earnings for investment in the U.S. economy. We also believe these goals can be achieved in a fiscally responsible manner, taking into account the positive macroeconomic benefits from tax reform and a realistic budget baseline that acknowledges that longstanding tax provisions extended repeatedly on a short-term basis are in reality a permanent feature of current law.

We understand that tax reform will require a careful and balanced examination of existing tax preferences and that reform of the U.S. international tax system will be accompanied by appropriate safeguards to protect America's tax base. However, policymakers must be careful that proposals intended to protect against loss of the U.S. tax base are not so broad

[8] PwC, *Evolution of Territorial Tax Systems in the OECD*, prepared for the Technology CEO Council, April 2013; updated for accession of Latvia to the OECD in 2016, and Latvia's adoption of territorial rules in 2013.
[9] EY, *Buying and Selling: Cross-Border Mergers and Acquisitions and the U.S. Corporate Income Tax*, prepared for Business Roundtable, March 2015.

that they undermine the ability of American companies to compete against companies not encumbered by such restrictions.

At the end of the day, if U.S. tax reform is to be successful — if the United States is to end the competitive tax disadvantage that U.S. companies currently face — the reformed system should result in companies wanting to be headquartered in the United States over foreign domiciles. For too long we have observed investment dollars flowing out of the United States, companies inverting or being acquired by a foreign competitor, or entrepreneurs founding their new businesses outside of the United States due to the U.S. tax disadvantage. It is now time to establish a U.S. tax advantage. Let us once again make the United States the best place in the world to establish and grow a business.

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Business Roundtable, as the leaders of America's largest businesses, urges Congress and the Administration to work together with the highest priority to enact permanent, pro-growth tax reform this year in a fair and fiscally responsible manner. We stand ready to work with you to achieve this goal and to put America on a path of accelerated economic growth with higher wages and greater employment opportunities for all Americans.