The OECD BEPS Action Plan and the Need for US Tax Reform

by Dave Camp

I want to begin by expressing my appreciation for the opportunity to speak today at the 2015 OECD International Tax Conference. As a former Chairman of the House Ways and Means Committee, I have long been familiar with the historic mission of OECD to assist countries in forming consensus around policies that promote economic growth and cooperation. And I have followed closely the OECD's current effort to address base erosion and profit shifting, with its BEPS Action Plan.

I want to commend the US Council for International Business and the Business and Industry Advisory Committee for your efforts to provide constructive input to the OECD on issues of concern to US employers.

I want to speak today about the OECD BEPS initiative in the context of the current debate over US tax reform.

Although nominally a project aimed at a specific problem – the erosion of governments' tax bases and profit shifting – the reality is that the 15-point BEPS action plan opens the door to rewriting the rules of international taxation in nearly every respect, and doing so in a period of only two years.

While the BEPS project was intended to develop a new global consensus on the rules of international taxation, many governments have not waited for the BEPS process to play out and consensus rules to emerge. Some of the public commentary accompanying the effort has prompted some taxing authorities to seek an immediate increase in the tax paid by US companies. Others are using the BEPS project to advance a domestic tax agenda and to claim their "fair share" of corporate tax revenues. Even our close ally and proponent of the BEPS project, the United Kingdom, moved ahead of the project, enacting a "diverted profits tax" that took effect on April 1.

As many here are aware, the risk inherent in this trend is that as soon as one country moves ahead of the OECD consensus process, others are spurred to action, not wanting to be left behind. As a result, the danger of "global tax chaos marked by the massive re-emergence of double taxation," of which the OECD Action Plan itself warned, may have markedly increased.

As Chairman of the House Ways and Means Committee, I joined in June 2014 with now-Senate Finance Chairman Orrin Hatch in a statement expressing our concerns about the potential for aggressive actions by some countries to levy more taxes on US taxpayers before a consensus has been reached on the issues under consideration in the OECD BEPS Action Plan. Despite the best efforts of OECD officials – and here I want to thank Pascal Saint-Amans for his leadership – and the parties involved in this effort, many of the concerns Chairman Hatch and I expressed about the potential for the BEPS process to result in double or multiple taxation of cross-border investment continue to be relevant.

In particular, it appears that the accelerated timetable for completing the BEPS process itself has created pressures that make it difficult to have the meaningful discussions that are necessary to avoid numerous intergovernmental disputes in the future. The challenge of achieving true consensus continues to be a concern for many in the United States, especially as countries are beginning to consider how best to interpret and implement the recommendations of the BEPS Action plan.

To this point, I note that BIAC in their recent BEPS position paper has raised the concern that some serious business issues are not being sufficiently considered or addressed, notwithstanding the efforts of the OECD and G20 member governments. In their paper, BIAC identifies several areas of concern, including the need to narrow the overly broad scope of some BEPS proposals, the need for a consideration of the broader economic impact of proposals, the need for clear guidance given the uncertainty of how these complex proposals may be adopted and implemented by individual countries, and the need to consider the potential interaction of the various proposals before they are implemented.

The National Association of Manufacturers, or NAM, the nation's largest industrial trade association, also recently wrote a similar letter, raising concerns about the potential for the BEPS project to harm the global competitiveness of U.S. companies and threaten the jobs of U.S. workers. NAM noted that little attention seems to have been paid to whether burdensome new taxpayer reporting requirements will needlessly risk disclosure of sensitive, confidential U.S. taxpayer information to foreign competitors.

These are serious concerns that need to be carefully addressed before the project is concluded, and not neglected in the rush to meet an artificial deadline.

The letter that current Ways and Means Chairman Paul Ryan and Finance Chairman Hatch sent yesterday to Treasury Secretary Lew is a clear sign that my former colleagues in Congress take to heart the concerns being raised by BIAC and others. Chairman Ryan and Chairman Hatch state clearly that it is the responsibility and authority of the Congress to craft tax rules that work best for US companies and the US economy.

The BEPS process highlights the need for effective consultation by the Treasury Department with Congress. The importance of effective consultation will only increase during the implementation process as administrative actions are considered and legislative proposals are being developed. Just as the Administration is consulting effectively with Congressional leaders on trade promotion authority legislation, we need a similar level of dialogue on the critical tax policy issues that are being considered as part of the OECD BEPS Action Plan.

All of these concerns convince me that the best way for the United States to address the potential problem of BEPS continue to be the enactment of comprehensive tax reforms that lower the corporate rate to a more internationally competitive level and modernize the badly outdated and uncompetitive US international tax structure.

An understanding of the full adverse impact of today's US tax rules must begin by acknowledging that the United States has the highest <u>statutory</u> corporate tax rate among major global economies.

The top US statutory corporate tax rate, including the average state corporate income tax, is 39.0 percent, more than 14 percentage points higher than the 2015 average (24.6 percent) for other OECD countries, and more than 10 percentage points higher than the average (28.4 percent) for the other G7 countries.

For U.S. companies seeking to do business around the world, the outdated tax policy reflected in today's tax code is a barrier to success and leaves America falling further behind.

And when I say outdated, I'm not talking about the way we typically think of the term – as in having an iPhone 4s instead of the new 6 or 6-plus. When I say our international tax policy system is outdated, I'm talking about an architecture dating back to the 1960s.

The global economy has changed enormously since the 1960s. In 1960, US-headquartered companies comprised 17 of the world's largest 20 companies. By 2014, just six of the top 20 companies were headquartered in the United States.

Globalization – the growing interdependence of countries' economies -- has resulted from increasing international mobility and cross-border flows of trade, finance, investment, information, and ideas. Technology has continued to accelerate the growth of the worldwide marketplace for goods and services. Advances in communication, information technology, and transportation have dramatically reduced the cost and time it takes to move goods, capital, information, and people around the world. In this global marketplace, firms differentiate themselves by being nimble around the globe and by innovating faster than their competitors.

Just as the global economy has changed, tax systems around the world have also evolved. Governments in the developed and developing world have adopted policies that reflect a changing view of corporate income taxes. This modern view may have been occasioned by economics or practicality, but as I will discuss, the result is a growing gap between the United States and the rest of the world.

Every other G7 country and 28 of the other 33 OECD member countries have international tax rules that allow their resident companies to repatriate active foreign earnings to their home country without paying a significant second layer of domestic tax. This approach, sometimes referred to as a "participation exemption" or "dividend exemption" tax regime, differs markedly from the US worldwide tax system, in which the foreign earnings of US companies are subject to US corporate tax with a credit for taxes paid to the foreign jurisdiction.

The United Kingdom and Japan, in 2009, became the most recent major economies to adopt territorial tax systems, leaving the United States as one of the last modern economies that has not adopted this type of tax system. Of the 28 OECD countries with modernized international tax systems, only two – New Zealand and Finland – have reverted to worldwide tax systems, and both nations subsequently switched back to territorial tax systems.

With the highest statutory corporate tax rate among OECD countries and a corporate income tax that repels repatriated foreign earnings, US-based multinationals have a significant incentive to keep their foreign earnings abroad. Audit Analytics reports that over $2 trillion of

accumulated foreign earnings of public US companies has been identified as permanently reinvested abroad. While a substantial amount of these earnings have been reinvested in foreign operations, many companies have cash and liquid assets that would be reinvested here in the United States but for the outdated US tax rules.

A proper focus on removing the barriers to US companies repatriating earnings from their foreign operations back to the United States also would put to rest the notion that the foreign earnings of these US companies are somehow 'stateless' income. Under the current US worldwide tax system, the United States retains the right to tax the foreign earnings of US companies, but delays the imposition of tax until the income is repatriated.

The key reason unrepatriated income exists in many cases is that our high US tax rate and worldwide system combine to make reinvesting abroad much more attractive. A fair assessment of this fact also should result in an acknowledgement that much of this unrepatriated income is invested in the brick and mortar operations of US companies operating in countries around the world. That is why I provided different repatriation tax rates for cash assets and hard assets in the international reforms that I proposed last year as part of my comprehensive tax reform bill.

A modernized tax system similar to those in other advanced economies would encourage US companies to reinvest their foreign earnings in the United States by removing the current repatriation tax that only US headquartered companies must pay, putting domestic investments on a par with reinvestment abroad and also putting US headquartered companies on par with foreign headquartered companies.

Beyond just adopting territorial systems, an increasing number of countries are acting to provide "patent boxes" and related incentives for innovation. As Dr. Laura Tyson, former Chair of President Clinton's White House Council of Economic Advisers, noted in her recent testimony before the Senate Finance Committee, other countries "are using tax policy as a 'carrot' to attract the income and operations of US companies with significant intangible assets and the positive externalities associated with them – including the spillover effects boosting innovation, productivity, and wages." That is one reason why I included a "carrot" for intangible income earned from foreign market sales by US companies as part of the tax reform bill that I introduced last year.

The United States is operating in a global economy that increases both the competition American businesses and workers face and the opportunities available to them. As President Obama noted in his State of the Union address, 95 percent of the world's customers reside outside the United States. These foreign customers represent 80 percent of the world's purchasing power.

US businesses can't serve those rapidly growing markets by staying home. Reforming our tax laws to help our businesses better compete abroad increases the value of the assets of American companies and leads to increased American jobs. Delaying reform will mean that US businesses will be disproportionally impacted by a BEPS project that results in broadening the

amount of business income subject to tax if the United States continues to have its high corporate tax rate and worldwide system of taxation.

So, here we sit. We know America needs tax reform, and we know we need it now.

That brings me to some questions I often am asked. Do I think tax reform is possible? Why should we spend our time evaluating the impact of tax reform proposals and engaging in dialogues with Congress and the Administration if nothing is going to happen?

It would be easy to say that this Congress isn't going to do anything. It's easy to say tax reform isn't happening anytime soon, so we might as well not undertake the hard work of developing a constituency for tax reform or contribute ideas on what tax reform should look like.

But, I would also note, it is easy to be wrong. My personal view is that 2015 is a very important year for tax reform, notwithstanding the political challenges.

Keep in mind that President Obama was more forward-leaning in his State of the Union than he has been in years past. In February, President Obama included more tax reform details in his budget than in the past. And Treasury Secretary Lew's testimony before the Ways and Means Committee and the Senate Finance Committee seems to suggest an "open door" on tax issues. Reports indicate he is engaged more than in years past.

Some recent events give me hope that this new Congress can achieve some progress on tax reform this year with this new Congress.

For example, you can be sure that doctors who care for Medicare patients would have had good cause to doubt that Congress would ever permanently "fix" a physician pay system that has required 17 temporary "doc fix" measures since 1997. And yet, legislation permanently reforming the Medicare physician pay system was recently signed into law by President Obama. And what may be even more astounding is that the legislation was the product of bipartisan negotiations between Speaker Boehner and Leader Pelosi.

The Senate also recently approved a bipartisan agreement on Trade Promotion Authority, a plan to grant the President the ability to negotiate trade agreements with the guarantee of an up-or-down Congressional vote. One never knows until the votes are counted but House Republican leaders are optimistic that Congress later this month will provide a US President with enhanced trade negotiating authority for the first time since 2007.

Let's take a look at past history in trying to identify a path to tax reform in this Congress. Senate Finance Chairman Hatch recently noted that enacting the Tax Reform Act of 1986 represented a three-year legislative effort. On several occasions over that period, most participants concluded that reform efforts would not succeed, but they were wrong.

What was a three-year, bipartisan effort in '86 – before Twitter, before Facebook, before email and Gmail, before cable news – clearly today, is taking more time. And while tax reform may eventually happen in a more partisan way, right now it is too early to say whether a

Republican-controlled Congress can pass a tax reform bill in 2015 that a Democratic President will sign.

The fact is we just don't know.

What we do know is that just over a year ago, I released the most comprehensive rewrite of the tax code since 1986. That was a multi-year effort in and of itself.

At its core, my objective was to offer a serious proposal to make the tax code simpler and fairer for hardworking taxpayers. The legislation proposed to make the Code more effective and efficient by getting rid of narrowly targeted provisions to lower tax rates across the board for both individuals and corporations. This was to enable small and large businesses alike to expand operations, hire new workers, and increase benefits and take-home pay.

Over the four years that preceded my introduction of the Tax Reform Act of 2014 as H.R. 1, the Ways and Means Committee held over 30 public hearings, including the first joint hearings with the Senate Finance Committee on tax policy since World War II. Ways and Means Ranking Member Sandy Levin – my home state colleague – and I formed 11 bipartisan working groups to tackle different areas of the tax code. In that time, I also launched TaxReform.Gov, which received more than 14,000 public comments and suggestions, while then-Senate Finance Committee Chairman Max Baucus (D-MT) and I escaped the confines of Washington, DC to go out and talk with taxpayers all across the country.

In the process, tax reform went from just a handful of us talking about it to one of the dominant debates in Washington. The debate went from about "whether" to do tax reform to "how" to do tax reform.

Because of the active input from the US business community and the strong interest of many members of Congress, numerous Congressional hearings, bipartisan working groups, discussion drafts and white papers in both the House and Senate – a solid foundation has been built for tax reform.

In 1985, then Ways and means Chairman Dan Rostenkowski famously said, "Don't let yourself get misled…the tax reform train is moving…and there's a real danger that doubters will be left behind at the station."

His words still ring true today.

We know that the two new Chairmen of the tax writing committees want to do tax reform. While we don't know when they will complete this project, make no mistake – a new tax code is being built in Washington.

That is why I believe 2015 is a very important year for tax reform. With our economy growing at a slow pace since the end of the recession six years ago, , we simply can't wait longer to reform our tax laws to promote more, better-paying jobs here at home and make US businesses more competitive globally. 2017 or 2018 is too long for the American people to wait.

Independent economists agree: well-designed tax reform results in stronger economic growth, more jobs, and higher wages. When I proposed a comprehensive tax reform last year,

independent, non-partisan analysts at the Joint Tax Committee projected that it could increase the size of our economy by up to $3.4 trillion – that's equivalent to 20 percent of today's economy.

Based on that stronger growth, JCT staff estimated that we could see up to 2 million new jobs created, and there could be up to $700 billion in additional federal revenues that could be used to lower taxes even further or reduce the debt.

From a business standpoint, we must have tax reform. The current system tilts the playing field against US companies competing for acquisitions of foreign companies and US companies with foreign operations. Our current worldwide tax system essentially places a premium on the value of US companies' assets in the hands of a foreign bidder.

The recent wave of inversions and foreign takeovers show that, one way or another, individual businesses will seek to accomplish "tax reform" for themselves. But allowing that trend to continue represents a failure of Washington to protect the U.S. economy, the jobs it creates, and the families those jobs support.

In the absence of action by Congress to enact a more competitive US tax system, there will be an increase in the pace of US companies being acquired by foreign competitors, and that is something the American people will tolerate for only so long.

For all of these reasons, I introduced my comprehensive tax reform proposal, H.R. 1, last year. I still believe that real tax reform, that benefits all of us, is within reach if we all work together. It may take longer that we would like, and it may be accomplished in stages, but it can done. I hope you share my belief, and we can all continue to work together to make tax reform happen.

Thank you for inviting me to speak to you today.