MAYER • BROWN

Mayer Brown LLP
1999 K Street, N.W.
Washington, D.C. 20006-1101

Main Tel +1 202 263 3000
Main Fax +1 202 263 3300
www.mayerbrown.com

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The Honorable Adrian Smith
Financial Services Working Group
U.S. House of Representatives
Washington, DC 20515

The Honorable John Larson
Financial Services Working Group
U.S. House of Representatives
Washington, DC 20515

The Honorable Aaron Schock
Financial Services Working Group
U.S. House of Representatives
Washington, DC 20515

Dear Congressman Smith, Congressman Schock, and Congressman Larson:

We are submitting this letter in response to the House Ways and Means Committee's request for comments on tax reform proposals. We write to underscore our policy and legal concerns with a number of proposals to dramatically increase taxes on the use of foreign affiliated reinsurance, including the proposal contained in the Administration's FY 2014 Budget. We believe that such proposals violate U.S. obligations under the World Trade Organization's ("WTO") General Agreement on Trade in Services ("GATS"). Many such proposals are discriminatory in nature, thus violating U.S. National Treatment obligations (Article XVII), or impose conditions on access to the U.S. market that are incompatible with U.S. commitments. Enacting such proposals would leave many critical U.S. export sectors vulnerable to WTO-authorized retaliation. It would also damage the ability – and credibility - of the U.S. in its efforts to open foreign markets to U.S. insurance and reinsurance services. Finally, restricting the supply of reinsurance products would cause harm to U.S. insurance consumers in certain regions of the country and key sectors of the U.S. economy.

It is possible for the U.S. to utilize the exception in the GATS from national treatment obligations if the measure is merely to safeguard the member's tax base. However, to qualify for the exception, any measure cannot apply (as the GATS states) "in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where like conditions prevail, or a disguised restriction on trade in services."

As a practical matter, this means that a proposal cannot arbitrarily restrict competition and protect domestic servicers; it must be targeted at the problem. Any proposal must legitimately distinguish (via a safe harbor, or other means) between normal risk management practiced by all insurance companies and activity driven solely by inappropriate tax behavior. It must also take into account taxes paid, and the overall tax regime, in the home country of the foreign reinsurer, so as to actually determine whether any inappropriate tax incentives actually exist. And because

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any reinsurance is the movement not only of premiums but also risk (i.e., the future possibility of profits or losses), any proposal must account for claim payouts in a non-discriminatory fashion.

Some have argued that the election contained in the Administration's proposal mitigates any WTO inconsistency. But the election does not cure the violation, it exacerbates it. This is because the election violates U.S. market access commitments (GATS Article XVI(2)(e)), which states that "[i]n sectors where market-access commitments are undertaken, the measures which a Member shall not maintain or adopt… are defined as… measures which restrict or require specific types of legal entity… through which a service supplier may supply a service." Thus, the U.S. cannot condition access through the requirement that an overseas-based company pretend to be a U.S. company for the IRS in order to make cross-border reinsurance sales. The election provision also violates GATS National Treatment obligations, by applying a discriminatory additional level of taxation at the corporate level – unlike their U.S. counterparts. This also does not qualify for the exception, for many of the same reasons as the main provision.

At a time when the U.S. is rightly pressing a number of emerging markets to maintain competition in the insurance sector, meeting our WTO commitments in the financial services arena is critically important. In addition, these are the export markets the U.S. needs to meet the President's goal of doubling U.S. exports.

In short, now is not the time to have a retreat in global U.S. leadership in the services sector. Whether it is in the context of "pay-fors" or as a part of a larger reform of the U.S. tax code, WTO obligations and the U.S. commitment to competition in the marketplace should be of paramount importance. We hope and trust you will keep these considerations in mind.

With best regards,

Mickey Kantor

Susan C. Schwab