WRITTEN TESTIMONY OF TIMOTHY S. HEENAN
VICE PRESIDENT OF TREASURY AND TAX
PRAXAIR, INC.

BEFORE THE

COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

HEARING ON

THE INTERACTION OF TAX AND FINANCIAL ACCOUNTING ON TAX REFORM

FEBRUARY 8, 2012

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Good morning Chairman Camp, Ranking Member Levin and Members of the Committee. My name is Timothy Heenan. I am the Vice President of Treasury and Tax for Praxair, Inc., an American multinational and the largest industrial gases company in North and South America with 2011 sales of $11 billion. The company manufactures, sells and distributes atmospheric, process and specialty gases, and high-performance surface coatings. Praxair products, services and technologies bring productivity and environmental benefits to a wide variety of industries including aerospace, chemicals, food and beverage, electronics, healthcare, manufacturing, metals, among others. Praxair is headquartered in Danbury, Connecticut and its primary research and development facility is located in Tonawanda, New York. Praxair employs about 10,000 people in more than 500 facilities across the United States. My testimony today is based on my experiences working as a senior tax and treasury professional at Praxair for the last seven years and before that as a tax advisor for Ernst & Young.

I would like to thank this Committee for the opportunity to appear at today's hearing on the Interaction of Tax and Financial Accounting on Tax Reform. I would also like to thank the Chairman for his leadership and taking the important first steps toward comprehensive tax reform and the goals of rate reduction and simplification. As a threshold observation, U.S. competitiveness and job creation depend on the U.S. being an attractive place to invest. In this, our corporate tax code plays a significant role.

Today's hearing is focused on how accounting rules affect how publicly traded companies evaluate tax policy. The answer to this question, however, depends on who you ask: If a company's tax director is asked this question, he or she may prefer a lower effective tax rate at the expense of preserving certain "tax expenditures" since a lower rate will increase the company's accounting earnings per share ("EPS"). This should not come as a surprise since most tax directors are measured on their company's effective tax rate. If, however, this question is asked to the individuals who make the company's investment decisions, it is my experience that they will likely be much more focused on cash flow as opposed to accounting EPS. This response will be based on the recognition that cash flow is the key factor in an investment decision. In encouraging cash flow, timing of deductions, such as accelerated depreciation, play a critical role.

Praxair is a capital intensive manufacturer which has operations in over forty countries. Each year, Praxair's various business units from around the world compete with each other for limited funds for capital projects. Projects are selected for funding based on the project's future cash flow using a net present value model. Various factors are used to calculate a project's future cash flow, including the tax profile of the country where the project will be executed. Cash flow is determined by a combination of a country's tax rate, special deductions, and timing items such as accelerated depreciation. Projects yielding a higher cash flow are selected over projects yielding a lower cash flow. Under the current U.S. tax rules, accelerated depreciation, in particular, has a significant impact on Praxair's investment decisions.

Praxair's capital expenditures cannot be deducted in the year they are incurred. Rather, such costs are capitalized and deducted over time. It is important to note that these costs include more than the cost of machinery and equipment, they also include costs associated with labor and engineering. For financial statement purposes, Praxair deducts these costs pro-rata over the life of its projects. The U.S. tax code currently allows for "accelerated depreciation," permitting Praxair to deduct depreciation costs faster than for financial statement purposes. As a result, Praxair can deduct more of the cost of a capital asset in the first years of the asset's life. Shortening the capital recovery period of a U.S. project improves the company's cash flow and makes new domestic investments much more attractive. Better cash flow means more U.S. investment. More investment means greater

American competitiveness and more jobs. On the contrary, when the cash flow of U.S. projects decrease, new capital investments in foreign jurisdictions that offer both lower tax rates and accelerated depreciation become more attractive, thereby shifting capital investment abroad.

Under accounting rules, a tax rate reduction coupled with the elimination of timing items such accelerated depreciation will positively impact a typical company's financial statements by increasing its accounting earnings per share (EPS). That outcome may appeal to a company's tax director, whose performance is largely evaluated on his or her firm's effective tax rate. However, increased EPS does not equate to increased cash flow, which is the sole factor we use to evaluate investment decisions. A lower tax rate will benefit cash flow, but in promoting investment, accelerated depreciation is perhaps a more powerful tool than lower overall tax rates. This is because lower tax rates reward both old and new investment—whereas accelerated depreciation is targeted by only rewarding new investment, which is precisely what we need to restore our competitiveness and economic strength. As the Committee explores rate reduction, I encourage the Committee to weigh the cash flow benefits of a rate reduction versus any potential cash flow harm from eliminating tax expenditures, such as accelerated depreciation. In conducting this analysis, I encourage the Committee to consult with individuals at companies that are making investment decisions, including, but not limited to those firms' Chief Financial Officers and Treasurers.