

Reckoning day: Firms stuck with tab

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Of the \$353 billion in new business taxes in President Barack Obama's 10-year budget plan, about two-thirds — \$234 billion — is aimed at just three targets: hedge funds, foreign firms and U.S. companies that play on the world stage.

It's a day of reckoning long in coming, as Democrats have repeatedly sought to pick the corporate pockets to help pay for new programs, only to be thwarted by Republicans and George W. Bush.

John Castellani, president of the Business Roundtable, acknowledged that major corporations knew they would become prime tax targets, given past congressional battles and presidential campaign rhetoric.

"The surprise was the magnitude of the numbers," he said.

Now all three groups are mobilizing their members, updating talking points and heading to Capitol Hill to try to limit the damage.

They also have a few chips to play with the new administration, since Obama will rely on hedge funds to clear bad bank debt and foreign firms could play a key role in launching a new alternative energy sector.

Hedge funds

After years of operating in the shadows, hedge fund managers appear to have the most work ahead of them as they come under the congressional spotlight.

Former Rep. Richard Baker (R-La.) was hired a year ago to lead the Managed Funds Association, representing global hedge funds that manage about \$1.5 trillion in investments.

Because of the funds' high-risk nature, government regulators have tried to limit their ability to recruit working families, and the funds aren't required to disclose much about their operations. Some rules even prohibit disclosures, using language so hazy that some funds fear posting their staff profiles could violate them.

"All of that helps to characterize the industry in an unfortunate way," a bemused Baker said.

It also allows adversaries to fill in the gaps. Democrats have long painted hedge funds as secretive bands of billionaires making bundles of cash by exploiting loopholes in the rules.

Baker is working to change that image, preparing documents that show how many pension funds and university endowments are managed by hedge funds. And he's hired more staff and revamped the association's website.

He's also developing a state-by-state, district-by-district analysis showing the institutions from Louisiana to Oregon that rely on hedge fund managers, with a goal of making the industry less New York-oriented and more relevant to lawmakers and their constituents.

With his one-year moratorium on lobbying Congress now expired, Baker is taking those materials — along with a newly prepared “readable” synopsis of the complex role of hedge funds in the economy — to meetings with his old colleagues.

“We need to be more engaged at the table in telling our story,” he said. “It would have been advantageous to start earlier.”

That's particularly so, given that Obama's budget seeks to close what some Democrats argue is a gaping hole in the tax code related to the funds.

Hedge fund managers are paid a share of the profits on investments, which is called carried interest. That money is currently taxed at the 15 percent capital gains rate; Obama wants to count it as income, which would subject it to much higher tax rates.

The White House estimates that the tax tweak could generate \$24 billion in the next decade.

Baker seems resigned to some form of the proposal passing, but he wants to ensure that other investment outlets — from venture capitalists to real estate developers — share some of the pain. “We understand that some discussion of taxes will occur,” he said. “We just want to be in the room.”

His bigger fear, however, is any new industry regulations that Congress might pass. “We're very concerned we not have a regulatory environment that would not allow our businesses to do what they need to do,” he said, noting that too much regulation could rob Obama of a strong ally in his economic recovery efforts.

Foreign firms

Nancy McLernon heads the Organization for International Investment, which represents U.S. subsidiaries of foreign firms such as Sony, Nestle, Toyota and Food Lion. And she's in better shape than Baker simply because her clients have already endured congressional battles.

She only needs to update the localized data on jobs for House districts and Senate seats and spread the word to the slew of freshmen now in Congress.

“Five million Americans work for foreign subsidies, which is about 4 percent of the national work force” is more mantra than talking point to McLernon.

Her challenge is that she doesn't know yet just how Obama's budget proposal might affect her member companies.

The administration estimates that a whopping \$210 billion will be raised over the next 10 years from “international enforcement, reform deferral and other tax reform policies.”

“The devil's in the details, and we don't know what's in it,” she said. “But I have been around long enough to know that if we don't tell our story, someone else will.”

Her organization has already scheduled a March 31 briefing with senior congressional staff on international taxes and moved its annual meeting to Washington this year.

McLernon's worries are fueled in part by the whiff of isolationism already in the air on Capitol Hill.

When Congress slipped a Buy American provision into the stimulus bill, McLernon got calls from 10 foreign embassies the next day, demanding to know what it meant and whether the United States would set off a wave of global retrenchment.

She's also on guard for some old battles to reignite.

Congress has tried before to raise taxes on foreign-based insurance companies, and their domestically owned competitors are now pressing for such action again. The staff of Senate Finance Committee Chairman Max Baucus (D-Mont.) is reviewing the idea, which could generate billions of dollars in new revenue.

While the legislation would be narrowly tailored to insurance, it would draw widespread opposition from other sectors worried they might be next.

If it passes, McLernon suggested, foreign firms may decide to relocate their U.S. operations to friendlier environments. “Jobs could disappear,” she warned.

Such a legislative shift also could thwart Obama's goal to see millions of new jobs created in the alternative fuel sector, she said.

Foreign-based energy firms are further ahead in developing that technology. During the presidential campaign, both Obama and his Republican rival John McCain appeared at wind power subsidiaries owned by foreign firms.

If those firms believe the U.S. tax code may someday give domestic competitors an advantage, they could become reluctant to set up operations here and fuel the economic revolution that the president envisions.

U.S. internationals

Unlike McLernon, Castellani knows that a healthy proportion of the \$210 billion in proposed international tax fixes is aimed at members of the Business Roundtable, which represents some of the biggest firms in the United States.

In his nationally televised address before Congress last month, the president vowed to stop rewarding companies that move jobs overseas, which is code for promising to end their ability to defer payment of U.S. taxes on profits earned and held by their overseas subsidiaries until the money is transferred into domestic accounts.

Business argues that the deferral is important because those profits would be doubly taxed without it — once by the foreign government, then again by the United States.

It's a perennial fight between Big Business and Democrats that now favors the politicians. But an apparent victory by Congress in a fight over how best to keep jobs here could have unintended consequences, Castellani and his influential pool of CEOs will argue in private meetings with lawmakers.

“If you get rid of the deferral,” Castellani said, “the only way to stay competitive is to move the company overseas.”