Statement of the National Foreign Trade Council for the Record
House Ways and Means Committee
Subcommittee on Select Revenue Measures
Hearing on Expiring Tax Provisions
April 26, 2012

The National Foreign Trade Council (NFTC) welcomes this hearing and urges Congress to act, as soon as possible, on legislation to extend a number of pro-growth, pro-competitiveness tax provisions that expired at the end of 2011. Given the uncertainty created by not knowing what the state of the law may be and given the competitiveness pressures of the global marketplace, an immediate and seamless extension of these provisions will provide immediate benefits to the U.S. economy.

The NFTC, organized in 1914, is an association of some 250 U.S. business enterprises engaged in all aspects of international trade and investment. Our membership covers the full spectrum of industrial, commercial, financial, and service activities, and we seek to foster an environment in which U.S. companies can be dynamic and effective competitors in the international business arena.

NFTC members believe that pro-growth tax law changes will go a long way to shore up business confidence and promote U.S. economic growth and job creation. We urge Congress to adopt a bill that can be enacted as soon as possible and signed into law by the President that includes the following provisions that expired at the end of 2011:

The "CFC Look-Through" Rules

We support the extension of the law that allows "look-through" treatment for payments of dividends, interest, rents and royalties between related controlled foreign corporations. Without this provision American companies are subject to U.S. taxation when they redeploy foreign earnings from active business operations in foreign markets. Foreign businesses competing in the same markets pay no such tax to their home countries. Without the extension of this rule, American companies will remain at a competitive disadvantage in serving foreign customers and consumers.
The United States taxes U.S. companies on their worldwide income, but the general rule is that foreign subsidiary income is not taxed by the United States until the subsidiary earnings are brought back to the U.S. parent, usually in the form of a dividend. In 1962, Congress imposed immediate tax on “passive” subsidiary earnings. In a very general sense, Congress wanted to prevent companies from forming foreign subsidiaries for the purpose of “parking” portfolio investments out of the tax collector’s reach.

Since 1962, the general rule has deferred taxation of “active” business income from operations conducted in a single foreign country. In the past, the law taxed currently dividends, interest, rents or royalties paid from one foreign affiliate to another located in a different country as passive income. If the two subsidiaries were in the same country, current U.S. taxation did not apply.

Since 2006 Congress has permitted the active earnings of foreign affiliates of U.S. companies to be redeployed between those affiliates without current tax. This rule expired at the end of 2011. The traditional model for operating a global business has changed significantly over the last 40 years. Today’s global economy is significantly different from the environment that existed when these rules were first introduced in 1962. In today’s world, it makes no sense to impose income tax when U.S. companies want to fund the operations of a subsidiary in one country from the active business earnings of a subsidiary in a second country. Foreign-based companies in territorial jurisdictions pay no such tax.

For example, U.S. manufacturers typically establish specialized manufacturing sites, distribution hubs, and service centers. As a result, each related-party entity serves a very specialized function. Without an extension of this so-called “look-through” rule, U.S. tax law would inappropriately increase the cost for these foreign subsidiaries to serve their customers in a very competitive business environment. Foreign competitors do not pay current tax on these related-party payments of dividends, interest, rents and royalties.

Unless the look-through rule is extended, American companies will be at a material competitive disadvantage as compared to foreign-based companies. Suffering current U.S. taxation of active business income when subsidiaries make cross-border payments while the foreign competition pays no such tax would penalize U.S.-based multinationals for responding to the opportunity to serve foreign consumers by redeploying active foreign earnings among foreign affiliates.

Subpart F Active Business Financing Income

The NFTC supports extension of the provision that affords the general rule of deferral to the active business income of U.S. financial services companies. The provision-- referred to as the active financing exception-- is essential to the ability of U.S. financial services companies to compete in global markets. It also plays an important role in supporting U.S. exports. The ability of U.S. manufacturers to provide competitive financing for customers has a direct and positive impact on U.S. exports and manufacturing jobs.
Conclusion

The NFTC supports reforming the tax code to improve the competitiveness of the U.S. economy and increase jobs and wages of American workers. While permanent reform is essential, it will take time. In the short term, it is critical that Congress enacts a seamless extension of the business tax provision that expired at the end of 2011.

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