July 17, 2017

The Honorable Orrin Hatch
Chairman Senate Finance Committee
219 Dirksen Building
Washington, D.C. 20510

Dear Chairman Hatch:

The Information Technology Industry Council (ITI) hereby submits feedback on tax reform in response to your June 16, 2017 request for input. ITI represents 60 of the leading information and communications technology companies headquartered both in the United States and abroad.[1] ITI is the voice of the high-tech community, advocating for policies that advance US leadership in technology, promote innovation, open access to new and emerging markets, protect and enhance consumer choice, and foster increased global competition. ITI's member companies include wireless and wireline network equipment providers, computer hardware and software companies, Internet and digital service providers, mobile computing and communications device manufacturers, consumer electronics, and network security providers.

The technology sector consists of innovative industries that transform our daily lives and propel economic growth both at home and abroad. The innovations that emerge from our sector launch new global industries and underpin the solutions to many of the largest challenges faced by international society today. At the same time, the decisions made by governments about how to treat technology firms have a significant impact on economic growth and job creation. Today, the global economy is digitized and data-driven. Through the innovation of ITI members the private sector has capitalized on this dynamic marketplace to provide jobs for millions of Americans and led the world in technological advancements. This innovation and job creation are undermined by a tax system that does not reflect the economic realities of the 21st century.

Modernizing our tax system is of paramount importance to the success of ITI members and innovative industries more broadly. This moment presents a unique opportunity to enact meaningful reform that lowers the corporate rate, adopts a territorial-based system, and fosters innovation to create economic growth for future generations.

[1] For more information on ITI, including a list of its member companies, please visit: http://www.itic.org/about/member-companies.

The United States is the only major economy with both a high corporate tax rate and worldwide system. There is widespread recognition that our economic competitiveness has been hindered by this antiquated approach to tax. Since 2003, the average corporate income tax rate decreased from 30 percent to 22.5 percent as countries also moved with purpose to adopt territorial tax systems.

Today, at 35 percent, the United States has one of the highest marginal corporate tax rates in the world. This high rate operates as a deterrent on domestic investment and job creation. ITI members are unified in support of broadening the base to lower the rate. Conversations about how to achieve this goal often begin with questions about treatment of expensing as well as interest treatment. ITI companies feel strongly that expensing is a timing issue and that a lower rate is far more important than more robust cost recovery. As such, we would support the Senate Finance Committee limiting expensing and applying those savings to a lower corporate rate.

Interest treatment is a bit more complicated as it is foundational to certain business models and therefore critical to a number of our members. Arguments that equity and debt are similar misunderstand real world business practices. Debt and equity are not interchangeable forms of financing. There are numerous non-tax reasons that businesses choose debt over equity when raising capital. Many businesses do not have access to equity markets, making debt their only option to start and grow enterprises that in turn create new jobs. Borrowing also allows owners to access capital without diluting control of their business. In addition, debt is a cheaper financing solution than equity because it is more secure for investors, who charge a premium for the risks associated with equity. Proposals offering 100 percent expensing in place of interest deductibility particularly miss the mark. As such, we ask Senate Finance to be mindful of changes to the long held tax treatment of interest. Any changes must not upend operations. It is essential to allow companies time to transition to any new approach to debt treatment.

Beyond the rate, international tax issues are an urgent concern for our member companies. In fact, the profile of these issues grows year over year. Increasingly multilateral bodies and individual countries have moved to raise revenues and confront cross-border tax policy questions aggressively while the United States remains static in its broken system. Tax reform is urgently needed to create a system for our modern, technology driven economy and mitigate the impact of aggressive foreign actions on ITI member companies and United States interests.

Actions from other economies have created a true sense of urgency in this space. Recent actions such as the European Commission State Aid cases, changes to withholding tax regimes and other policies targeted at the “digital” economy (when increasingly the entire economy is

digital) have departed dramatically from the agreed upon multilateral approach often to the potential detriment of the United States Treasury. These policies target US-headquartered companies' IP-related income to collect revenues for treasuries around the world. Furthermore, we have seen a number of proposals intended to shift the international tax system to be based on data collection or where servers are located. Such an approach will impact more than e-commerce as these policies will touch every business that uses digital technology in its value chain. These aggressive policies are often coupled with strong incentives to attract key economic activity like research and development into lower tax regimes in those countries. This is a one-two punch for the United States. First, by having a disproportionate negative effect on US-headquartered firms, these policies have the effect of eroding the US tax base. Second, by offering generous tax cuts for locating IP-related operations, the ability of companies to create jobs in the United States suffers, which also weakens the US tax base and our economic health.

Adopting a competitive territorial tax system is essential to addressing these dynamics and aligning our system with the rest of the world. ITI member companies support a 95 percent dividend deduction regime such has been proposed in past efforts at international reform. We also recognize the Senate Finance Committee and other policy makers are examining so-called base erosion policies to couple with a territorial system. Given the extent and nature of our member's global operations, there are few aspects of reform more potentially consequential.

ITI companies have divergent opinions on the best way forward. What we can offer are some broad principles for your consideration given the diversity of businesses and experience globally. Overall, any base erosion policy should cause as little friction as possible in overseas operations and should not overtly penalize specific sectors of the economy. It is essential to note that the US will remain an outlier in comparison to most major economies in pursuing such an approach. Given this reality, we hope policymakers contemplate the impact on competitiveness of any policy implemented in this space. Furthermore, we note that a number of past reform efforts have targeted income related to intellectual property, raising basic concerns from some of our members about how intellectual property is defined as well as practical concerns about the complexity of implementing such a policy and the likely compliance burdens faced by both the taxpayer and the US Treasury as an entire layer of complexity is added to the Subpart F rules. Overall, the details of an IP-related policy or any other approach to "base erosion" will be a critical concern for our member companies. As you think through these policies, we would encourage the committee to pursue a balanced approach to the treatment of intangibles whereby deterrents and incentives are more equalized. Our companies operate in a very competitive global environment and tax reform take a balanced approach. Regardless of approach, we ask that you provide ample time for review and feedback about proposals in this area.

The treatment of offshore earnings is another critical concern in a transition to a territorial system. Because companies have been operating overseas for decades, reinvesting significant capital and making acquisitions of foreign businesses, their success abroad is integral to their success at home. Taxing these assets at any significant level will hinder companies' ability to remain competitive. Thus, distinguishing between short-term cash reserves and long-term investments is essential.

With the reform goal of global competitiveness in mind, ITI companies support a bifurcated approach similar to the provision included in the House tax reform blueprint, which we believe has broad Congressional support, that would apply an 8.75 percent tax to accumulated foreign earnings held in cash and cash equivalents and a 3.5 percent tax to accumulated foreign earnings invested in other assets. For companies that have invested outside of the United States, a reduced tax below ten percent on such assets, as well as the ability for companies to pay this tax liability over eight years with no interest charge, is of particular importance.

The third priority for ITI members are incentives for innovation. Although the United States is the global leader in innovative technologies, we have fallen behind in embracing a similarly-innovative approach to tax policy. As countries around the world increasingly modernize their tax systems, innovation incentives have been a key focus. By targeting and encouraging private sector investment in patents, intellectual property, manufacturing, and research and development (R&D), many of our trading partners offer generous incentives – such as tax allowances, credits, and withholdings – for companies to develop new and creative technologies in-country. This investment not only spurs greater domestic growth, but it also helps foster an economic environment that is conducive for investment in vanguard technologies. By coupling frontend incentives, like R&D tax credits on the wages of R&D workers, with back-end incentives, like innovation boxes, foreign governments are laser focused on attracting such economic activity.

We were pleased by recent the passage of a permanent R&D credit and view it as a critical step towards a more competitive, 21st century tax regime. We encourage you to retain the credit and expand the alternative simplified credit rate to 20 percent. Beyond the R&D credit, tax reform provides an ideal opportunity to further craft policies to ensure the United States remains the global leader in innovative technologies. One such idea is the adoption of an innovation box. Many OECD countries – among them key US trading partners – have begun to embrace such policies as a part of a broader national tax strategy to encourage in-country investment in innovation and job creation. There are questions as to what the ideal innovation box would look like in a domestic context, so we encourage continued conversations about how this concept could work in the United States.

Lastly, we would like to share some feedback regarding Treasury's review of tax regulations issued in 2016. ITI was pleased to see that on July 7th, Treasury issued a notice identifying eight regulations, including four suggested by ITI, that will be reviewed. The four regulations related to: the requirement of taxpayers to retroactively create records for all foreign assets and liabilities to track and covert the daily value of each foreign transaction into dollars using the relevant same-day currency valuation (Section 987); the elimination of taxpayers' ability to transfer foreign goodwill and going concern value to a foreign corporation without immediate or future US income tax (Section 367); the allowance of outside counsel to review records summoned by the IRS and participate in testimony to examine the correctness of a tax return (Section 7602); and the establishment of minimum documentation requirements for tracking debt and equity-related transactions (Section 385). We appreciate Treasury's diligence in examining the impact these regulations would have not only on the technology sector, but on American industry at-large and encourage the Senate to support the efforts of the Administration to reduce the regulatory burden on taxpayers.

Thank you for the opportunity to provide feedback. We look forward to working with you on tax reform in the coming months.

Sincerely,

Jennifer McCloskey
Director, ITI