ORGANIZATION *for* INTERNATIONAL INVESTMENT
Global Investment Grows America's Economy

July 22, 2014

The Honorable Ron Wyden
Chairman
Committee on Finance
United States Senate
Washington, DC 20510

The Honorable Orrin Hatch
Ranking Member
Committee on Finance
United States Senate
Washington, DC 20510

The Honorable Dave Camp
Chairman
Committee on Ways and Means
United States House of Representatives
Washington, DC 20515

The Honorable Sander Levin
Ranking Member
Committee on Ways and Means
United States House of Representatives
Washington, DC 20515

Re: Proposals to Further Limit Corporate Expatriations

Dear Senators Wyden and Hatch and Representatives Camp and Levin:

On behalf of the Organization for International Investment (OFII), I write to express our significant concerns with the management and control provisions included in S. 2360 and H.R. 4679, legislation to limit corporate expatriations (the Stop Corporate Inversions Act of 2014). These provisions, if enacted, would inadvertently discourage foreign investment in the U.S. economy and jeopardize American jobs.

OFII is a business association representing the U.S. subsidiaries of many of the world's leading global companies. The U.S. subsidiaries of companies based abroad directly employ 5.6 million Americans and support an annual U.S. payroll of over $400 billion. OFII works to ensure the United States remains the top location for global investment. As such, OFII advocates for fair, non-discriminatory treatment of foreign-based companies and promotes policies that will encourage them to establish U.S. operations, increase American employment, and boost U.S. economic growth.

Generally, the proposals in both the Senate and House versions of the Act would treat any foreign corporation as a U.S. corporation if it acquires, after May 8, 2014, the properties of a U.S. corporation or partnership if either (i) after the acquisition, the former shareholders of the U.S. corporation or partnership own more than 50% of the stock of the foreign corporation, or (ii) the group of companies that includes the foreign corporation is primarily managed and controlled in the United States and has significant domestic business activities.

OFII strongly opposes the inclusion of management and control provisions in the Stop Corporate Inversions Act. These provisions, if enacted, could essentially – and inappropriately so – introduce a subjective management and control test for corporate residence into U.S. tax law, jeopardizing American jobs and undermining foreign direct investment. The provisions go beyond the intended scope of the legislation to limit corporate expatriations of U.S.-based companies and instead discourage foreign-based multinationals from allocating global resources to the United States.

Historic Foreign Companies Inadvertently Impacted

Many U.S. subsidiaries with foreign headquarters have significant business activities in the United States, which may include some senior-level management personnel. These management level jobs are of great benefit to the U.S. subsidiary and encourage additional investment in the United States. Under the proposal, if such a foreign-parented group makes an acquisition of a U.S. business – however small – such acquisition could cause the foreign parent of the group to be treated as a U.S. corporation for tax purposes. This creates a clear disincentive to invest and locate global executives or management functions in the United States.

Many multinational companies structure management along regional business units or business lines. For example, a non-U.S. multinational may have operations in multiple countries around the world, including in North and South America. Such companies often decentralize management along regional lines, so that management of the Americas may take place through a regional headquarters located in the United States. Similarly, a multinational with several distinct lines of business may have a line of business that has significant operations in one or more North American countries, so that the business unit's headquarters is located in the United States. Such companies may also serve as regional headquarters for supply chain management and research and development functions.

High Paying Management Jobs and Connected Functions Would Leave U.S.

Each of the structures described above could potentially run afoul of the management and control test, with the result that foreign corporations could potentially and inappropriately become U.S. corporations under the Stop Corporate Inversions Act. As a result, foreign-based multinationals will likely consider moving these senior management jobs and business units outside the United States. The loss of top management of business units will be detrimental to the U.S. economy, since the location of these functions impacts decisions regarding sources of supply and location of employees and key support functions. This means the loss of management jobs may also mean the loss of research and marketing jobs and expenditures, all of which would tend to move higher paying U.S. jobs and support staff outside the United States.

Furthermore, replacing the 100-year-old objective test for corporate residency with a subjective and undefined evaluation of the location of management introduces an unacceptable amount of risk in the audit process for most U.S. subsidiaries of foreign-based companies. The resulting uncertainty surrounding the implementation of the proposed standard, combined with the sweeping penalty for failing the test, will result in companies taking significant steps to adapt. This increases the risk of high-value American jobs moving to other countries and undermining U.S. competitiveness.

Discourages Foreign Direct Investment

Over the past two decades, mergers and acquisitions accounted for over 80 percent of U.S. foreign direct investment inflows.[1] Moreover, IRS data for 2011 shows that U.S. subsidiaries of foreign corporations pay a higher effective tax rate (27 percent) than all active C-corporations (22

[1] From 1992 through 2008, mergers and acquisitions accounted for 90 percent of U.S. foreign direct investment inflows. While this number dropped to 35 percent in 2009 before increasing to 57 percent in 2010 and to 70 percent in 2011, for the full period of 1992 to 2011, mergers and acquisitions still led to 84 percent of U.S. foreign direct investment inflows. *See* Ikenson, OFII Report, *"insourcing Companies: How They Raise Our Game*, Oct. 30, 2013 (available at http://www.ofii.org/sites/default/files/OFIIRaisingOurGame_Full.pdf), citing to reports prepared by the Bureau of Economic Analysis and the United Nations Conference on Trade and Development.

percent).[2] Thus, any rule that discourages foreign-based multinational companies with substantial U.S. operations – the very multinational companies employing millions of American workers – from making additional investments in the United States through mergers or acquisitions will have a stifling effect on overall foreign direct investment in the United States and the jobs and economic activities it generates.

The exception to the inversion rules is overly narrow and will not shield foreign direct investment from the scope of the proposal. The substantial business activities provision is crafted so narrowly, it will essentially never apply to a multinational company with global operations. Recently promulgated Treasury regulations provide that the substantial business activities test will be satisfied only if more than 25 percent of the worldwide group's income, assets, and employees are located in the country of the foreign corporation's organization. These regulations have been heavily criticized as providing an unrealistic threshold in today's global economy, where many multinationals do not have 25 percent of their business in any single country. Not only would the proposed bill codify the 25 percent test; it would permit Treasury to increase the threshold even further.[3]

Invites International Retaliation

The management and control provisions would also invite retaliation from other countries. A unilateral change of corporate residency standards effectively overrides commonly understood norms of international taxation. This perceived encroachment could cause our global trading partners to enact retaliatory taxes against U.S.-based companies with management and control functions in their jurisdictions. Further, the management and control provisions would conflict with U.S. tax treaties because global companies could become dual residents of both the United States and their original country of incorporation and face double taxation.

Accordingly, OFII strongly opposes the inclusion of the management and control test in the Stop Corporate Inversion Act. These provisions go beyond the intended scope of the legislation to limit corporate expatriations in a way that introduces significant harm to high-value American jobs and obstructs future investment by global companies looking to expand and grow in the United States.

Thank you in advance for your consideration.

Sincerely yours,

Nancy McLernon
President & CEO
Organization for International Investment

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2 IRS data available at http://www.irs.gov/uac/SOI-Tax-Stats-Returns-of-Active-Corporations-with-50-Percent-or-More-Foreign-Ownership-Table-24.

3 On the other hand, the requirement in the management and control provision that the company must also have significant business operations in the United States will be equally useless as a backstop to the management and control provisions because it permits Treasury to *reduce* the threshold.