COMMITTEE ON WAYS AND MEANS

U.S. HOUSE OF REPRESENTATIVES
WASHINGTON, DC 20515

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Dr. Douglas Elmendorf
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Congressional Budget Office
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Director Elmendorf,

The Congressional Budget Office ("CBO") exists to provide independent, unbiased and non-partisan analysis for Members of Congress. On January 8, 2013, the CBO released a report entitled "Options for Taxing U.S. Multinational Corporations." I am writing to express my concern and disappointment that this report does not comport with the unbiased analysis Congress expects from CBO. This report purports to provide an even-handed review of different policy issues related to the taxation of foreign source income. However, a closer analysis of the report reveals that it is heavily slanted and biased in favor of one specific approach to the taxation of foreign source income – and relies heavily on sources that tend to support that conclusion while ignoring sources that support a different conclusion.

The report presumes as settled an area of economic theory that is in fact subject to significant controversy -- specifically whether the U.S. system for taxing foreign source income should be consistent with the theory of capital export neutrality or capital import neutrality. The report's presumption that capital export neutrality is the appropriate stance is evident by:

- The process through which the report was subject to outside peer review,
- The academic citations used to buttress the CBO analysis,
- The description in the report (often without citation) of the rationale for and consequences of foreign investment,
- The report's extensive analysis of tax policy options proposed by the Administration, and
- The complete lack of consideration of alternative policy options proposed by Congress.

While the report does not explicitly endorse one policy over the other, the presumptions and contents of the report clearly portray the theory of capital export neutrality as superior and thus results in a significantly flawed report that fails to provide an objective and unbiased analysis to Members of Congress.

The report was peer reviewed by two outside experts, Kimberly Clausing and Stephen Shay. Ms. Clausing's research on this topic – which most recently established the red herring of a "pure territorial" system (which no one is proposing) and then determined that such a system would increase employment overseas – is routinely cited by opponents of territorial tax policy, to the point that her analysis was cited by Vice President Biden in a nationally televised speech at the Democratic National Convention in which the Vice President attacked the concept of territorial taxation. For his part, Mr. Shay previously served as the Deputy Assistant Secretary of the Treasury for Tax Policy (International) in the Obama Administration and authored the very anti-deferral policies proposed by the Administration and reviewed at length in the CBO report. In no way can this be viewed as a balanced review process.

Further, the report includes a number of citations to other academic work to support its analysis and conclusions. A close review of these citations reveals an overwhelming bias to academic work that is critical of the concept of territoriality. For example, Ms Clausing's research is cited six times, far more than another outside analyst. In addition, the report includes 14 other citations to research opposed to territorially, such as the research by Ed Kleinbard, who in 2007 published an article titled, "Throw Territorial Taxation from the Train".

On page 2, the report makes two broad assertions that can only be true if one considers the theory of capital export neutrality to be the correct policy. When describing a worldwide system of taxation the report states, "As a result, those options would generally lead to more economically efficient business investment and increase corporate tax revenues from firms that remained incorporated in the United States." The report further states in its description of a territorial system "Such policies could result in a less efficient allocation of resources among countries by increasing incentives to shift business operations and reported income to countries with lower taxes." This latter assertion is essentially repeated on page 22 when the report states "[Exempting active foreign dividends] would make investment behavior by U.S. firms less efficient by increasing incentives to invest in low-tax countries." Further, on page 22 the report makes a blanket statement that "In general, countries with territorial (or exemption) tax systems collect less revenue, all else being equal, than they would with worldwide tax systems." The report provides no citations or empirical evidence to support such a broad claim.

The report includes an extensive discussion of the tax policy options proposed by the Administration but utterly fails to provide an equal and balanced review of proposals on territorial taxation. The report limits this analysis to one option published by the Joint Committee on Taxation in 2005, eight years ago. This option, however, has never been seriously considered by Congress (largely because it would raise revenue by disallowing deductions for legitimate business expenses, thus creating "stateless expenses" and more closely resembling the principle of capital export neutrality that underlies worldwide taxation). More recently, significant legislation has been introduced in Congress and considered in Congressional hearings. Additionally, in October 2011, the Ways & Means Committee released a discussion draft of comprehensive legislation on the topic of territorial taxation. These alternative proposals contain policy options that would address many of the extensive criticisms of a territorial system described in the CBO report. None of these alternative proposals were addressed in any way in the report. In fact, their existence was not even acknowledged.

It is my understanding that this report reflects analysis that CBO staff had an interest in conducting and that CBO staff essentially "shopped" this analysis in order to find a Senator or Member of Congress who would request CBO to conduct this analysis. In a time of significant budget constraints, it is more than troubling to hear that CBO has sufficient excess resources that its staff can produce reports on policy areas that are not CBO's primary area of responsibility but at the same time requests for analysis of actual legislative proposals in policy areas in which Congress does rely on CBO are substantially delayed.

In light of the concerns raised in this letter, I request that you provide a written response to flaws identified in this report, recommendations for how these flaws can be corrected, and an explanation as to the steps CBO will take in order to avoid producing such flawed analysis in the future.

Sincerely,

Dave Camp

DAVE CAMP
Chairman

cc: The Honorable John Boehner
The Honorable Eric Cantor
The Honorable Kevin McCarthy
The Honorable Cathy McMorris Rodgers
The Honorable Greg Walden
The Honorable James Lankford
The Honorable Lynn Jenkins
The Honorable Virginia Foxx
The Honorable Steve Southerland
The Honorable Ann Wagner
The Honorable Pete Sessions
The Honorable Peter Roskam
The Honorable Paul Ryan
The Honorable Harold Rogers
The Honorable Bill Young
The Honorable Rodney Alexander