COALITION for a PROSPEROUS AMERICA

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April 23, 2021

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

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

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

Re: International Taxation Overhaul Framework

Dear Senator Wyden, Senator Brown, and Senator Warner:

Thank you for your efforts to address the inequality in our corporate tax code and ensuring mega-corporations pay their fair share.[1] On behalf of our domestic manufacturing, agricultural and worker members, we would like to provide suggestions to your framework.

1. **End Tax Avoidance with Sales Factor Apportionment**

The persistent problem of profit shifting is a fundamental flaw in our current system. It causes massive tax avoidance and incentivizes offshoring of production. We don't think it can be corrected without the taxation of profits based upon the destination of sales in a sales factor apportionment system.

Three difficult problems are at the core. First, the tax system wrongly distinguishes between US and foreign headquartered companies. This distinction simply should not exist because it is economically insignificant and is an avenue to game the system. The domicile distinction generates tax competition, foreign buyouts and inversions.

Second, the US tax system treats every subsidiary of a company as independent and separate. The SEC, company managers, and shareholders, in contrast, properly consider the whole company as a single, economic whole. Absent the distorting incentives of our tax system, the complex subsidiary structure of many multinationals would make no business sense. This should end.

Third, the current physical presence test should end. It is an outdated concept created in the early 20th-century when it seemed obvious that a company could not profit through sales in the US

[1] https://www.finance.senate.gov/imo/media/doc/040121%20Overhauling%20International%20Taxation.pdf

without being located here. Because companies can indeed engage in substantial sales here without a physical presence, the physical presence requirement is an offshoring incentive because it creates a loophole in favor of overseas corporations. The rise of e-commerce and the pandemic revealed how little US commerce relies on a physical presence.

Taxing based upon the destination of sales through sales factor apportionment solves these three core problems. The multinational parent and its subsidiaries are treated as a group. The group's attributed total net profits are based on the percentage of sales they make to the United States. The domestic vs. foreign headquarter distinction is eliminated. Profit shifting issues are eliminated because the sales that matter are sales outside the corporation group. Internal transactions do not matter. Digital and other similar concerns no longer apply as the physical presence test is replaced with an economic test.

The sales-based formula does not include capital or labor taxation so there is no longer a tax incentive to locate production outside the United States. Tax rests solely on participation in the large US market. Congress could embrace this simpler and fairer tax system, allowing all multinationals to pay US taxes – just like American domestic companies.

However, your current proposed framework does not include any suggestions towards this system, so we would like to address the proposals of the framework specifically.

2. **GILTI: Country-by-Country reporting and ending QBAI**

We agree the Global Intangible Low-Taxed Income (GILTI) system insufficiently addressed the multinational corporate tax avoidance issues. The most prominent companies in the world still have incentives to offshore jobs and stash profits in tax havens.

Therefore, we support repealing the Qualified Business Asset Investments (QBAI) deduction. QBAI incentivized corporations to invest their profit in overseas production. The US tax code should not incentivize factory creation overseas. The system should spur investment in the US, not in foreign countries.

Additionally, the GILTI regime allowed a mechanism known as jurisdictional "blending." Companies can avoid GILTI liability on their tax haven operations using tax credits from higher-tax countries. GILTI liability permits the blending of tax haven reporting with higher tax jurisdiction reporting, rendering it dysfunctional.

Therefore, we support the effort to calculate the GILTI minimum tax on a per-country basis. With every country out there competing in various ways for the tax "Race to the Bottom," the US must have an effective system.

The suggested framework proposes a dual basket approach to simplify the attribution of GILTI. We believe this proposal provides more tax avoidance opportunities. No company pays the statutory tax rate. Multinational corporations can incentivize other countries to compete using unaccounted-for methods to reduce their effective corporate tax rate.

A per-country basis allows the IRS to tailor GILTI regulations to the jurisdiction. The simplified dual-basket approach leaves open the possibility for manipulation. A country in the high tax basket could implement a new tax incentive that effectively puts it in the low-tax basket, but not right away. If the law does not allow immediate flexibility to recognize the tax game, the avoidance will exist for several tax years before the code/regulations are corrected. In the meantime, another multinational will gain an advantage over domestic companies. For this reason, we argue the per-country basis is better but sales factor apportionment is best.

3. **The BEAT must be replaced.**

We understand the incentive to retain the Border Erosion Anti-Abuse Tax (BEAT) and rework the calculations suggested in the framework. However, the Cost of Goods sold exemption cannot be resolved. The BEAT was too limited in scope to achieve the promised return, with too many detrimental effects to consider keeping. The promise to protect from foreign multinational corporations' profit shifting never materialized. But the Cost of Goods exemptions is vast and was going to reduce the effectiveness. The effort to add another tax bracket on the BEAT is not only more complex but fails to address this issue.

With a small inversion exception, the BEAT does not apply to payments for the cost of goods sold. Accounting advice routinely recommended increasing the cost of goods sold on financial statements to avoid the BEAT tax.

Congress should not be implying that simple reallocation of profits to different categories in a foreign subsidiary is a permissible use of the US tax system to profit shift sales from American customers. We see more strength in the Made in America tax alternative.

We still have concerns about the Made in America tax of Stopping Harmful Inversions and Ending Low-tax Developments (SHIELD). Tying the application of SHIELD to the OECD Pillar 2 negotiations leaves it at the mercy of foreign tax havens.[2] SHIELD will only work if it is close to the corporate tax rate. Again, we argue for the superiority of a sales factor method.

4. **FDII alteration should benefit American domestic companies.**

We support altering the Foreign-Derived Intangible Income (FDII) to focus on rewarding domestic jobs and businesses. Ending the benefits of rewarding offshoring is paramount to any alteration combined with incentivizing American ingenuity. Ending the QBAI elements in FDII and tying the benefit to annual US innovation are significant changes if FDII must be retained.

Please consider these recommendations as you work to solves these complex international tax issues. And remember, domestic companies' competitiveness is vital for a successful rework of the code. We would also be happy to discuss Sales Factor Apportionment further at your earliest convenience.

Sincerely,

Zach Mottl, Chairman
Coalition for a Prosperous America

Michael Stumo, CEO
Coalition for a Prosperous America

[2] Johnston, Stephanie Soong and Strocko, Kiarra M. "Global Tax Reform Deal Must Respect Irish Rate, Donohoe Says" Tax Analysts, Doc 2021-16512, April 22, 2021.