

Hearing on the OECD Base Erosion and Profit Shifting (BEPS) Project

HEARING
BEFORE THE
SUBCOMMITTEE ON TAX POLICY
OF THE
COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES
ONE HUNDRED FOURTEENTH CONGRESS
FIRST SESSION

December 1, 2015

SERIAL 114-TP04

Printed for the use of the Committee on Ways and Means

COMMITTEE ON WAYS AND MEANS

KEVIN BRADY, Texas, *Chairman*

SAM JOHNSON, Texas
DEVIN NUNES, California
PATRICK J. TIBERI, Ohio
DAVID G. REICHERT, Washington
CHARLES W. BOUSTANY, JR., Louisiana
PETER J. ROSKAM, Illinois
TOM PRICE, Georgia
VERN BUCHANAN, Florida
ADRIAN SMITH, Nebraska
LYNN JENKINS, Kansas
ERIK PAULSEN, Minnesota
KENNY MARCHANT, Texas
DIANE BLACK, Tennessee
TOM REED, New York
TODD YOUNG, Indiana
MIKE KELLY, Pennsylvania
JIM RENACCI, Ohio
PAT MEEHAN, Pennsylvania
KRISTI NOEM, South Dakota
GEORGE HOLDING, North Carolina
JASON SMITH, Missouri
ROBERT J. DOLD, Illinois
TOM RICE, South Carolina

SANDER M. LEVIN, Michigan
CHARLES B. RANGEL, New York
JIM MCDERMOTT, Washington
JOHN LEWIS, Georgia
RICHARD E. NEAL, Massachusetts
XAVIER BECERRA, California
LLOYD DOGGETT, Texas
MIKE THOMPSON, California
JOHN B. LARSON, Connecticut
EARL BLUMENAUER, Oregon
RON KIND, Wisconsin
BILL PASCRELL, JR., New Jersey
JOSEPH CROWLEY, New York
DANNY DAVIS, Illinois
LINDA SÁNCHEZ, California

DAVID STEWART, *Staff Director*

JANICE MAYS, *Minority Chief Counsel and Staff Director*

SUBCOMMITTEE ON TAX POLICY

CHARLES W. BOUSTANY, JR., Louisiana, *Chairman*

DAVID G. REICHERT, Washington
PATRICK J. TIBERI, Ohio
TOM REED, New York
TODD YOUNG, Indiana
MIKE KELLY, Pennsylvania
JIM RENACCI, Ohio
KRISTI NOEM, South Dakota
GEORGE HOLDING, North Carolina

RICHARD E. NEAL, Massachusetts
JOHN B. LARSON, Connecticut
LINDA SÁNCHEZ, California
MIKE THOMPSON, California
LLOYD DOGGETT, Texas

CONTENTS

Advisory of December 1, 2015 announcing the hearing

WITNESSES

Panel One

Robert Stack

Deputy Assistant Secretary for International Tax Affairs, U.S. Department of the Treasury

Testimony

Witness Statement [[PDF](#)]

Panel Two

Barbara Angus

Principal, Ernst & Young

Witness Statement [[PDF](#)]

Catherine Schultz

Vice President for Tax Policy, National Foreign Trade Council

Witness Statement [[PDF](#)]

Gary Sprague

Counsel, The Software Coalition

Witness Statement [[PDF](#)]

Martin Sullivan

Chief Economist, Tax Notes

Witness Statement [[PDF](#)]

Hearing on the OECD Base Erosion and Profit Shifting (BEPS) Project

U.S. House of Representatives,
Committee on Ways and Means,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10:04 a.m., in Room 1100, Longworth House Office Building, Hon. Charles W. Boustany, Jr. [chairman of the subcommittee] presiding.

*Chairman Boustany. Good morning. And I want to call this hearing to order.

You might remember this Subcommittee was formerly called the Select Revenue Measures Subcommittee. But, to reflect the central role of tax in the Ways and Means Committee agenda, Chairman Brady and the rest of the Members decided to change its name to the Subcommittee on Tax Policy to give it its rightful position among subcommittees.

I also want to acknowledge the fine work done by the two chairmen before me, Mr. Reichert and Mr. Tiberi, in moving forward the agenda on tax reform. Thank you, gentlemen, for the fine work of leading the subcommittee.

Today the Subcommittee on Tax Policy will examine the final recommendations recently issued by the OECD on their base erosion and profit shifting project.

The alarming increase in foreign acquisitions of U.S. companies over the past decade, and especially in the last year, have exposed the critical and urgent need for tax reform in America. At 39 percent, the U.S. now faces the highest federal and state combined corporate rate in the developed world, which is rapidly draining America of its homegrown innovation and business, and forcing companies to relocate to countries with more business-friendly tax regimes.

Globalization of the business marketplace has created historic opportunities for growth that were previously impossible. U.S. tax policy must account for these changes in this rapidly complex changing environment. Just last week, Pfizer, an American company founded in 1849 in New York City, announced the largest foreign acquisition of an American company in history. That is not the first, nor will it be the last.

Foreign acquisition has been pushed over the line by our broken tax code -- and the last time comprehensive tax reform took place in the United States was 1986. And since then, our international counterparts have capitalized on our lack of action, outpacing us to a debilitating degree in adopting tax reforms needed to attract capital investment.

As international tax regimes have evolved, multinational companies have also evolved to become increasingly savvy in minimizing their overall tax liability. International competition for business and a fiduciary duty to shareholders obligates companies to be proactive. The political and policy hurdles that have prevented tax reform efforts from moving forward seem to pale in comparison to the problem America faces with the mass exodus of American companies through foreign acquisitions.

Since 2001, global economic instability, alongside the increasing mobility of capital and high-value profitable business activities, have served as natural and powerful motivators for international tax reform. The substantial migration of multinational companies to more favorable tax jurisdictions has placed front and center an acute international awareness that there are limits to the tax burdens countries can place on their resident companies before they must seek more favorable tax environment elsewhere.

All the while, the United States has failed to keep with the pace. It is being left behind. Indeed, the need for tax revenue resulted in the push by OECD to launch the BEPS project.

The OECD BEPS project was intended to target limited, overly aggressive tax planning, and resulted in inappropriate tax avoidance. In fact, one key theme of the BEPS project was to eliminate cash boxes. In effect, shell companies with few employees or economic activities, and which are subject to no or low taxes. However, the project quickly expanded into a fundamental rewrite of global tax practices, including those of the United States, in a relatively opaque process outside the reach of U.S. political process.

The OECD's BEPS project recommendations are deeply troubling on a number of levels, not the least of which is the aggressive attempt to impose substantial tax policy changes on the international community under the guise of eliminating so-called harmful tax practices to ensure multinational companies pay their "fair share" of taxes owed in the jurisdictions in which they operate. This is a highly subjective standard set by the OECD that seems to unnecessarily target American companies, while also disregarding the detrimental impact these recommendations will have on U.S. companies that currently operate under the worldwide system of taxation observed in the U.S.

The BEPS project may have been motivated by an underlying belief that creating a business-friendly tax regime to attract business investment to one's country is itself an illegitimate and harmful practice that must be eliminated. But the BEPS project ended up making recommendations that will achieve the opposite result, by encouraging countries to create patent boxes, which will effectively force worldwide companies to shift their business operations out of the United States in the absence of change.

Moreover, the exposure of American companies' highly sensitive information through the country-by-country reporting requirements within BEPS' recommendations are not constrained by any rationale for the breadth of information required, and are also lacking appropriate protections for highly-sensitive information in this regard.

The BEPS project final recommendations issued this year, coupled with the present European Commission investigation into alleged receipt of illegal state aid by mostly American companies, exposed what appears to be an extremely disturbing and multifaceted attack specifically targeted at American companies.

Ladies and gentlemen, we are out of time. We have nearly three decades of inertia with regard to tax reform. This must be the Congress of action that takes the tough but necessary steps to reform our tax code for the sake of American families, American companies, and America's stature as the world's leader in fostering innovation and business growth.

*Chairman Boustany. And, with that, I will yield to my ranking member, Mr. Neal, for an opening statement.

*Mr. Neal. Thank you very much, Mr. Chairman. And congratulations on your new post. A reminder that I have now either been the chairman or the ranking member with the three people sitting to my right. So I provide some institutional anchor to the conversation that we are about to have.

Our tax subcommittee has a long and rich bipartisan history of coming together to address some of the nation's biggest problems. We have worked together in the past, and I hope to continue to work together on tackling very important issues of this day. Thank you for calling this important hearing on OECD's base erosion and profit shifting project. The timing could not be more fitting.

A new wave of inversions has gripped the corporate world, as yet another U.S. multinational has renounced their U.S. corporate citizenship. In a record-setting \$160 billion deal, Pfizer and Allergan -- and a reminder, Allergan was also formerly an American company -- have agreed to merge and create the world's largest pharmaceutical company. With this merger, the U.S. tax base continues to erode. Perhaps this latest inversion will prompt Congress to come together on reforms so this does not continue to happen.

These inversions happen because of a broken tax code which allows these deals to take place. Congress must take action immediately, as we did in 2004, with legislation that I sponsored, to stop the flow of inversions until we can meaningfully fix our broken tax code.

Our rudimentary tax code remains ill-equipped to handle our increasingly globalized and digital economy. As a result, we have seen an explosion of multinational companies shift profits, activities, and property from high tax countries to low tax countries. By OECD's best guess, countries are losing as much as \$240 billion a year in lost revenue.

I want to commend the Obama Administration, Secretary Lew, for their efforts in working with the international community and finding common-sense solutions to address these taxation challenges. I look forward to the hearing, the testimony from our distinguished panelists, on the best ways to address the challenges ahead of us, and to ensure that the OECD process is not one where our jurisdictions try to grab revenue that rightly belongs to the United States.

But ultimately, the task of fixing our tax code falls on us, specifically on this Subcommittee. Mr. Chairman, it is my hope that we can use this hearing as a springboard toward meaningful reform, one that broadens the base, lowers the rate in a revenue-neutral way, as the Obama Administration has proposed.

Thank you, Mr. Chairman.

*Chairman Boustany. I thank the gentleman. Today we will hear from two panels comprised of experts on international taxation. I am very excited to have these panelists, who are all well-known experts in this area.

Our first panel will be Mr. Robert Stack, deputy assistant secretary for international tax affairs, U.S. Department of Treasury.

Mr. Stack, thank you for being here today. We appreciate the fine work you have done over the years, and we look forward to hearing your testimony. Rest assured the committee has received your written statement. It will be made part of the formal hearing record. We ask you to keep to five minutes on your oral remarks, and you may begin when you are ready.

STATEMENT OF ROBERT B. STACK, DEPUTY ASSISTANT SECRETARY FOR INTERNATIONAL TAX AFFAIRS, U.S. DEPARTMENT OF THE TREASURY

*Mr. Stack. Chairman Boustany, Ranking Member Neal, and distinguished members of the subcommittee, I appreciate the opportunity to appear today to discuss some key international tax issues, including the recently-completed G20 OECD base erosion and profit shifting -- or BEPS -- project. We appreciate the committee's interest in these important issues.

In June 2012, the G20 Summit in Los Cabos, Mexico, the leaders of the world's largest economies identified the ability of multinational companies to reduce their tax bills by shifting income into low and no-tax jurisdictions as a significant global concern. They instructed their governments to develop an action plan to address these issues, which was endorsed by the G20 leaders in St. Petersburg in September 2013. The project came to fruition with the submission of the final reports to the G20 this fall.

The BEPS reports cover 15 separate topics. Some reports, such as those on the digital economy and controlled foreign corporation rules, are more or less descriptive of the underlying issues, and discuss approaches or options that different countries might take, without demonstrating any particular agreement among participants on a particular path. Other reports, such as those on interest deductibility and hybrid securities, describe the elements of a common approach that countries might take with respect to those issues. With respect to transfer pricing,

the arm's length standard was further amplified in connection with issues around funding, risk, hard-to-value intangibles.

And finally, in the areas of preventing treaty shopping, requiring country-by-country reporting, fighting harmful tax practices, including through the exchange of cross-border rulings, and improving dispute resolution, countries did agree to a minimum standard.

I believe that the transparency provided by country-by-country reporting, the tightened transfer pricing rules, and the agreement to exchange cross-border tax rulings will go a long way to curtail the phenomenon of stateless income. Companies will very likely be reluctant to show on their country-by-country reports substantial amounts of income or lower -- in low or no-tax jurisdictions. And the transfer pricing work will better align profits with the functions, assets, and risks that create that profit.

The exchange of rulings will drive out bad practices and shine sunlight on the practices that remain. The improvement of dispute resolution and the inclusion, where possible, of arbitration, will streamline dispute resolution and should thereby reduce instances of double taxation.

Throughout this work, the U.S. Treasury Department worked closely with stakeholders -- in particular, the U.S. business community, which stands to be most directly affected by this work. And this was particularly the case in fashioning the rules on country-by-country reporting. Across the board, the BEPS deliverables are better than they would have been if the U.S. Treasury Department had not been heavily involved in their negotiation. We are proud of the role we played in the BEPS process, but our work is not done.

Where do we go from here? Well, certain technical work remains for the OECD in 2016 and beyond. And the participants in the G20 OECD project will be turning its attention to implementation of the BEPS deliverables, as well as monitoring what countries actually do with respect to those deliverables.

But we must do more than that. The G20 OECD project has produced well over 1,000 pages of material, some of it quite technical in detail. It is imperative that we turn our attention to ensuring that countries are able to implement these rules in a fair and impartial manner, based on the rule of law. What good is having carefully crafted new transfer pricing rules, if the agent in another country auditing a U.S. multinational is compensated based on the size of the assessment he or she can make against the multinational, regardless of its technical merit?

Can these rules really be fairly implemented if there is not access to meaningful appeals process? Ensuring the fair and effective administration of the BEPS deliverables must be part of our ongoing work. Indeed, the best way to foster the G20 goal of supporting global growth is to actively promote the connection between foreign direct investment growth and efficient and effective tax administrations.

Foreign leaders often come to the United States seeking greater foreign direct investment in their countries from our investors, seemingly unaware of the impediment to such investment resulting from their very own tax administrations. We need to do a better job of making the

connection between fair and efficient administration, foreign direct investment, and global growth. We are working hard to ensure that issues around effective and fair tax administration are made part of the post-BEPS agenda.

I would like to close by noting that it is no secret that the BEPS project was inspired to no small degree by the fact that large U.S. multinationals have been able to keep large amounts of money offshore in low-tax jurisdictions untaxed until those amounts are repatriated to the U.S. This phenomenon, and the sometimes very resulting low effective rates of tax, in turn have led to the perception abroad that U.S. multinationals are not paying their so-called fair share.

Thus, the BEPS phenomenon also lends support to the need for business tax reform. The President's proposal to lower corporate rates and broaden the base enjoys bipartisan support. We look forward to continuing to work with Congress to bring business tax reform to fruition.

Let me repeat my appreciation for the committee's interest in these important issues. And I would be happy to answer any questions you may have. Thank you.

*Chairman Boustany. Thank you, Mr. Stack. I -- clearly, this Committee now certainly has a sense of urgency about what is happening on the international front. And, as developments have occurred in a rapid pace, whether it is the creation of innovation boxes or patent boxes by European countries, or the completion of the OECD BEPS recommendations, we are falling behind. We need to pick up our pace. And that means we need to move forward with tax reform. We need a firm commitment that the Administration will work with us getting beyond where we are today, and really roll up the sleeves to try to move forward on this.

But one of the concerns that a number of us have had, as we have watched through the fall with the completion of these recommendations on the BEPS project, is that Treasury might be perceived as speaking or committing to legislative policy recommendations on behalf of Congress without full consultation with Congress.

BEPS implementation will focus on getting countries to make legislative changes, which will require congressional action in this country. And I just want you to outline for us, in signing off on BEPS, to what extent did Treasury and others in the Administration consult with Congress, or consider whether Congress would agree with any of the specific tax policy recommendations?

*Mr. Stack. Thank you, Mr. Chairman. I can report very directly that the -- if you go through the BEPS' 15 action items, there are 2 in particular that absolutely would need congressional legislative action. One is the work on interest stripping, which is in the BEPS project. And there is a second piece on what we call hybrid securities. That is a situation in which you get a deduction, let's say, in the U.S. because it is treated like interest, but when it is received in the other jurisdiction, they view it as a dividend and don't tax it, so that creates stateless income.

We were very careful, Mr. Chairman, not to include those in the minimum standard agreed at the OECD, precisely because we, as the Administration, could not and would not commit the U.S. Congress. I think, if you work through the other items, if you think, for example, of treaty matters, where we might agree, as a matter of Treasury, to put something in our model, a treaty,

of course, requires the advice and consent of the Senate. Fully mindful of that, and all our obligations in the BEPS process, take into account the legislative processes in the United States.

I mean I would just add for the record that there is nothing in the BEPS project that is a legally binding commitment on the part of the U.S. Government. And so, I think we tried very hard to respect the legislative role and the difference between the legislative and the executive in every aspect of our work.

*Chairman Boustany. Well, I appreciate that. And I think what we need to do now, going forward, is accelerate our level of communication on how we are going to move forward. Because other countries are taking steps, very aggressive steps, with some of the implementation of these recommendations. And if we fail to reform our code appropriately, we will not lead this process, it will be led by others, and I don't think the outcome is going to be as amenable to American companies as we would all hope.

I want to shift gears for a minute with one last question for you. I want to examine this EU state aid situation. EU state aid cases seem to be another example of foreign governments targeting U.S. firms to expand their tax bases. And we have seen the press reports. I have actually had a conversation with folks at Apple who are very concerned about this. I believe you share my concern that these EU state aid cases will lead to retroactive foreign tax increases on U.S. companies that could result in American taxpayers footing the bill through foreign tax credits, further eroding our base.

I am very concerned that the effects will go far beyond the EU's initial cases -- I mean we are in the early stages of this -- and that these cases could have substantial and direct impact on our U.S. companies -- and ultimately our U.S. taxpayers.

In light of the EU's state aid cases, what is Treasury doing to protect the interests of the United States?

*Mr. Stack. Thank you, Mr. Chairman. I would like to begin this discussion with a note of humility. I am a trained U.S. tax lawyer. I am not a European lawyer. I am not a competition lawyer in Europe, nor have we seen the final legal documents of all the various investigations that are ongoing.

In light of that, we were faced with a judgement, which is do we, as the Treasury Department, simply sit and let these cases kind of move forward and unfold with the possibility that I can talk -- which I will talk more about -- of the effect on U.S. bilateral relationships and/or the possibility of an ultimate foreign tax credit if, indeed, these taxes are determined to be creditable, which is an open question I need to put on the record.

Or we could speak now about the U.S. interest in these cases, even though the work is not finally done. So what Treasury has done is we have made it clear to the EU Commission directly that the United States has a stake in these cases.

The first -- our first stake is as follows. The United States has income tax treaties with the member states in the EU. We do not have an income tax treaty with the EU. And that is because income tax in the EU is left to the members to do their own income tax. Well, there is a great deal of uncertainty in the current proceedings whether or not the commission is substituting its own tax determination for that of the member states. And if it were to do that, I think it calls into question our bilateral relationships with members of the EU. And it is worth mentioning that the U.S. has an interest in understanding, with clarity, the precise nature of income tax enforcement administration in the EU. That is number one.

Number two, some of the numbers that have been reported in the press here are what I would call eye-popping. And while it is true -- and I will repeat for the record that we have not analyzed whether or not taxes required to be paid in these jurisdictions will, in fact, be creditable. The fact that they may be could mean that, at the end of the day, U.S. taxpayers wind up footing the bill for these charges by the EU State Aid Commission.

But let me make two other points that I think are very important here.

One is that I believe we also have a concern that these taxes are being imposed retroactively under circumstances in which -- I do not believe countries, companies, tax advisors, or auditors ever expected a state aid analysis of the type that is emerging from this work. In our view, when a novel approach to law is taken, that is precisely the situation in which a prospective remedy would be appropriate, to ensure that the behavior ceases without imposing very large tax impositions on a retroactive basis. So we have been very careful to note that we think the basic fairness calls for these to be retroactive.

Beyond being public about our concerns, and demonstrating the U.S. interest, and demonstrating our concern that fairness calls for a prospective approach, to be honest, it is not 100 percent clear what other tools are at our disposal, except to make our concerns known. And we have done that, and hopefully will continue to do that.

*Chairman Boustany. We look forward to exploring options with you on that. You put your finger exactly on the real concern that I have, other members of the committee have, about the retroactive nature of this, and how it is really, in effect, going after advance pricing agreements that are in existence. And this is deeply problematic.

I do believe we are going to need policy ideas that can be discussed between the Administration and this Committee on outlining our way forward on that. I thank you.

I now yield to Mr. Neal for questioning.

*Mr. Neal. Thank you, Mr. Chairman. I think on that question and the answer that was given by Mr. Stack there would be broad agreement on this Subcommittee and the full committee. I don't know that there was anything that the witness said that we could disagree with on that. I thought it was right on target. So thank you for establishing that.

Mr. Stack, it appears clear that the Pfizer Allergan merger is moving forward, and the resulting inversion of one of the largest U.S. pharmaceutical companies is imminent. You and the witnesses on the next panel have testified on the need for tax reform, and specifically international tax reform, as an important and even vital step to ensuring that multinational companies remain competitive globally, and continue to create jobs and income in the United States. I think you would agree so far that such tax reform has been elusive, despite years of conversation on the committee.

Are there some things that Congress could do right now, as we continue our efforts, to reform the tax code that could stem the tide of inversions?

*Mr. Stack. Thank you, Congressman. Yes, I actually believe there are. And I think that tomorrow I believe that if Congress were to lower the threshold for an inversion that forces the inverted company to retain its U.S. tax domicile from, let's say, 80 percent of the current statute to 50 percent, I believe that this would act very strongly to stem the tide of inversions because companies are quite reluctant to, let's say, give up control entirely, even in the public context, through a merger with another entity.

Second, I think that plugging our interest-stripping rules, so that once a company is inverted it is not able to take excess amounts of income out of the United States in the form of interest, is an imperative that we could do today, both to stem the tide of inversions, and also to level the playing field between foreign and domestic U.S. companies. I don't see those as necessarily having to wait for the full package of tax reform. And this is something I believe Congress could do.

As Secretary Lew has said, we have tried to do with our regulatory authority what we can. But these are some actions Congress could take that would help greatly, I believe, stem the flow of inversions.

*Mr. Neal. Mr. Stack, I have also heard from a number of multinational companies talk about the bad things that BEPS might do. I think everyone in the room would agree that it is certainly not in the United States's best interest to do something like pulling back from BEPS in the project, or stand on the sidelines as the rest of the world implements BEPS rules that could greatly impact our multinational corporations. For the members of this Committee, that could be tantamount, I think, to malpractice.

But to look at this from another angle, I think there are a number of very important things that the U.S. could specifically do, and that Members of Congress could join in in a helpful role.

There is an opportunity here, I think, for some very basic -- many things that could be done on insight that other countries are now choosing to do. Their authority under the new rules is to ensure that the United States, after a period of time, would push the participating countries to ensure that their efforts are being monitored by their peers. Would you offer your insights on that, as well?

*Mr. Stack. Certainly, Congressman. I think the -- frankly, the next phase that we will be working very intensely on in BEPS goes to both the implementation -- how will countries implement it. And here I mentioned I would like to push for the rule of law. And then, what kind of monitoring will we do? Will we watch other countries to see how they are implementing these rules?

From the U.S. perspective, there is a lot of areas where we are going to care a lot about the monitoring. We care a great deal about how country-by-country reporting is going to be done, whether it is confidential and whether it is used for the appropriate purposes. We are going to care a lot about whether new permanent establishment rules are applied in fair and efficient manner.

So, one of the ongoing work in BEPS is going to be creating these monitoring tools, so that, over time, we are watching to see that countries are not simply using these new rules to grab revenue, but applying them in a principled way. So that will be absolutely part of our ongoing work in BEPS.

And the country-by-country, I should add, in 2020 we actually all come back together to assess how the rules are working, how countries are doing them, are they producing necessary information for countries. And adjustments will be made, as necessary, at that time to the proposed rules, as well.

*Mr. Neal. Thank you, Mr. Stack. Thank you, Mr. Chairman.

*Chairman Boustany. Mr. Reichert?

*Mr. Reichert. Thank you, Mr. Chairman. And I want to take a moment, too, to thank you and Pat and the rest of our team over here, and then, of course, recognize Mr. Neal for his expertise and a good partner over the last year as I was chairman, and the team on the Democrat side.

I am an old cop, retired cop. So I am all about teamwork. And I understand that in this world sometimes politics get in the way of teamwork. But I think that you are hearing a lot of agreement so far with the testimony that you provided. And we will see how that goes as we continue to question you, but I appreciate all the work that you have done. And, as Chairman Boustany said, we really look forward to working with you to help make America stronger, and have that fair playing field that we all are searching for.

I want to focus on dispute resolution. You mentioned that in your testimony. Prior to the release of the BEPS final report, the number of tax disputes initiated between countries far outpace the number of disputes actually resolved. And, as countries begin to implement the various changes to their own international tax rules, as recommended by the BEPS final report, the number of unresolved disputes is almost certain to increase. I think you would agree with that.

However, the final report did not call for mandatory binding arbitration. And as you mentioned in your testimony, the United States, along with 20 other countries, remain committed to pursuing mandatory binding arbitration procedures.

So, my question, Mr. Stack, is why was mandatory binding arbitration, which is, again, of great importance to American companies and the United States, in general, not included in the final report?

*Mr. Stack. Thank you, Congressman. The short answer is the OECD BEPS project was a consensus kind of approach that sometimes played to the U.S. advantage, as we were trying to push items that we cared about. And in other circumstances, countries made clear that they were not yet ready to move forward on mandatory binding arbitration.

The reasons for that, by the way, are not always nefarious. I mean some countries don't have experience with it. Some countries worry about whether or not they can keep up with wealthier countries that might be able to put a lot of resources into it. And many countries have a concern that it raises issues of sovereignty to give away the right to make their tax determinations. And, of course, I suspect some are concerned that they would come out on the losing end of many arbitrations if, in fact, their tax administration was put to the test.

The good news, however, Congressman, is the fact that -- you referred to the fact that there are 20 countries ready to move forward in mandatory binding arbitration. This is something, when we are not successful in getting it in BEPS, we pushed it through the G7, and we have created quite a deal of momentum around it.

And I can also report that the 20 countries that are interested represent 90 percent of the dispute cases around the world. So, by bringing together a lot of the developed countries that actually have the cases today, we are able to put the real critical mass of countries into the pot of moving forward on mandatory binding arbitration, and we are deeply engaged in that work at the OECD and the multilateral.

The thinking I have is if we can get this critical mass of countries having experience with binding arbitration, that over time it will grow out and attract the countries that for now are not willing to do that, most notably a country like India. And so we would try to demonstrate its success, make it part of the international tax fabric and, over time, I believe we will have success in making mandatory binding arbitration a standard tool in our international toolbox.

*Mr. Reichert. And I recognized at the end of your testimony you asked yourself the question where do we go from here, and you mentioned tech work, implementation, large document -- 1,000 pages. Mr. Neal also asked about reporting and monitoring, which you mentioned again at the end of your comments. And you are looking for fair, efficient, effective, all of those things you mentioned.

Where do we go from here when it comes to binding arbitration? Is it your testimony, then, that demonstrating success is a likely way to get countries to come on board with dispute resolution language?

*Mr. Stack. Thank you, Congressman. I should have added that, as a very concrete next step, that we are working in Paris on something called a multilateral instrument, which will try to put in one instrument the various treaty-related matters that have been agreed in the BEPS process. Mandatory binding arbitration will, we expect, be part of this multilateral instrument, at which point countries can sign up to the instrument and, in effect, put it into effect with those 20 countries, automatically if you will, subject, of course, to ratification by the Senate.

And so, that gives us a very concrete, near-term vehicle to move forward with mandatory binding arbitration. And then I think we would watch the results and try to build out from there.

*Mr. Reichert. Thank you. I yield back.

*Chairman Boustany. Mr. Larson?

*Mr. Larson. Thank you, Mr. Chairman, and congratulations to you. And kudos always to Mr. Neal and your other predecessors who served as chairmen here, as well. And we want to get all these accolades out, and also condolences to Mr. Kelly on Notre Dame's loss this past weekend. I was with you, I wanted you to know.

Thank you again for your testimony, Mr. Stack, and for your service to the nation. And if I could, just a couple of follow-up questions, one on what Mr. Neal had to say, and the other one is -- it relates to the BEPS process.

There is great concern about wholesale rewriting of the rules on the digital economy, with countries wanting the rights to tax companies with a so-called digital presence in their country. A, did that occur? And can you discuss some of the Administration's proposals regarding the digital economy and subpart F income?

*Mr. Stack. Thank you, Congressman. Yes. I mean I think that, as I said in my opening statement, I think the U.S. presence in the BEPS project was critical to moving international rules in a better place for the U.S.

As the -- our digital companies are doing business all over the world. They are household names. They have penetrated markets and the consciousness of people and politicians all over the world.

And one of the issues we were facing in BEPS was whether or not there should be new rules to tax people who sell into an economy through the digital economy. And there is a great deal of fervor and political pressure to write such new rules. And I am proud to report that the digital report in the OECD was an excellent discussion of the technical tax elements of digital. But, at the end of the day, none of the more aggressive proposals for taxation based on a digital presence were adopted.

In the report there are options. And I believe also that European countries will turn, over time, more to that collection, which is totally appropriate. And I believe we were able to play a very constructive role in the digital space.

With respect to the U.S. issues on digital in our subpart F reforms, I would say that, quite different from the work in the OECD, whether we needed a brand new paradigm to tax the digital age, what we were really doing in the President's budget proposals was really trying to conform our subpart F rules to the fact that we now have different modes of achieving, in the digital space, things that brick-and-mortar countries used to do.

So let me give you a very simple example of our rules. Our subpart F rules are based on a premise that, if you sell out of the U.S., let's say, to Bermuda, and then Bermuda on-sells, let's say, into Europe, that the presence of this intermediate company provides an opportunity to do a little game-playing with how much income stays in the U.S. And so, we have a rule called foreign-based company rules, that says, well, if you're going to buy from a related person and on-sell, we're going to treat that Bermuda profit as really subpart F, bring it back into the U.S.

Well, in the digital space, if you think about it, you don't need to buy and sell a widget. You might license some IP and then stamp a disk in Bermuda and sell it in. And really, I think the easy way to understand our proposal is we simply brought our subpart F rules up to what we had been doing in the brick and mortar world, so that similar games could not be played by tech companies in the digital space. And we have got a couple of examples like that in our budget.

*Mr. Larson. So let me quickly ask you, as well, you mentioned that there were -- in addressing Mr. Neal's concerns, there were two things that Congress could do immediately. We all hope, and certainly would like to see the bipartisan effort to continue for tax reform. But you mentioned there were two immediate things, one lowering the threshold and the other dealing with interest stripping.

You said going from 80 to 50 percent. Why 80 to 50? And, with interest stripping, could you give us a quick explanation of how that occurs?

*Mr. Stack. Sure. Thank you. Well, in the interest stripping, you know, I often say when I speak, you know, you read a lot in the press about these highly-engineered structures to do base stripping around the world. And what I have said publicly sometimes, if you're a foreign multinational you don't really have to do something very fancy to strip out of the U.S. base, you just have to -- maybe you even dividend up a note. You just hand something to your owner and say, "Now I owe you \$1 million." And those interest deductions start clicking in the United States, and we are losing revenue at every moment.

Our proposal -- and one that we pushed at the OECD -- said, "Wait a second. First of all, a multinational shouldn't get, in our jurisdiction, any more than its pro rata share of its third-party borrowing." And without getting too much into the weeds, what we did was we came up with a way to say you can get your share of your global borrowing based on your EBITDA in the United States. And that seems fair. Or you can take a fixed percentage of your EBITDA so you don't have to kind of prove.

And in the Administration's proposal we put it at 10 percent. The OECD work suggested a corridor of 10 to 30. But I would just point out for the committee both of those are far removed

of the 50 percent in our current 163J, which seem to permit far more interest stripping than we can probably afford, or that is based on sound tax policy.

*Mr. Larson. Thank you.

*Chairman Boustany. I thank the gentleman. Mr. Tiberi?

*Mr. Tiberi. Thank you, Mr. Stack. I have got a headache. This is just unbelievable.

[Laughter.]

*Mr. Tiberi. So, in responding to Dr. Boustany's question about the EU state aid cases, you said you are not sure what else Treasury can do besides express concerns.

Mr. Neal correctly identified the problem, and that is Congress not acting. But I would also argue, Mr. Neal, that there has been a lack of leadership at the White House on this very issue, as well.

To me, it is not very complicated. Number one, it is outrageous, what the EU is doing in retroactively targeting U.S. multinationals. I just think it is outrageous. But number two, to me, in my Fred Flintstone mind it is not really complicated, what the problem is. We have a very uncompetitive tax code.

So, you can point to states. I was in Connecticut recently and I saw my friend, and the chatter there was about a large U.S. multinational company that has been headquartered there for a long, long time that was considering moving because of a new tax that was put in place in that state.

In my state of Ohio, we lost longtime multinational -- and not even multinational -- domestic companies not to just India, but to Indiana, to Georgia, to Texas. And the companies, many of them public, cited the tax code in Ohio. And this has happened internationally, as well. And yet we talk about trying to prevent ways by writing regulations and rules.

Mr. Stack, I don't understand why we can't look at this picture -- I am cynically asking, I am not really asking you, because it is above your pay grade.

[Laughter.]

*Mr. Tiberi. Why the Administration and Congress can't come together and do what happens in communities in Ohio. One community loses a major employer to another community because the tax rate is lower in that community than the community they left. We see this all over. It is the marketplace.

And, at the end of the day, you write rules to try to stop this, and maybe we can -- you know, we can hit that peg for a little while, but it is going to come up somewhere else. And the reality is we have an uncompetitive tax system. And if we can lower the rate and go to a system, some exemption-type system, that puts our large employers who do business all over the world on the

same playing field, quite frankly, that the rest of the world's rules are, then we could actually maybe see some of this loss of jobs and ultimate loss of revenue stop.

And for the life of me, I can't understand, so I ask you this personally, not as a member of the Administration, someone who leans to the left, rather than to the right. What is the problem with lowering rates and going to an exemption-type system that puts us -- puts our employers on a level playing field? Why not just do that?

*Mr. Stack. Thank you, Congressman. First of all, I think you have just described the President's plan.

*Mr. Tiberi. Wow.

*Mr. Stack. Because the President's plan would lower the corporate rates, would broaden the base, and, in many of the jurisdictions around the world, where you pay more than a minimum tax, you are exactly on equal footing with your competitors in those jurisdictions.

*Mr. Tiberi. Boy, oh boy. I remember watching the Democrat Convention and Joe Biden making fun of the exemption system, saying that would ship jobs overseas. So maybe the Vice President needs to get on board with the President, because I clearly don't think that what I am describing is the President's plan, because we would have passed that back in 2011. Or maybe you should have passed it back in 2009.

I mean, clearly, the market is doing something differently than what we would like them to do. And so, we have a -- not a loss of jobs. We have a loss of really good companies. The only thing worse than an inversion is the company actually moving their headquarters overseas.

And I don't know about the community you are from. The community that I am from, the jobs that -- the employers that make up the heart and soul of the communities, whether they are small businesses, medium-sized businesses, or large businesses, are the ones that are headquartered there, because they are involved in the United Way, they are involved in the educational system. They provide so many dollars to the community. And we are losing those.

And, rather than trying to come up with these BEPS rules and anti-inversion rules, I just don't understand and don't see the leadership from the White House to say, "Look, let's look what other countries have done. Let's look at what Ireland has done. Let's look at what the UK has done. Let's look at what other major employers, countries in the world have done, and follow their lead." If we would have done that three years ago, we wouldn't be having this hearing today. And maybe what we would actually be having is a great debate in Connecticut and in Massachusetts and Ohio and Louisiana about jobs coming here from Europe, rather than losing jobs to Europe.

I yield back.

*Chairman Boustany. I think the gentleman really outlined the problem beautifully. I thank him for that analysis.

Ms. Sanchez?

*Ms. Sanchez. Thank you, Mr. Chairman. And I am prepared to yield more time to Mr. Tiberi, if he wants to unveil the Tiberi-Obama plan.

[Laughter.]

*Mr. Tiberi. If you will support it, Ms. Sanchez.

*Mr. Thompson. I ask unanimous consent that we do a letter asking the Vice President to support the Obama-Tiberi plan.

[Laughter.]

*Ms. Sanchez. That is right, that is right. Reclaiming my time, Mr. Stack, thank you for being here today.

You mentioned that the U.S. had a presence in the BEPS discussion, and that that was a favorable outcome, to have that input. You talked about making it known that we have a vested interest in what comes out of that project, and that you favor a prospective approach, and that there is this issue of retroactivity.

I am curious to know what other ways did your -- did Treasury's participation in the BEPS project improve the outcome, the overall outcome, of the project?

*Mr. Stack. Thank you, Congresswoman. In preparing for today I had occasion to go back through these BEPS action items and just think of the ways the United States demonstrated a very strong intellectual leadership in -- actually, across the board of the actions. And let me just give you a couple of examples.

You know, transfer pricing is the prices that companies pay between affiliates across borders. Today, a lot of the action is around royalties and intellectual property, which is offshore. That constituted three action items: 8, 9, and 10. And there was an enormous push around the world to really water down the rules that respect contracts and respect the separateness of legal entities so that tax auditors and administrators could almost have carte blanche to look at a multinational setup and say, "Well, we think so much more profit should have been here than there."

We were extraordinarily aggressive in the transfer pricing space, and I think we have produced a report -- and I don't think it is -- I don't think I need to be the test of it, but I think within the U.S. tax community people have seen that move back to something that is far more a recognition of the arm's length standard and how to apply it.

On country-by-country reporting, I understand fully that it has been the subject of some complaint, because I can understand that any time you add burdens, et cetera, then there are concerns. But I have to say, on that one, the very first -- first of all, the world started off wanting

multinationals to publicly produce their country-by-country data all over the world, number one. And number two, the first draft of that report didn't just want six or seven items per country. I believe the first draft wanted something in the neighborhood of 19 or 20 items. And there was going to be a -- far more complexity.

And we worked with the business community, and we came back to OECD and said, "Look, this is what can be done in the least burdensome way. This is really all companies need." And we were able to push the country-by-country stuff over the line.

In the hybrid work -- and this is weedy, I will confess, and I won't get into the details -- but there were times when the administrators around the world wanted U.S. multinationals to identify every single item on their books and records that might actually cause a mismatch. And we said, "Wait a second. This should be done among related parties," because that is really where the problems are.

So, I think we went item after item, led very strongly, and have improved the quality of the work by our tenaciousness, our adherence to principle, and our technical skills.

*Ms. Sanchez. I appreciate your answer. And I would just add one further thing before I yield back my time, that if Mr. Tiberi is interested in us, the U.S., conforming our laws to that of most nations around the world, I would just point out that in the performance rights arena we lag far behind where the rest of the world is, and we give up revenue that sits overseas because we don't pay performance rights here in this country, as other countries do to our performers.

And, with that, I will yield back the balance of my time.

*Chairman Boustany. I thank the gentlelady. We will go next to Mr. Kelly.

*Mr. Kelly. I thank the chairman. Mr. Larson, thank you for your condolences, although I would just say to you that we both know Jerry Hogan. Jerry Hogan is the father of Kevin Hogan, the quarterback at Stanford. Jerry is a good friend of all of ours. His brother, Tom, and I went to school together at Notre Dame. And Jerry was also Notre Dame, too. But Kevin -- I was happy -- as much as I hate to see the Irish lose, I love seeing the Hogans win. So it is something about this Irish deal that keeps us together.

Mr. Stack, thanks so much for being here today. I am going to ask you a question, though. And I think Mr. Tiberi hit on it very clearly. Now I come from the private sector. And in the private sector you are always looking for market opportunities. And in our case we are looking at a global market. And we are looking at competitors who look at us and say, "This is a country whose pocket we can pick," because of tax policy and regulations that make it very hard for us to be competitive on a world stage.

Now, Senator Levin had proposed a bill in early 2014 that would place strict limits on mergers in which they move their tax address outside the U.S. Under the Senator's plan U.S. companies trying to buy a foreign company and relocate their headquarters to a lower tax country would have to ensure that shareholders of non-U.S. companies owned at least 50 percent

of the combined company, up from 20 percent now. The bill would consider inverted companies to be domestic for U.S. tax purposes if executive control remained in the United States and if 25 percent of sales, employees, or assets remained in the United States. The measure would have been retroactive to May 2014, and would be in place two years while Congress considers broader tax changes.

Mr. Levin was responding to 14 companies that had conducted mergers since 2011 in which they moved their headquarters outside the U.S. and into a lower tax jurisdiction. At the time of his announcement, Pfizer was contemplating such an inversion. Fast forward to today. Pfizer has announced that is just what they are doing.

So, if you just did the Levin bill, that is a bill that actually became law, would that by itself forestall this migration of the U.S. tax base, considering the question within the context, relative of the tax advantage that foreign acquirers would gain from tighter inversion rules on U.S. companies?

*Mr. Stack. Congressman, yes. I -- we have a budget proposal that differs from the Levin proposal in some minor ways that I can't recall as I speak at this moment. But the general concept of telling a company that if you are -- if you retain more than 50 percent ownership by the U.S. shareholders of the formerly inverted company, you have it inverted and you are still U.S., we think would help greatly stem the flow of inversions.

*Mr. Kelly. Okay. But I think, when I heard Mr. Tiberi talk -- and I think we all agree -- in the private sector there is something about a carrot and a stick, and how you incentivize people to behave properly, or the way you would like to see them behave.

So, I don't believe that a bigger stick that creates it harder for people to be profitable -- and, by the way, we all want to see companies be profitable because they hire more people, they make more capital investments -- I would rather see a carrot that makes sense in relation to what the rest of the world perceives as a global market, and as an advantage that they have, or in restructuring their tax code to say, "Come over here and shop with us, you can be here," knowing that -- I think this is the part that is really hard for people to sometimes grasp -- the total cost of operation includes everything, not just your raw materials and your labor, but also tax policy.

When we artificially increase the cost of any product or service by a tax code or by regulation that makes it impossible to be on the same shelf globally as other countries, then it is time for us to take a look at what it is that we are doing wrong. Not what they are doing wrong. They are responding to an opportunity. It is not that they are not patriotic; they are just not stupid. Why the hell would you stay here, and continue to pay those kind of taxes and those kind of regulations, and then be held up as the worst people in the world because you are not paying your fair share? There is something that just doesn't make sense about this whole piece.

And this is not a Democrat or Republican issue. This is an American issue. We continue to lose red-white-and-blue jobs. We continue to decimate our local economies. We continue to downgrade our ability to compete globally and then blame it on some kind of a corporate strategy. That is not the problem here. The problem is we have no strategy, going forward, to

gain market share. And I am talking about global market share. If you really want to lift this economy, then do it the right way.

So I don't expect you to respond to that, but, I mean, I don't think the Levin bill does it. I would argue against any time that somehow a bigger stick, swung harder, is going to encourage people to stay. You know what they are going to do? They are going to say, "You know what? I am going to stay. I am not going to leave. But in the future, I am making investments someplace else, and I will let this die on the vine. It can wither and go away. I will still succeed, but it won't be here."

And I think that is the real crux of the matter. We seem to think that somehow, by beating people, that we are going to make them perform better. That is not the key. The incentive is much, much brighter for America when we actually encourage people to make investments here, not tax them out of business or regulate them out of business and make them totally uncompetitive on a global stage.

Thank you, I yield back.

*Chairman Boustany. The chair recognizes Mr. Thompson.

*Mr. Thompson. Well, thank you, Mr. Chairman. And I also congratulate you on your rise to prominence in this fantastic subcommittee.

Mr. Stack, thank you very much for being here. And it is interesting. We all seem to be coming from the same place on the dais, irrespective of the side. We may have a different way of articulating it, Mr. Kelly, but I think we all want to make sure that the U.S. is a competitive place where we attract businesses, businesses who will stay here, businesses who will come here, businesses that will create jobs, businesses that will pay a tax level that give us the revenues that we need in order to fund the priorities that we have, as a congress, as Americans.

And so, I guess my -- what I am interested in is maybe some help from you, some guidance from you, as to how we get there. Your focus has been on business and international tax reform. The other side of the equation is the comprehensive tax reform that has had us all wrapped around our axles for the last many years. And is it your perception that we need to do one before the other?

You talked a little bit about some specific tax policy that could be done, irrespective of comprehensive, that would help things around, help things move along. But is it better to break it off and do the business international, or would doing comprehensive help you get to where you believe we need to be, in regard to the business and international?

*Mr. Stack. Thank you, Congressman. I would mention, just as an opener, there has been, in terms of carrots and sticks and competitiveness -- as a tax policy committee, I think you folks know better than I do that, at the end of the day, the most competitive rate might be zero, but then we don't raise any revenue.

So, as tax policy folks, we always are all thinking about what is the revenue we need to fund the government we have. And finding a happy medium with that and these competitiveness concerns is kind of an obvious point. And so we are not free, I take it, to just join a race to the bottom to, let's say, zero corporate tax rates without an alternative revenue source.

As to the second question, I would simply point out that the business tax reform in the last two years -- there seems to have been some bipartisan consensus that a revenue-neutral business tax reform could be broken apart and done independently. And I think there has been a lot of good work done in lowering the rates and broadening the base and trying to get to the revenue-neutral business tax reform. Whether or not it is better to put it on with the comprehensive and the individual, I am simply going to report, as the international guy on the team, I am afraid that falls a little above my paygrade.

I don't -- I think there is a lot of complicated issues that folks -- that you all appreciate perhaps better than I do about the complexity of going to the full comprehensive, you know, in the current environment. And I think there was a judgement made at some point to try to do the business-only on a revenue-neutral basis, and that seemed to be, for a while, the most promising thing we could do.

*Mr. Thompson. Thank you. Before I yield back, I just want to elaborate a little bit on the last point you made, and that is the importance of being revenue-neutral. It has got to be able to pay for itself. And, if it doesn't, all we are doing is digging the deficit hole deeper, and passing on greater debt to future generations. I think that is real important to keep in our focus, as we do any tax policy in this House.

Thank you, and I yield back.

*Chairman Boustany. I thank the gentleman. Mr. Renacci?

*Mr. Renacci. Thank you, Mr. Chairman. And I want to thank you for holding this hearing on this very important issue.

It is clear that our international tax system is outdated and anti-competitive, and makes U.S. companies vulnerable to foreign takeovers. In northeast Ohio we already have one large, multinational that has inverted. We have another company that is considering inversion. We have another one that looks like they are going to be taken over. So these are issues that are very concerning to me. And, Mr. Stack, you and I have talked about this in the past. So I do think we have to continue to look at this and do what is necessary to make sure that we are competitive here.

Mr. Stack, I am going to get into the weeds a little bit, though, on one of the items finalized on round one. As you know, action 13 requires companies to maintain and report significant transfer pricing documentation. Some have said that action 13 may be the most important action item arising out of the BEPS project. I want to focus on the difference between two of the types of documentations that companies will be required to report, country-by-country, CBC, reporting; and master file information.

Can you explain what types of documentation businesses must provide under these two types of reporting?

*Mr. Stack. Thank you, Congressman. The country-by-country report is really a template in which a country would list the various jurisdictions around the world in which it does business, and then it would list out six or seven economic indicators: its revenue, its taxes paid, its taxes accrued, its assets, its retained earnings, number of employees. And then it would have a little code of, like, what kind of a business does that company do. It is a distributor or a manufacturer.

So it is really a form, if you will, that sets forth that kind of information. The form will be filed with the U.S. tax return. And then the U.S. Government will, with appropriate treaty or tax information exchange partners, exchange that form with jurisdictions around the world that have promised to keep it confidential, and use it for kind of a risk assessment.

The master file is really a different document. And, by the way, the work in this space about harmonizing transfer pricing documentation around the world precedent BEPS, because multinationals were basically stuck with a situation in which every country in which they did business was asking for a different kind of transfer pricing documentation to substantiate what it did.

So the OECD went to work and said, "Gee, we could have a win-win here. We can simplify this documentation to reduce the burdens on business and, at the same time, get the countries what they need." And that aspect of it consists of two parts, really. There is something called the master file, which I will talk about, and then there is something called a local file.

And the local file is, oh, tell me about your foreign affiliates that have direct transactions with my country, so we can go in and check your transfer pricing. The master file is this overview document. Tell us about -- in fact, I highlighted just a couple of sections of it -- give us a high level -- it is intended to provide a high-level overview in order to place the multinational group's transfer pricing practices in their global economic, legal, financial, and tax context.

It is not intended to require exhaustive listings of minutiae, a listing of every patent, as this would be unnecessarily burdensome. Instead, it is an overview of the business, the nature of the operations, its transfer pricing policies, et cetera. And in producing that master file, which is written by the company, it should include lists of important agreements. But the company should use prudent business judgement in determining the appropriate level of detail.

So this is your big, overarching picture. It goes to the company. When they come in to audit you they know something about you and how you function. And that is the master file.

*Mr. Renacci. Mr. Stack, I am running out of time, but are you concerned that the master file information will be used by foreign governments to launch frivolous foreign audits or, even worse, leaked to foreign competitors?

*Mr. Stack. I am -- one can never say never, Congressman, right? However, we have to look at this context of the countries had the opportunity to ask for this on their own beforehand. We

will be vigilant in watching how American companies are treated around the world, and we will try to take actions appropriately.

*Mr. Renacci. And I am going to move back to state aid, which I know the chairman talked about.

It is disturbing to me that American companies are being targeted in proceedings and aren't given an opportunity to defend themselves. My understanding is that only the countries can defend the state aid proceeding at the commission level. Companies that are subject to increased retroactive taxes -- which we talked about, almost 10 years -- are precluded from participating in the commission's proceedings.

Mr. Stack, do you share the concern of fairness of these proceedings, if the company is not allowed to participate in these hearings?

*Mr. Stack. Congressman, I am not an expert in the procedures in the state aid proceedings, so I am a little loathe to kind of judge them, you know, from afar. Obviously, opportunities like ability to present your case are part and parcel of fairness, in our view. But I don't know their procedures well enough to comment.

What I have chosen is the retroactivity aspect, because I think that stares us all in the face to say, "Hey, these are new rules, they should be applied prospectively, not retroactively," and that is the piece that I have chosen to focus in on. And I apologize, I am not a procedural expert to know enough for the basis of your question. But, obviously, I am concerned about the fair treatment of our companies.

*Mr. Renacci. Thank you, Mr. Stack. I yield back.

*Chairman Boustany. I thank the gentleman.

Mrs. Noem?

*Mrs. Noem. Mr. Stack, thank you for being here today. I will keep mine short.

I am concerned that there isn't mandatory binding arbitration procedures in the final report. When the United States, obviously, made it a priority, and several many other companies -- or countries, as well, asked for that, we look at the number of tax disputes every year -- far exceed those that are resolved. And as many countries start to implement some of the changes that were recommended in the final BEPS report, we are bound to see more tax disputes.

Why was there no binding arbitration procedures put in the final report?

*Mr. Stack. Thank you, Congresswoman. I -- we were also disappointed that we were not able to have mandatory binding arbitration as part of the final deliverables.

The nature of the BEPS process, however, was a consensus process. And so, countries were able, in effect, to veto the idea that we would have binding mandatory --

*Mrs. Noem. I understand that it was a major concern for many countries, up to 20 of the major countries that are part of the negotiations.

*Mr. Stack. Yes, yes, it is. And the nature of the OECD process is it takes one country, basically, to block moving something forward.

Now, on the flip side of that is, when it came to the transfer pricing work, the United States was able to be very aggressive in saying, you know, "We have certain demands before that work comes out." I --

*Mrs. Noem. So what is our next process? What do we do about getting some procedures put in place?

*Mr. Stack. So we have 20 countries that have said, "We want to do mandatory binding," and they represent 90 percent of the world's disputes right now. And we are moving to put that in this multilateral instrument that, hopefully, that -- part of which the United States can join, and hopefully get it signed and ratified by our Senate. And we will have made enormous progress, even though there will be some outlier countries, for the time being, that will not have mandatory binding arbitration with us.

So, it is not a whole loaf, but it is a pretty good loaf.

*Mrs. Noem. And the time frame on having those recommendations ready for the Senate's consideration would be?

*Mr. Stack. So the multilateral is hoping to finish a draft in 2016. I think that is very ambitious. So I think we are looking over the next couple of years when this would play out.

And, of course, we need to have those provisions look like provisions that we think our Senate would ratify. So there is a fair amount of work on that.

*Mrs. Noem. Okay, thank you. With that, I yield back.

*Chairman Boustany. I thank the gentlelady.

Mr. Holding?

*Mr. Holding. Thank you, Mr. Chairman. I want to follow up on a couple of lines of inquiry from my colleagues.

First, from Mr. Tiberi -- just expand on his comments. You know, it is not only about rates. And if we could just simply, lower the rates, broaden the base, you know, we would be much more competitive. It is also compliance cost. I had a series of interesting meetings with

large multinationals, and just talked about how they comply with the U.S. tax code, and how they comply with other countries.

You take one particular company, tens of billions of dollars in revenue. Their U.S.-based operations, they have 40 IRS employees in their accounting division to continually prepare their returns, and so forth. In their UK-based operations with similar amounts of revenue, they are able to comply with the tax code there with no revenue agents in their accounting offices. It is a huge burden to comply with our tax code. So it is not only a matter of lowering the rates, Mr. Chairman, you know, it is a matter of simplifying the system so that companies can easily comply.

I want to follow up a little bit on Mr. Renacci's comments about the master files. You know, it is -- in the master files -- I mean the information there is not general. There are a lot of specifics there regarding supply chains, service agreements, extremely sensitive information. Imagine the sensitivity of a defense contractor's information who is doing work all around the world, different countries, dozens upon dozens of different countries on every continent. You can imagine the angst they would have in supplying, you know, the information required by the master file.

So, I mean, I understand that Treasury will be compiling those, collecting and compiling those master files. Is that correct?

*Mr. Stack. Congressman, we will -- the IRS will collect the country-by-country file. The master file goes directly from companies to the countries in which they operate.

*Mr. Holding. Okay. Will the Treasury also have the master files?

*Mr. Stack. We -- if -- let's say there is a U.S. company that operates in foreign jurisdictions. We would not necessarily get a master file from, let's say, a U.S. resident multinational, because they are our taxpayer, they are here, and we have all the information we need about them.

*Mr. Holding. So, I mean, if the master file is misused in some way, what recourse does a company have?

*Mr. Stack. I think that one of the reasons I would like to move our focus -- let me back up.

Companies already today deal with tax administrations that don't always behave in the best ways, and they struggle with that. And it is one of the reasons we want to move the BEPS work more into focusing on tax administration.

The second thing to keep in mind is companies -- countries were always free to ask for a master file. What we really did at the OECD was homogenize the work so that there is, like, one file asked for around the world. We didn't really have a special power to tell countries what they could ask of multinational --

*Mr. Holding. So in the BEPS process, was there consideration of some form of recourse that a company might have or, you know, special safe harbor provisions, where a company could shield sensitive information?

*Mr. Stack. I --

*Mr. Holding. Is there any arbiter of that --

*Mr. Stack. On that last point, Congressman, we -- the companies have the pen on that report, and we do not expect them to, willy nilly, give away sensitive information. Because we think the master file rules can be read in such a way that companies can use judgement to be sure the country gets the high-level view that I described without necessarily pouring out, you know, super-sensitive information. That was the judgement --

*Mr. Holding. So, you know, during the BEPS process it was clear that the various countries involved were working hard to protect their own multinational countries, protect their own interests. So Treasury, at the table at the BEPS process, what were you doing to protect U.S. multinational countries during this process?

*Mr. Stack. I think --

*Mr. Holding. Give me your top three hits.

*Mr. Stack. I think the top three hits are the work we did to make the transfer pricing respect the legal entities and contracts of our companies, I think the work we did to get the country-by-country reporting to be manageable for our multinationals, and I think the work we did to protect our digital companies from overreaching by foreign jurisdictions. Those are the three that I would say pop to mind --

*Mr. Holding. Give me a couple where you think you failed.

*Mr. Stack. I -- we were disappointed that things like permanent establishment rules are looser than we would like, although there we said, "Well, we are not necessarily going to adopt those, but the rest of the world wants to." And there we are going to come back on more work to make sure we can ringfence the work done on permanent establishment rules.

And the fact that countries around the world have opted for a kind of a very loose principal purpose test for treaty abuse was disappointing to us. Now, again, the U.S. is not going to adopt that approach, but other countries seemed to want to do that.

We wanted, in both those cases, more clear and administrable rules for other countries to follow, but other countries had different ideas.

*Mr. Holding. Thank you. Thank you, Mr. Chairman.

*Chairman Boustany. I thank the gentleman. And I think Mr. Holding hit on some very important questions, given that we have 6103 protections for U.S. taxpayers and yet, under the master file, we have serious concerns about those kinds of protections, going forward.

Mr. Stack, thank you for being here today. We appreciate your testimony. It has been extraordinarily -- oh, I am sorry.

Mr. Reed?

*Mr. Reed. I know I am from New York, so we are often forgotten here. But if we could have the last word, Mr. Chairman, I would appreciate it.

*Chairman Boustany. You got it.

*Mr. Reed. Thank you, Mr. Stack. I do want to zero in a little bit on this master file issue, because it is of a concern to me.

So what I am hearing from your testimony is, essentially -- and from your written testimony -- is the Treasury is going to require country-by-country reporting mechanisms for certain companies -- I think it is \$800 million or more, or above. But with the master file, Treasury is not requiring that information.

And essentially, what I heard from your testimony -- and is this accurate -- that you are essentially saying companies are in the best position to protect their information, therefore we are going to let them make the determination as to what information they release in that master file. Is that the testimony you are offering?

*Mr. Stack. Yes, Congressman.

*Mr. Reed. Okay. So what is Treasury going to do if someone challenges that determination by the businesses, that maybe they erred in their judgement, and a taxing administration says, "We need more information"? What is Treasury's position or response to those multinational companies that are in that situation?

*Mr. Stack. So those question -- that question could go in two directions. The first direction could be that a U.S. -- a foreign country is always asking our multinationals for more information. It is a constant part of being a multinational tax director. And then you have the laws of the local country, and you -- that local subsidiary may or may not have that information. And that is kind of a common, everyday dispute in the multinational space. So, in this case, that would be no different.

A trickier question could be, well, let's say they don't like the level of detail in the master file. And so they --

*Mr. Reed. That is my question.

*Mr. Stack. Yes, and they impose a penalty, or they do something --

*Mr. Reed. Correct.

*Mr. Stack. Then I do think -- but I don't think this is different in kind from a whole slew of administrative things we have to be paying more attention to, to protect our multinationals that I would like to get on the next wave of the agenda, which is: how do tax administrations act; do they act in good faith, in accordance with what the general consensus --

*Mr. Reed. You are going away from my question here, Mr. Stack.

*Mr. Stack. Yes?

*Mr. Reed. Because, if I am understanding correctly, country-by-country reporting is going to be given to you, the Treasury --

*Mr. Stack. Yes, right.

*Mr. Reed. And then that is going to be protected by tax information --

*Mr. Stack. Yes.

*Mr. Reed. -- treaty agreements, and you will have the ability to defend what information is released, et cetera, and stand by those companies that are targeted maybe in an inappropriate manner.

But with the master file data, I don't see the same type of protection that Treasury is offering to companies that, you know, make that error in judgement or say, you know, "We gave you enough information," and the tax administration says, "No, we are going to hit you with a penalty."

Treasury is essentially telling our guys, "You are on your own," is what I am hearing from your testimony.

*Mr. Stack. Well, the report does call for countries to treat it confidentially. But what I want to emphasize here is -- and this is difficult --

*Mr. Reed. How are they going to treat it confidentially?

*Mr. Stack. Because, in many of these jurisdictions, it is expected to be treated as tax return information in those jurisdictions. So it would just be --

*Mr. Reed. So your understanding is that the foreign countries are going to protect that information. And what is the penalty if the foreign country violates that --

*Mr. Stack. We don't have a specific penalty, Congressman. I mean, and that is fair. I think --

*Mr. Reed. That is the problem.

*Mr. Stack. It is --

*Mr. Reed. That is the problem.

*Mr. Stack. It is, Congressman, except if we never had a BEPS project, those countries could ask for the same information. We didn't do anything special in the BEPS project that the country couldn't have done on its own. What we did do was try to get a homogenized look at these --

*Mr. Reed. All right, so --

*Mr. Stack. -- across the countries.

*Mr. Reed. Going into the negotiation, you recognized that the countries had the ability to potentially --

*Mr. Stack. Yes.

*Mr. Reed. -- abuse or inappropriately use that information, but we elected -- you elected not to take that issue up. You elected to negotiate other points is what I am hearing.

*Mr. Stack. No. Actually, Congressman, I think my big, heavy lift in the next part of BEPS is I want to get all the tax administration issues like this on the table, and get the world to agree to peer reviews and standards for what a fair and just tax administration should look like. And when we do that, that country could not assert a penalty on a master file, just because it is missing some jot or tittle, because that is not the spirit of that work.

That is a reason to stay engaged multinationally, but it is more work to be done for -- to be sure, and it is a heavy lift. I wouldn't doubt that. But it is important.

*Mr. Reed. So that is for future consideration and future --

*Mr. Stack. Yes.

*Mr. Reed. -- negotiation. Because --

*Mr. Stack. And it is important.

*Mr. Reed. Because that is another question I have. One of the things I am seeing here, potentially, on the international scene, especially with the EU, is the EU seems to be targeting, for lack of a better term, this revenue. And as they face austerity budgets in the EU, I just see, in my opinion, an aggressive attack by the EU to go after this revenue.

And you just said there is a future BEPS environment that you envision. What is post-BEPS? Where are you going? What is after? What can we expect in those negotiations, going forward, especially when the EU seems to be taking a very aggressive approach here?

*Mr. Stack. Yes. So I think I just want to -- because they are doing it through their competition committee, they don't necessarily participate in the overall tax work that we do at the OECD, and that is part of the problem, I think, that you are pointing to.

*Mr. Reed. Yes.

*Mr. Stack. In the -- coming back to the tax world that I live in, I think the next phase in BEPS is how do we implement this, how do we monitor each other, how we are implementing it. And something the U.S. is aggressively trying to put on the table is how do we make everybody else behave with all this information. And that is something that I want to get companies and countries to focus on, both through the G20 and also at the OECD.

*Mr. Reed. I appreciate it. I notice my time has expired. With that, I yield back. I appreciate the information.

*Chairman Boustany. I thank the gentleman.

Well, thank you, Mr. Stack, for appearing before this Subcommittee. You helped walk us through some very difficult and complicated issues. Obviously, a lot more is going to be done in this area. I want to assure you that both sides of the aisle of this Subcommittee have a deep interest in how this is going to be implemented, and there are a number of outstanding questions. So, again, thank you, and we look forward to staying in touch.

We will now call the second panel up.

[Pause.]

*Chairman Boustany. We will now hear from our second panel of witnesses. We have a very distinguished panel, starting with Barbara Angus, principal with Ernst and Young, followed by Gary Sprague, counsel, The Software Coalition. Then Catherine Schultz, vice president for tax policy, National Foreign Trade Council and Martin Sullivan, chief economist, Tax Analysts.

The committee, as I stated earlier, has received your written statements. They will be made part of the formal record. We look forward to hearing your oral remarks, and I would ask each of you to limit those oral remarks to five minutes.

Ms. Angus, you may begin when you are ready.

STATEMENT OF BARBARA M. ANGUS, PRINCIPAL, ERNST AND YOUNG

*Ms. Angus. Chairman Boustany, Ranking Member Neal, and distinguished members of the subcommittee, it is an honor to appear before you. My name is Barbara Angus, and I am leader of strategic international tax policy services for Ernst and Young. Earlier I had the privilege of serving as international tax counsel for the Treasury Department, and as business tax counsel for the Joint Committee on Taxation. I am appearing today on my own behalf, and not on behalf of EY or any client.

I am pleased to be here to discuss the practical implications of the final reports issued by the OECD as part of its BEPS project. Other countries are already implementing aspects of the recommendations, so this hearing is very timely. As the Ways and Means Committee continues its work toward U.S. tax reform, it is important to consider the BEPS recommendations, the actions that other countries are taking in response, and how those actions will affect global companies that are headquartered or invested in the U.S.

At the core of the reports issued by the OECD last month are recommendations for significant changes affecting fundamental elements of the international tax framework. Countries must now consider whether, how, and when to act with respect to the BEPS recommendations. They will act in their own interests and under their own timetables.

The OECD project arose out of a growing political and public focus in many countries on the taxation of foreign companies. Therefore, I have no doubt that significant action with respect to BEPS will take place across countries around the world. Indeed, countries had already begun taking unilateral action to address BEPS, even before the OECD issued its reports.

The international tax changes that are embodied in the BEPS recommendations have significant implications for all global businesses. While the OECD did not deliberately target U.S. companies, the recommendations could have a disproportionate impact on U.S. businesses because of their geographic spread and the particular pressures of the U.S. worldwide tax system. Moreover, some countries have singled out U.S. companies, and the recommendations could well be used by countries in such targeting.

Global companies face uncertainty in light of the BEPS recommendations, significant uncertainty. The BEPS recommendations generally reflect a move away from relatively clear rules and well-understood standards to less-specific rules, more subjective tests, and vaguer concepts. Global companies face significant new compliance burdens highlighted by the new country-by-country reporting requirement.

Global companies face significant risk of misuse of their business information. The new reporting would put global information about a company into the hands of all countries where it operates. For U.S. companies, which tend to have the broadest global footprint, the risk of breaches of confidentiality is particularly acute.

In this regard, many U.S. companies believe it is in their interests for the U.S. to implement the recommended country-by-country reporting so that they can provide their information to the IRS to be shared under U.S. information exchange relationships, subject to the U.S. rules on confidentiality of taxpayer information. This approach would mean greater protection and lower

administrative burdens than the alternative, of U.S. companies directly providing their information to multiple foreign countries.

Global companies face significant risk of controversy. The new rules are subject to varied interpretation. Controversy imposes substantial resource burdens on both taxpayers and tax authorities. For taxpayers, controversy in a foreign country is even more complex.

Global companies face significant risk of double taxation. Where countries do not apply the new transfer pricing guidelines included in the BEPS recommendations in the same way, for example, multiple countries may assert taxing jurisdiction over the same dollar of income. One of the BEPS focus areas was improving the dispute resolution mechanisms used to prevent this kind of double taxation. But the BEPS project made little progress in this area, which is a major disappointment for the U.S. business community.

Importantly, there is continuing work in the OECD on BEPS that provides opportunity to ameliorate these issues. Business input is much needed, and the U.S. business community, which has much at stake, should continue its participation in the OECD process. In order to ensure that U.S. interests are protected, it is essential that Treasury, in consultation with the tax rating committees, continues to play an active role in all aspects of the OECD/BEPS work.

Countries' actions with respect to the BEPS recommendations will dramatically change the global tax landscape. The aspects of the current U.S. tax system that detract from the attractiveness of the United States as a location to headquarter and invest will become more acute as other countries implement the BEPS recommendations. The BEPS project, and the response by foreign countries, should be viewed as yet another reason why tax reform must be an urgent priority.

Thank you for your opportunity to present these views [sic].

I would be happy to answer any questions.

*Chairman Boustany. Thank you, Ms. Angus.

Mr. Sprague?

STATEMENT OF GARY D. SPRAGUE, COUNSEL, THE SOFTWARE COALITION

*Mr. Sprague. Chairman Boustany, Ranking Member Neal, and members of the subcommittee, thank you for inviting me to appear today on behalf of The Software Coalition to provide testimony on the impact of the OECD G20 BEPS project on U.S. software companies. In particular, how the BEPS project will reduce the U.S. tax base and create disincentives for U.S. multinationals to create R&D jobs in the United States. The members of our coalition are listed in our written submission.

Our comments today will focus on those BEPS developments of greatest significance to the U.S. software industry, namely corporate income tax nexus in countries into which our companies export goods and services, transfer pricing, R&D employment incentives, and the unraveling of consensus among countries on international tax norms. While my comments are delivered on behalf of the U.S. software industry, U.S. multinationals and other high-tech industries are similarly impacted.

First, the changes to tax treaty rules that establish when an exporter is subject to income tax in the country into which it exports goods or services. A key focus of the BEPS work was a push by market countries to obtain greater taxing rights over non-resident exporters which make sales into their countries. The BEPS work significantly reduces the threshold for income tax nexus, so that a member company of an MNC group may have to file tax returns and pay taxes in a market country, even if it has no physical presence in that country.

Second, with respect to the OECD transfer pricing guidelines, these guidelines determine how much of a group's income is subject to tax in a particular country where that group operates. The principal effect of these transfer pricing changes will be to decrease the returns allocated to intangible property and other assets in favor of returns to people functions. This also will increase tax collections by market countries, since U.S. software companies do not hold their intangible assets in such countries.

Third, I will comment on the BEPS work regarding incentive tax regimes for R&D employment. The BEPS work recognizes that countries may set their national tax rate at any level. Most OECD member states have significantly reduced their rates of corporate income tax in recent years. At the same time, the BEPS work has created guidelines for targeted R&D employment regimes. Several countries that compete with the U.S. for technology investments have enacted so-called IP Box regimes that provide an even lower incentive tax rate for income derived from IP developed in their country. These rules create a strong incentive for U.S. multinationals to locate R&D functions in those countries.

Finally, I would like to comment on a particularly unfortunate side effect of the current political and administrative environment relating to international tax. In our view, the BEPS process has encouraged, or at least tacitly permitted, some countries to circumvent the normal consensus-building process at the OECD and to act unilaterally. This stands in stark contrast to much good work the OECD has done historically to develop an international tax consensus.

On the related point, we note the EU state aid cases represent another example of foreign governments endeavoring to tax income which ultimately is part of the U.S. tax base. What, then, are the implications for U.S. tax policy? We believe that Congress should enact comprehensive international tax reform, which would include reducing the corporate tax rate to an internationally competitive rate -- for example, to 25 or even 20, as some have suggested.

As part of such comprehensive reform, we favor a territorial system, such as 95 or 100 percent dividend exemption system, consistent with other major OECD countries, and a transition rule that allows tax-favored repatriation of earnings.

Further, the U.S. should enact a best-in-class IP Box regime that provides an effective incentive to protect and create R&D jobs in the U.S. Please see our letter of September 14 to Chairman Boustany and Ranking Member Neal, which details our recommendations on the proposal.

This proposal would provide the following benefits to the U.S.: preserves the competitiveness of U.S. multinationals; it encourages the repatriation of IP by those U.S. multinationals which now hold their IP offshore, and discourages newly emerging companies from migrating their IP outside the United States in the first place; third, it would reduce the incentive for inversions through foreign acquisitions by diminishing the incentive for tax-motivated foreign takeovers; finally, it would encourage U.S. job growth and innovated industries by countering the incentives which now exist for U.S. multinationals to locate R&D jobs offshore.

The work on BEPS is not finished. Therefore, we would encourage U.S. Treasury to continue taking an active role in ongoing technical discussions to be held in 2016 and beyond. In particular, the new tax nexus rules will present U.S. multinationals with considerable unnecessary expense and increased compliance burdens.

Accordingly, Treasury should encourage our treaty partners to adopt alternative means of compliance and reasonable transition periods.

I very much appreciate the opportunity to provide testimony on behalf of the software industry, and would be pleased to answer any questions.

*Chairman Boustany. We thank you, Mr. Sprague.

Ms. Schultz?

STATEMENT OF CATHERINE SCHULTZ, VICE PRESIDENT FOR TAX POLICY,
NATIONAL FOREIGN TRADE COUNCIL

*Ms. Schultz. Chairman Boustany, Ranking Member Neal, and members of the subcommittee, thank you for inviting me to speak today about the G20 and OECD report on base erosion and profit shifting. I request that my complete statement be made part of the record.

The National Foreign Trade Council, organized in 1914, is an association of some 250 U.S. business enterprises engaged in all aspects of international trade and investment. The NFTC believes the current U.S. tax law is outdated and must be modernized by enacting tax reform that reduces the U.S. corporate income tax to be more in line with our trading partners, and adopts a competitive territorial tax system that does not disadvantage U.S. businesses competing in foreign markets. Competitive U.S. tax reform would address many of the concerns raised in the BEPS project.

The Treasury Department staff should be commended for their efforts to attempt to ensure the rules that were drafted were as grounded as they could be in reasonable and objective tax

law. Unfortunately, this was a difficult task, since the BEPS project was politically driven and, we believe, appeared to be aimed more at raising revenue from U.S.-based multinational corporations, rather than other global companies.

We have several concerns with the CBC report. The country-by-country report is intended to provide information that is to be used only as high-level risk assessment tool. Completing a CBC report will be cumbersome and expensive for taxpayers, particularly for taxpayers who have operations in many countries. There are many NFTC members who operate in over 100 countries. If tax authorities release taxpayer information to the public, as some recommend, there is concern about determining the correct amount due on a tax return, based on media reports, rather than tax law. Companies understand they must share tax information on a confidential basis to the relevant tax authorities, where it can be explained in context. However, they are unwilling to be subject to audit by media spin.

It is important to note that if the U.S. does not require country-by-country reporting subject to confidential information exchange via the U.S. treaty network, U.S. companies will still have to comply with the reporting requirements, because each country will demand that the local subsidiaries of companies produce a global CBC report under its local variation of the rules, which will be expensive, and may expose confidential information to improper disclosure.

The NFTC hopes the U.S. will continue to make the case to maintain the confidentiality of CBC reporting, as the countries who participated in the BEPS project will review the implementation of the CBC reporting in 2020.

Countries are already adopting these reporting guidelines, and many are not following the BEPS report guidelines. Indeed, China has already said that it will require entire value chains to be reported in all local analysis. Companies are concerned with how the information they are required to file under the master file will be used by local authorities. We believe it is important for Treasury and the IRS to provide further guidance, so companies can report their information to the IRS with section 6103-protected information exchanged via the U.S. treaty network. Otherwise, as I have noted, countries will be entitled to request it for -- without section 6103 protections.

There are several other concerns that the NFTC member companies have with the final BEPS report, and I will try to get through them pretty quickly.

The action 7 on permanent establishment changes several of the longstanding definitions of what constitutes a permanent establishment, which subjects a business to income in a local country. Action 7 changed the definition of a deemed income tax permanent establishment to achieve in-country tax results under applicable transfer pricing rules. This will result in more companies being subject to tax in a local jurisdiction, and could result in potentially double or triple taxation for companies.

I am not going to spend a lot of time going over the transfer pricing rules, but we do have a lot of concern about the new rules on value creation. It is often hard to determine where value is created. In a value creation that is supposedly tied to function, it will be difficult to determine

the final values, because value and function are not always linked. So we have a lot of new transfer pricing rules with new value creations. It could be very difficult. Some countries are adding additional value creation requirements. China is considering a value contribution method that departs from the BEPS guidelines. Location-specific advantages will be used -- analysis.

The NFTC is concerned about the general aggressive global tax enforcement environment. The BEPS report action 11 analyzed base erosion and estimated how much is lost to -- worldwide to aggressive tax planning. Interestingly, this analysis was not done prior to the start of the BEPS project, but only at the very end.

As countries continue their aggressive stance to collect enough taxes to counter base erosion, who will determine what enough is? If BEPS is hard to determine beyond a I-know-it-as-I-see-it standard, how will it be determined when it no longer exists? As other governments increase taxes on U.S. multinational companies, the U.S. is likely to provide foreign tax credits to those companies to offset double taxation on the same income. As the number of foreign tax credits increase, we will see more base erosion. But this time it will be the U.S. base that is eroded.

What can Congress do to protect the U.S. base from being eroded further? The NFTC is strongly in favor of tax reform that lowers corporate income taxes in line with our trading partners, and moves to a competitive territorial-style tax system.

Thank you for the opportunity to present the views of the National Foreign Trade Council, and I would be happy to answer any questions.

*Chairman Boustany. We thank you, Ms. Schultz.

Mr. Sullivan?

STATEMENT OF MARTIN A. SULLIVAN, PH.D., CHIEF ECONOMIST, TAX ANALYSTS

*Mr. Sullivan. Good morning, Chairman Boustany, Ranking Member Neal, members of the committee. Thank you for inviting me to discuss the BEPS project and its effect on the U.S. economy.

In 2013 the OECD initiated the BEPS project to address the flaws in the international tax system that allowed multinationals to shift profits but not corresponding business operations from high to low-tax countries. At the core of the OECD's response is a focus on aligning taxable profits with value creation with economic activity, with economic substance. This is likely to have significant consequences for the competitiveness of multinationals, on how multinationals allocate investment across borders, and on how countries engage in tax competition.

Check-the-box regulations issued in 1996 made it easier for U.S. multinationals to shift profits into tax havens. The BEPS alignment of taxable profits with business operations would take much of the juice out of these -- out of this check-the-box tax planning. In 1998, when Treasury wanted to withdraw check-the-box regulations, many questioned why the U.S. should

have rules that help foreign governments collect taxes. Now it is the BEPS project that will help foreign governments collect taxes.

Before, multinationals could lower their taxes with tax planning that had minimal impact on real activities. Now, to lower taxes, they will be required to shift jobs and capital investment to low-tax countries. If BEPS succeeds, we will be entering a new era when cross-border profit shifting is replaced with cross-border shifting of jobs and of capital.

Countries with low tax rates and real economies, countries like Ireland, Singapore, Switzerland, and the United Kingdom, are the likely winners. Their gains will come at the expense of high-tax countries that will lose jobs and will lose investment. With a combined federal-state rate of 39 percent, the United States is particularly vulnerable.

The likely response by foreign parliamentary governments that can more easily change their tax laws will be to set their corporate rates even lower than they are now. The UK has already announced that it will reduce its corporate rate to 18 percent in 2020. Competition for real activity will increase. The already problematic effects of the high U.S. corporate rate will be compounded by these rate cuts.

Reducing the corporate tax rate has always been a top priority. The BEPS project will raise the stakes. The critical question is how do we pay for it. The economics of corporate tax reform are trickier than most people realize. It is entirely possible that any revenue-neutral corporate tax reform that rolls back investment incentives will impede and not promote economic growth.

At the top of the list of the usual suspects to pay for a rate cut is a reduction in depreciation allowances. Unfortunately, the positive growth effects of a rate cut are more than offset by the negative effects of slower capital recovery. If you add to that capitalization of R&D, as proposed by Chairman Camp, you have a tax reform that penalizes capital formation, with the heaviest burden on domestic manufacturing.

Clearly, to boost America's competitiveness, we need a new approach. Revenue neutrality within the corporate sector is not a useful guiding principle for 21st century tax reform. We need to downsize our most economically damaging tax and replace those revenues with revenues from other sources.

One option is for the United States to follow the example of other nations and adopt a value-added tax. This would greatly enhance U.S. competitiveness because revenue from the capital-repelling corporate tax would be replaced with a highly-efficient consumption tax.

Another approach would be to shift away from taxing business entities and towards taxing investors. The main advantage of this approach stems from differences in cross-border mobility. Investors are less mobile than investment. Most OECD countries have raised shareholder taxes, while cutting their corporate taxes. And because the burden of corporate taxation is increasingly falling on labor, a shift from corporations to shareholders will increase progressivity.

On the international side, the Camp approach to territorial taxation, including all of its strong anti-base erosion provisions, still seems correct. We need to banish lock-out from our international tax rules. To the extent we impose any tax on foreign profits, we should levy that tax as profits are earned, not when they are distributed.

We need strong and tough earnings stripping rules. It is common practice for foreign-headquartered multinationals operating in the U.S. to cut their U.S. tax by paying interest to foreign affiliates. Earnings stripping is a major motivation for inversions.

Finally, as proposed by Chairman Camp, we need to adopt a one-time tax on unrepatriated foreign profits. From an economic perspective, this tax is as good as it gets. As a tax on old capital, it does not affect incentives on new investment. Congress should consider a deemed repatriation proposal with rates substantially higher than those proposed in the Camp plan, and use those revenues for tax cuts that promote domestic jobs and domestic capital formation.

Mr. Chairman, thank you very much.

*Chairman Boustany. Thank you, Mr. Sullivan. We will now proceed with questions. Let me start with Ms. Schultz and Ms. Angus.

Under the BEPS action item 13, the master file information that is required is something of concern. We had some discussion with it earlier. Based on what we know today, what recourse does a company have if it discloses sensitive business information to a foreign jurisdiction and that information gets out to a foreign competitor?

*Ms. Schultz. Yes. I think, as Mr. Stack said, companies have to work very hard to try to make sure that whatever information is provided is not proprietary. But a lot of countries are requiring that information.

So, you may say, "I am going to put this much information on, and if they ask for additional information they can do it through the audit process and we will then, you know, have a separate conversation to review that information," but the way it is set up right now, a lot of these governments are already making these changes, and are going to require that information. It is going to be very difficult, if information is required and it doesn't go through an exchange of information provision, for companies to be able to control what happens with that information.

There is also a big push by some of the civil society to make sure that as much information gets published as possible. They think that to have corporate transparency you need to have all the tax information out in the public. So a lot of the proprietary information that companies really hold very tightly, especially value chain information, is stuff that they are very concerned could get released or could get given to some other governments, or through civil society, and released in another way.

*Chairman Boustany. Thank you. Ms. Angus, do you want to comment?

*Ms. Angus. I agree with --

*Chairman Boustany. Please turn your microphone on.

*Ms. Angus. I agree with the comments by Ms. Schultz, and also Mr. Stack, that the master file is an important document to focus on. Because it is a more extensive document than the country-by-country report, it can provide more information. It is in narrative form. So precisely what information is provided and how it is described is in the hands of companies, and they will need to approach this very carefully to be compliant with the requirements but give themselves as much protection as they can.

Once a master file is provided to a government, as with any other information that a company has to provide to the tax authority, they then fall under that country's rules as to the protection of that information, and we certainly have seen experience where U.S. companies have had unfortunate experiences in the past with countries not protecting information the way that it is protected in the U.S.

I think that is an important issue to be considered as the work in the OECD goes forward. The OECD has an opportunity to take a leadership role here and get countries really focused on the price of obtaining the information that they want about companies has to be to protect that information.

*Chairman Boustany. I thank you. And I see that in the country-by-country reporting it is limited to large multinational groups with consolidated group revenue of at least 750 billion Euro. Does the master file disclosure requirement in action 13 have similar restrictions?

*Ms. Angus. It does not have those restrictions, as specified by the OECD. And the countries that have already begun to adopt the master file have not always put in any restrictions. So it could apply to any company of any size.

*Chairman Boustany. I thank you. And finally, a question for Mr. Sprague.

BEPS was supposedly meant to level the playing field and address tax evasion and tax avoidance in an even-handed fashion. Can you elaborate further on how BEPS is encouraging the creation of IP regimes in various countries? Are these patent boxes, or innovation boxes, likely to effectively force companies that use a lot of intangibles to move operations out of the United States?

*Mr. Sprague. Thank you, Mr. Chairman. The short answer to the last question is yes. The BEPS process, very interestingly, resulted in, essentially, a setting of minimum standards for IP boxes. So even though general corporate tax rates outside the United States are lower, considerably lower, than the U.S. rate, every country that has adopted an IP box will have an even lower rate for income in the IP box. It is remarkable, how many countries have either already adopted or are intending to adopt an IP box. The rate to the UK, for example, is 10. The rate in Ireland is likely to be 6.25. Those are very powerful incentives.

The agreement that has come up through the BEPS process essentially is to establish a connection, a very direct connection, between the amount of income that can be taxed in the IP

box and the amount of R&D development activity that is performed in the country. So, as a consequence, the very direct result of the IP incentive is to incentivize all companies -- U.S. companies included -- to move R&D functions into the countries that offer such IP boxes.

*Chairman Boustany. I thank you.

Mr. Neal?

*Mr. Neal. Thank you much, Mr. Chairman.

Mr. Sprague, you correctly noted that many of our competitors, particularly in the G20, have lowered their corporate rate. And you cited the British, for example, as Mr. Sullivan did. Simultaneously, while lowering that corporate rate, Prime Minister Cameron is now calling for more defense spending. Who is going to make up the difference in revenue?

*Mr. Sprague. Well, that is a political question that I guess --

*Mr. Neal. I am going to give Mr. Sullivan a shot at it, as well.

*Mr. Sprague. You guys get to -- you get to decide. You know, my -- from an international corporate tax competitiveness perspective, I am a private practitioner. You know? I work with companies. They ask me what the tax rate is outside the United States compared to the U.S., and I tell them. And that provides a very powerful incentive for them to move operations outside the U.S.

And one very important result of the BEPS process -- I think Ms. Schultz commented on this -- the transfer pricing changes, in particular, are going to encourage companies, our clients, U.S. multinationals, U.S. software companies, to put high-value jobs outside the United States, because it is those high-value jobs that are going to solidify the foreign structures to make them stand up better to challenges of the market jurisdictions.

*Mr. Neal. Mr. Sullivan?

*Mr. Sullivan. Thank you, Mr. Neal. You know, the question keeps coming up over and over again. Or it doesn't -- actually, it doesn't come up enough. How are we going to pay for a lower rate?

I am in favor of a low corporate rate. I would go to 10 -- I would go to 15 percent to 10 percent. But we have to find alternative sources of revenue. Obviously, a value-added tax is not very popular in the U.S. Congress right now, although it is what other countries have done to lower their corporate taxes. And perhaps the more realistic alternative that you also see in other countries is raising taxes on shareholders, raising taxes on investors.

So you would move the point of imposing tax on capital away from the mobile corporations that can move outside of the United States and place that burden on shareholders. And you see

more and more in the academic community experts are recognizing that this is a far better approach than trying to impose tax on corporations.

*Mr. Neal. Thank you. And, Mr. Sprague, how much of the trapped cash that U.S. multinationals have held overseas is attributable to software companies, do you know?

*Mr. Sprague. I don't know, offhand. I mean there are many industries that have trapped cash overseas. I think there are articles that publish those statistics from time to time.

*Mr. Neal. What is the software industry currently doing with that money?

*Mr. Sprague. Generally, the money is used to reinvest outside the United States, reinvest in operations outside the United States, make acquisitions outside of the United States. Because of the lockout effect of U.S. tax law, the income or the cash can't be dividended back to the United States without the punitive U.S. tax. And so it is way more efficient to deploy that cash to grow business operations outside the U.S.

*Mr. Neal. Mr. Sullivan, you want to comment on that?

*Mr. Sullivan. Well, the -- I think one -- maybe one way of thinking about this is what will they do with the money if the money is brought --

*Mr. Neal. That is the point, yes.

*Mr. Sullivan. -- if they are allowed to bring it back. And we saw, back in 2004, when we had a repatriation holiday -- I don't know about specifically the software industry, but, despite all of the discussion about how it was going to be used for investment and plant and equipment and job creation, most of it went into paying dividends and share buybacks.

*Mr. Neal. And I think that is the point. And I -- having experienced that moment, when it was suggested that the repatriated money could be used for job creation, that certainly -- we -- there is broad agreement today that certainly did not happen.

*Mr. Sullivan. And you know, we certainly want to get rid of the lockout effect.

*Mr. Neal. Exactly.

*Mr. Sullivan. We don't want to have that money trapped offshore.

*Mr. Neal. Right.

*Mr. Sullivan. But I think some of the claims about how much benefit we will get for it as being a major stimulus that will transform the economy, I think, is a little bit overblown.

*Mr. Neal. You know, there seems to be some consensus amongst the panelists that trying to get that money back at a reasonable rate would be very productive for America's economic

purpose. And I think that that is where we ought to be focusing our attention, but not to miss the point that that argument was made here.

I was on the committee at the time and objected strongly to the notion that that money should be brought back at five and a quarter. And it was brought back at five and a quarter. And even the most aggressive proponents of bringing that money back later acknowledged not only did they not do any hiring, but that the money was given to the shareholders, and it was called good management. Now, that is up to them to make the determination. But not to miss the point, under the guise of job creation, that money was returned.

Thank you, Mr. Chairman.

*Chairman Boustany. Mr. Reichert?

*Mr. Reichert. Thank you, Mr. Chairman. Thank you all for being here, and for providing your testimony, taking time out of your busy schedules to be with us today. Just a quick follow-up question on BEPS action 13 that the chairman was pursuing.

I would just like a little bit of a -- more elaboration, Ms. Angus, on -- and Ms. Schultz -- on what other countries are doing. So you have referenced the more than 60 countries in the last 2 years are now taking actions related to BEPS action 13. So what are those actions that other countries are taking, and how do they affect the United States? Either one of you would be --

*Ms. Angus. Well, with respect to country-by-country reporting -- and in particular, we have seen a flurry of activity starting before the OECD final reports, but speeding up since the issuance of the reports last month. And there are three countries that have already adopted country-by-country reporting: Mexico, Poland, and Spain. There are several others that have legislation in the process that is expected to be completed shortly that will have country-by-country reporting in place, and many other countries are considering it.

At the same time, there are countries that have also acted with respect to putting in place master file requirements.

*Mr. Reichert. Ms. Schultz?

*Ms. Schultz. I agree with Ms. Angus, that you start to see the countries that originally were called unilateral actors. Now they are called early adopters, before the BEPS report was finished. Just sort of changed the dialogue a little bit on who was doing what.

But just by putting the BEPS action report -- by starting the BEPS project, countries already started to make changes in their tax laws, and said that they were doing it because of BEPS. There were a lot of countries doing tax reform. There is countries that have started to add the -- as Barbara said, countries are already starting to do the things from the BEPS action report, but a lot of them started well before the BEPS project was finished. There was a lot of tax reform taking place. There were a lot of countries taking a look at their rules, both indirect

and direct taxation on how they were taxing the income that they considered to be the BEPS income, the base erosion income.

And one of the things that Mr. Sullivan said about the VAT, a lot of governments, because the U.S. is the only OECD country without a VAT system, a lot of these governments had already started to look at the VAT and said, "If you need a specific agent for VAT purposes, we will give you a PE for direct tax purposes." So governments have started to try to figure out a way to get more income tax from U.S. multinationals in many other ways, not just looking at the CBC and the master file.

So, by doing these early actions, there has been an awful lot of activity prior to the finish of the BEPS project, where companies have had to be more aware of where the changes were coming.

*Mr. Reichert. And what are the impacts on American companies?

*Ms. Schultz. It is much more expensive for American companies. We are seeing companies -- just the complication of complying with all these different rules, and paying attention to who is changing their rules under which -- at which time, it is becoming a little bit more difficult for companies to make sure that they are ready to comply with all these different rules.

It has also increased the number of disputes already, significantly. The number of audits is up. And the number of disputes is going to go up substantially, as well.

*Mr. Reichert. Ms. Sprague -- or Angus, I am sorry.

*Ms. Angus. I would just add that it -- certainly change is happening like this all around the world. At the same time it creates significant uncertainty. In many cases the changes are not fully described or detailed, so there is uncertainty about how the rules will be applied.

And we are seeing an increase in tax authorities using the label of BEPS to justify challenges of companies under current law. So, potential for significant retroactive effect, where the law hasn't been changed, but they are using this as an excuse to make a challenge against a company.

*Mr. Reichert. Thank you, and I yield back, Mr. Chairman.

*Chairman Boustany. Mr. Larson?

*Mr. Larson. Thank you, Mr. Chairman, and thank all the panelists for your testimony.

Mr. Sullivan, if I could, I would just like to ask a couple of questions. And one of them -- and what I appreciate about these hearings -- and I want to say, Mr. Chairman -- is that this provides us an opportunity to demystify for the American public a lot of the terminology that we utilize. I can imagine someone tuning in -- I don't think our ratings are probably that high, but I can imagine someone tuning in and listening to the conversation here, and when I go home to Augie

and Ray's and I talk about the lockout effect, and I talk about base erosion and earnings stripping and check-the-box, et cetera, they kind of look at me and say, "Well, yes, but what are you doing about jobs."

And while I do think that there is a direct correlation between these, Mr. Sullivan, if you could, briefly discuss how we can make changes to some of our international tax rules to help grow jobs in this country, while preventing the further base erosion, if possible. And then I would like you to expand upon what you had to say about what is going on in academic circles about a discussion -- you and Ms. Schultz mentioned the VAT tax. Probably the unlikelihood of that happen (sic), but the thinking as it relates to shareholders and investors. So those two questions, sir, if you could.

*Mr. Sullivan. Thank you, Mr. Larson. That is quite a challenge, for an economist to put something in plain English, but I will try.

[Laughter.]

*Mr. Sullivan. It is about jobs. And we want domestic job creation. And when we look at our tax system, the major flaw of our tax system is the corporate tax. It has always been a flaw. But for the prior 50 years we have had so much economic growth that we haven't really -- we have been able to endure it.

But now we really can't afford to have a high corporate tax rate. And so, what we -- all roads will lead you to the same conclusion. We need to get the corporate tax beaten down as much as possible, because it repels capital from the domestic economy, which raises productivity, which raises wages, which creates jobs. And so we need to be thinking about different types of proposals.

And so, we want -- so the conventional tax reform is about broadening the base and lowering the rates. We don't really have that option any more. We need to broaden the base. We need to lower the rates without getting rid of domestic -- incentives for domestic capital formation. And so we need to look at other sources of revenue.

And I think, you know, it is an education process. At first we thought we could broaden the base and lower the rates, and now we see that it is not possible. We can't get the rate below 30 percent. We need to get it to, you know, to 20, and we can't even get it to 30 right now. And so, what I think more and more academics are looking at -- on both sides of the aisle, this is not a partisan issue -- is where else can we get revenue. How can we collect tax in a more efficient way? Nobody likes to raise taxes on anybody, but where are the best places to look?

And if you look at what is going on around the world, where everybody is -- all the other countries are lowering their corporate rate, they are raising their value-added taxes. And we don't have that option. But also, what they are doing is they are -- they have fairly high taxes on their -- at the personal level. Ireland has very high personal tax rates. UK has a 45 percent top individual rate. And all throughout the world you see this conscious decision to lower the corporate rate and replace it with a higher individual rate.

*Mr. Larson. And so how would that -- as you were saying in the -- how would the proposal work, in terms of shifting responsibility to shareholders and investors? How would that -- what kind of revenue would -- could that get us towards revenue neutrality? Could that help make up the base? What is the thinking along those --

*Mr. Sullivan. Well, the -- it is -- there are limitations on how much you can raise the taxes at the shareholder level. You can certainly get the capital gains rate back up to 28 percent. You could certainly think about getting the dividend rate back to -- at the regular level. And then we raise a significant amount of revenue that could be used for lowering the corporate rate.

*Mr. Larson. Thank you. I yield back.

*Chairman Boustany. Mr. Kelly?

*Mr. Kelly. Thanks, Mr. Chairman, and thank you all for being here.

I continue, though, to -- as I listen to you all, coming from a little different world than the world I am existing in right now, other than really pro-growth tax reform and regulation reform, all the rest of these things are interesting topics to sit around some night, have a nice drink and discuss it and debate it. But the reality of it is, if you look -- let's just relate it to where we are right now, related to football. Look at what the other guys are doing and winning, and adopt those practices. Look at why the other guys are losing, and then thank them for continuing on that same path, because it makes your win a lot easier.

And what you each have said is exactly what we all agree on, and that is tax reform. But not just tax reform, but pro-growth tax reform, based on the market, the global market that we now compete in. Sometimes I think we are going back to the Dark Ages and we are having debates about how many angels we can fit on the head of the pin, instead of how many people we can get back to work.

In my world, profitable companies pay taxes, working people pay taxes. That is the key to it. So getting more people back to work. But you have to have a product on the shelf that competes with everybody else in the global marketplace. And you have all talked about it. And it is just kind of mystifying that we are sitting here, asking you questions like, "How could we possibly fix this?"

What is the problem? The cost of operation. So every good or service that we do -- and I don't care what it is that you look at -- if we are going to make it harder to go to market, more expensive to go to market with a product that can't compete on a price range with everybody else in the world, we are going to continue to lose. And to think that somehow, by having you come in here, and baring your souls to us, or giving us ideas is going to get it done, it is not.

Please tell me about the difference between what the Irish did -- very charming. Love them, cute as the devil they are, but they have been picking our pockets for a long time. And they just lowered their rate again, because they looked at the world and said, "Wait a minute. These guys are getting close to us. We got to cut our rates." Tell me the difference between what the Irish

are able to do overnight, what Cameron is able to do -- quickly -- and a pivot to making more profitable, and give you more market share. What is the difference between those models and our models? Just real -- and I mean real quickly, because I think the answer is pretty obvious.

Any of you. Ms. Angus, what would you do right now, today? And what are they able to do that we are not able to do?

*Mr. Sprague. You know, if I can respond to that --

*Mr. Kelly. Sure, Mr. Sprague, please.

*Mr. Sprague. You know, the Irish tax policy has been consistent for many years, to hold fast to a low corporate tax rate to make them, as they describe, the most competitive jurisdiction in Europe for inward investment. They have done exactly what Mr. Sullivan did --

*Mr. Kelly. Exactly. But how did they do it? What process did they go through to pivot to that position? We have been deliberating for years here. I mean they don't have to sit around and deliberate on it as much, it seems to me. Isn't it a quick response? Isn't it an early conviction made saying, "Listen, in order for us to compete we have to act now, and not continue to talk"?

*Mr. Neal. Will the gentleman yield?

*Mr. Kelly. No. I will in a minute, I will in a minute. I know we are both Irishmen. I want to get to this.

[Laughter.]

*Mr. Kelly. Because I am telling you, I know what they are doing.

*Mr. Sprague. You know, their parliament and their ministry of finance has always been consistent: "This is our international tax policy."

One thing that I think is worthwhile communicating to you is that Ireland came under huge pressure from the EU several years ago to raise their tax rate because Ireland was successful. Ireland achieved --

*Mr. Kelly. Well, of course, yes.

*Mr. Sprague. -- lots of inward investment --

*Mr. Kelly. If you want to change the rules, that is the easy way to do away with your competition.

Anybody, please tell me how quickly they were able to respond.

*Ms. Angus. They have a parliamentary system, and we do not.

*Mr. Kelly. Thank you. That is what I am trying to get to. We continue to play ring around the rosy with this, and we know what the answer is, but we keep saying this is something we have got to get done, but we just can't do it.

*Mr. Sullivan. You know, Mr. Cameron in the UK, and same thing in Ireland, they made conscious decisions to raise their other taxes to pay --

*Mr. Kelly. Right. Individuals pay almost 50 percent.

*Mr. Sullivan. Excuse me?

*Mr. Kelly. Individuals pay 50 percent.

*Mr. Sullivan. Yes.

*Mr. Kelly. But keep in mind they used to pay a lower percentage on no wages. They would gladly pay 50 percent on higher wages, because they end up with a net gain in their pocket. That is not hard to figure out.

*Mr. Sullivan. When Ireland was devastated by the financial crisis --

*Mr. Kelly. Right.

*Mr. Sullivan. -- they cut government worker salaries by 15 and 20 percent. They raised all of their other taxes, but they kept the corporate rate at 12.5 percent. And there was no debate about it.

*Mr. Kelly. Yes. But my point, Marty, is they were able to act quickly.

*Mr. Sullivan. Yes.

*Mr. Kelly. That is the whole point. The purpose of debate is fine, if the consequences are that you actually get something done. And this is a Forrest Gump moment. There ain't no fixing stupid. Thank you. I yield back.

*Mr. Neal. Mr. Chairman?

*Chairman Boustany. Yes.

*Mr. Neal. Just to play up on what Mr. Kelly said, the other thing that they did, they took advantage early on of European Union subsidies for infrastructure. They were way ahead of the rest of Europe. The roadways were done. The Internet was prominent across the island. And there is another lesson for everybody: Everybody on that island is literate. That education is the gold standard of Europe.

*Chairman Boustany. Mr. Renacci?

*Mr. Renacci. Thank you, Mr. Chairman. I want to thank the panel. It has been enlightening to listen to you. And I spent a week over in Europe talking with members that were looking at this BEPS project. And Mr. Neal asked a question which I thought was kind of interesting, because I asked a similar question when I was over there. They are lowering rates. And, as we heard, Mr. Cameron is increasing spending. And the question was how are they going to do that.

Well, the answer that I was told was, ultimately, they are going to get American companies over there, they are going to increase their tax base and their jobs. That gets to Mr. Larson's question about jobs. If they can get American companies over there, and they can increase the number of jobs over there, that is how they are going to raise their tax revenues to pay for their military spending. And that is one of the things that we have to start looking at, is how we can be more competitive.

The corporate tax rate is a piece of our revenue structure. But, of course, we all know the individual tax rate is the majority of our revenue that we get in. And how we fix this system is that we look toward more jobs here. And today, if we continue to do nothing, and more companies go overseas, those companies are going to end up taking our jobs over there, increasing their payroll taxes, and having the dollars that we should be having by increasing them here.

I was a businessman for 28 years. If I can save 20 percent, I am going to save 20 percent. If I have to pay 20 percent more, I am going to have less employees. It is a pretty simple fact when you work in the business world here in America, that if you can move overseas you are going to do that. So this is something we have to move on. And that is why I appreciate all of your comments.

I want to go back to -- I am actually glad that we hit on action 13, because I really think that is important, and the cost of -- companies to have to provide that. Because that is also a job issue. If I got to spend more money here to comply with action 13, I am going to have less for jobs. So that is one issue.

Mr. Sprague, I noted that at least one company -- well, at least one of your member companies is a target of these state aid investigations. But this is for the entire panel. Does it appear that U.S. companies are being targeted more than the EU companies when it comes to state aid? I don't know who can answer that, but --

*Mr. Sprague. Well, there -- of the various companies that have been targeted, only one is a non-American company. We, of course, don't have information as to how the competition directorate made their decisions, but many commentators have noted the fact that all of the rest of the targets are, indeed, U.S. companies.

*Mr. Renacci. Yes, it is interesting. Because, again, I go back to the fact as -- how are European countries going to raise their revenues? It keeps going back to figuring out how -- a way to get the American profits taxed overseas. So these are issues that we continue to go back and forth on.

Ms. Angus, in your testimony you said that the BEPS recommendations generally reflect a move away from the relatively clear roles and well-understood standards to less-specific roles, more subjective tests, and vaguer concepts. Can you explain how the vague roles adversely impact American companies, in particular?

*Ms. Angus. Certainly I think vague rules are subject to different interpretation in different hands. That is an invitation for double taxation, for more than one country to seek to tax the same dollar of income.

I think there are fundamental ways that the BEPS recommendations have increased vagueness. Maybe one I would single out are the proposed changes to the permanent establishment rules, the rules for setting a threshold for when a country is considered to have taxable -- a company is considered to have taxable presence in a country.

The BEPS recommendation would move away from a relatively clear set of rules to much vaguer standards, so that a company entering into business in a country won't know when it will cross the line and be considered to be like a domestic company, and subject to the full rules, the full compliance procedures in that country. That adds a huge burden, in terms of the need to fully comply with all aspects of the tax system, to file a tax return as if it was a domestic company.

It also can have implications beyond the income tax. If a company is viewed as having a permanent establishment, it may be required to register for value-added tax. There may be other licensing requirements that get carried with it. And, at the same time, its home country may not believe that there is a permanent establishment there, may not be willing to cede taxing jurisdiction. And so you have double tax.

*Mr. Renacci. Thank you, Mr. Chairman. I yield back.

*Chairman Boustany. I thank the gentleman.

Mrs. Noem?

*Mrs. Noem. Thank you, Mr. Chairman.

Ms. Angus, we talked a lot today about U.S. multinationals. We tend to think of them when we are talking about the international tax system. But in all reality, in your testimony you shared that a company doesn't necessarily have to be large to be impacted. And all global companies are going to face uncertainty with regard to cross-border operation and investment, in light of the BEPS recommendations.

But could you comment about the impact that the BEPS recommendations and related measures might have on smaller U.S.-based companies? In particular, looking at what they might do in regards to expansion into other countries, and what they might do to expand their presence in -- overseas, to market their goods.

*Ms. Angus. I think the issue with respect to smaller companies is a really important one that we sometimes lose sight of. People think that an international company equates with being a large company. That is not true today. The smallest of companies can operate cross-border. Some might say that the smallest of companies must operate cross-border in today's global economy. And for them, the uncertainty, the new compliance burdens, the potential for double taxation is particularly stark.

A smaller company doesn't have the resources to invest in order to put in the infrastructure to produce a country-by-country report, to be able to get the representation to understand the details of the tax rules in every country in which it might be doing some business to try to see will it be considered to have a permanent establishment in that country, and then need to come in to the full compliance net in that country. Those issues really can operate as barriers to that activity if the potential to serve that market could cause the company to suddenly become a full taxpayer in that country, and fully into the system.

The answer might be it is better not to serve that market, and that is a really unfortunate answer, I think, for both the U.S. company and for the potential consumers in that country.

*Mrs. Noem. I think that is why I wanted to highlight your testimony, because most of the discussion here today people would think revolved around very large entities and companies that have multiple opportunities to expand into many different countries. But in reality today, many small businesses, this is such a burdensome change in recommendations that are being made here, that it could completely eliminate their ability to be a part of a market, or even continue to stay in business if a lot of these things are implemented.

So thank you for giving us some more insight into that, because, regardless of size of company, this could be very detrimental into the future.

Thank you. I yield back, Mr. Chairman.

*Chairman Boustany. I thank you.

Mr. Reed?

*Mr. Reed. Thank you, Mr. Chairman. Interested in having a conversation about research and development, and what this BEPS project and tax policy is doing in regards to where R&D is located.

So, Mr. Sprague, I read your testimony and found some of your comments insightful here. For your member corporations or companies, most of their R&D is done where? I think I know the answer to that, but I just want to make sure we are clear on that.

And after the BEPS project, where do you see that impacting, and how does that negatively or positively impact that R&D component of your member companies?

*Mr. Sprague. Well, major U.S. multinationals will tend to do R&D in many places around the world. The life cycle of an R&D-intensive company coming from the U.S. is that R&D will start out being done in the U.S. But as the company grows, they will tend to look for excellence elsewhere. Sometimes that is in India. You know, sometimes that is in other places.

The effect of the BEPS process on the choice of location for R&D will be, I think, in two areas. One is for countries that do have an innovation box, they are putting on the table an incentive: Please move your R&D to our country. So every R&D-intensive company will look at that and make a decision as to whether it is worthwhile to move the R&D to the UK, for example, in order to take advantage of that innovation box.

The other incentive is a little more subtle, and that goes to the transfer pricing points. U.S. software companies are, by and large, organized in fairly efficient structures. They generally will have a centralized sales entity somewhere, and try to minimize the footprint and the higher tax market jurisdictions. And a big theme, as I noted in my testimony, of the transfer pricing is the market jurisdictions will try to attract income into the market countries and tax it there, so that counter to that, under the BEPS project, is to move high-value functions -- not just R&D, but high-value management functions -- into places like Ireland, for example, in order to provide a counterweight to the Germanies and Frances of the market jurisdictions.

So, when thinking about how the BEPS project will influence the decision of companies where to locate high-value jobs, the R&D part is part of it. But the high-value job generally -- not just R&D -- is also a part of it.

*Mr. Reed. So, what is your recommended course, as to try to avert that situation, going forward?

*Mr. Sprague. Well, the --

*Mr. Reed. The Boustany-Neal bill. I heard it over here, but --

[Laughter.]

*Mr. Sprague. Yes. No, as I said in the testimony, we think the single best thing is comprehensive international tax reform with a competitive U.S. innovation box to make it more attractive for U.S. companies to keep the R&D here.

*Mr. Reed. And, obviously, we have had that conversation at length today about the possibility of that occurring. And, you know, not very optimistic that is going to happen any time soon.

So there -- is there any short-term -- I always operated -- when I was in private business, I always had a short-term, mid-term, long-term plan. Obviously, if we could get to tax reform on a comprehensive basis, you know, that is something that I would love to see on a short term horizon. Highly unlikely, in my opinion, we are going to get there in the next six months or

thereafter. So is there anything we could be focusing on from the panel to try to stop this loss of high-value, high-functioning R&D activity that you would recommend to us?

*Ms. Schultz. You could make the R&D tax credit permanent. That would help a lot. The fact that the credit is short-term, and always expiring, is really detrimental to long-term planning by companies. And having that assurance would really be great. If you want to do anything, make the R&D tax credit permanent.

*Mr. Reed. I appreciate that very much. And I think -- hopefully, we can get that taken care of sooner, rather than later. So I appreciate that input.

Anything else, Ms. Angus or Mr. Sullivan, in regards to short-term -- because I am really concerned about the loss. Once you lose that R&D, once you lose those high-value positions, it is tough to get that back. So any short, mid-term, other than permanency of the R&D tax credit, which I totally appreciate and totally support? Anything else anyone else could offer for us?

*Ms. Angus. I think that the permanent R&D credit is certainly important. I think that comments that have been made earlier with respect to the BEPS project, the importance of continuing the work, and now pushing it in the direction of trying to ensure fair, effective, and a transparent tax administration around the world, to counter some of the potential for aggressive interpretations of some of the proposals that would -- for example, overreach in the transfer pricing area is a really important thing to continue to work on. None of that, of course, is a substitute for all the work that you all are doing on tax reform.

*Mr. Reed. I appreciate that, Ms. Angus. And that is the action 13 issue that we talked about earlier with Mr. Stack from the Treasury Department.

With that I yield back. I notice my time is up.

*Chairman Boustany. I thank the gentleman. I want to thank all of you for your expert testimony. This has been very helpful. We have gleaned a lot of valuable information.

And I'd like to also advise you that Members may submit written questions to be answered in writing. Hopefully you can get back to us within a couple of weeks with that.

With that, the committee stands adjourned.

[Whereupon, at 12:26 p.m., the subcommittee was adjourned.]

[Public Submissions for the Record](#)