INVESTMENT COMPANY INSTITUTE

MEMO# 27706

November 19, 2013

Senate Finance Committee Proposals for International Tax Reform

[27706]

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TO: ADVISER DISTRIBUTOR TAX ISSUES TASK FORCE No. 11-13
TAX COMMITTEE No. 35-13 RE: SENATE FINANCE COMMITTEE PROPOSALS FOR INTERNATIONAL TAX REFORM

Senator Max Baucus (D – Montana), Chairman of the Senate Finance Committee, has released a staff discussion draft on international business tax reform. [1] The Finance Committee staff plans to release additional discussion drafts later this week.

The staff discussion draft proposes a number of reforms. These reforms are intended to be revenue-neutral in the long-term and coupled with a reduction in the corporate tax rate that is paid for by a broadening of the corporate tax base. The proposals are meant to be considered together and not as stand-alone provisions.

The staff proposals include:

1. Taxing all foreign income of U.S. companies immediately or not at all. This would be accomplished by:
    - Taxing passive and highly mobile income annually at full U.S. rates.
    - Taxing income from selling products and providing services to U.S. customers annually at full U.S. rates with limited exceptions.
    - Taxing income from products and services sold into foreign markets under one of two options:
        - A minimum tax that immediately taxes all such income at 80% (or some other percentage) of the U.S. corporate tax rate with full foreign tax credits, coupled with a full exemption for foreign earnings upon repatriation; or
        - A minimum tax that immediately taxes all such income at 60% (or some other percentage) of the U.S. corporate rate if derived from active business operations but at the full U.S. rate if not, coupled with a full exemption for foreign earnings upon repatriation.
    - Subjecting earnings of foreign subsidiaries from periods before the effective date of the proposal that have not been subject to U.S. tax to a one-time tax at a reduced rate of, for example, 20%, payable over eight years.
    - Allowing credits, with some exceptions, for taxes paid to foreign jurisdictions to

the extent the associated income is subject to U.S. tax.

2. Eliminating opportunities to avoid U.S. tax on U.S. income by:
    - Limiting interest deductions for domestic companies to the extent that the earnings of their foreign subsidiaries are exempt from U.S. tax and to the extent that the domestic companies are over-leveraged when compared to their foreign subsidiaries.
    - Limiting income shifting through tangible property transfers.
    - Denying deductions for related-party payments arising in a base erosion arrangement.
    - Repealing the domestic international sales corporation rules.
    - Limiting the extent to which foreign tax credits can eliminate U.S. tax on income from investments in foreign companies that are not controlled foreign corporations.
    - Restoring withholding taxes on interest paid by domestic corporations to residents of countries not providing similar benefits for U.S. investors.
    - Preventing foreign investors from using partnerships to avoid U.S. taxation.
3. Modernizing and simplifying other international tax rules by:
    - Eliminating parts of the “check-the-box” rules under which U.S. multinationals can disregard certain foreign subsidiaries for U.S. tax purposes.
    - Simplifying the foreign tax credit rules.
    - Apportioning interest expense on a worldwide basis for purposes of matching interest expense to income generated by borrowed funds.
    - Modernizing the rules applying to overseas banking and insurance businesses.
    - Simplifying the rules for taxing passive foreign investment companies (PFICs).
    - Modernizing the rules addressing foreign investment in U.S. real estate.

The Finance Committee staff has asked for comments on this discussion draft by January 17, 2014. We will discuss these proposals on the Tax Committee call on Thursday, November 21, 2013; [2] later calls will be scheduled if necessary.

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endnotes

[1] The discussion draft, as well as a summary and technical explanation, can be found on the Senate Finance Committee website here.

[2] See Institute Memorandum (27698) dated November 13, 2013.