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October 15, 2009

The President's Economic Recovery Advisory Board
The White House
1600 Pennsylvania Avenue
Washington, DC 20500

Dear Advisory Board Members:

On behalf of Business Roundtable, I am submitting the attached recommendations outlining Business Roundtable's principles for achieving a competitive corporate tax system to enhance U.S. economic growth and stimulate job creation.

The principles set forth the need for:

- Establishing a corporate tax rate competitive with the rates of our major trading partners
- Providing international tax rules that provide a level playing field for American companies and their foreign-headquartered competitors, and
- Providing an expanded and permanent R&D tax incentive to maintain the United States as an attractive location for innovation and research.

I would be pleased to meet with the Advisory Board and its staff to provide you any additional information to assist you in this important work.

Sincerely,

John J. Castellani

Attachment: *A Competitive U.S. Corporate Tax System Will Create More and Better Paying Jobs and Increase U.S. Economic Growth*

A Competitive U.S. Corporate Tax System
Will Create More and Better Paying Jobs
and Increase U.S. Economic Growth

Business Roundtable believes it is essential for the recovery of the U.S. economy and for future economic growth that the United States adopt a competitive corporate tax system. The corporate tax system is a key factor influencing investment in the United States and affecting the ability of U.S. companies to compete globally with their foreign-headquartered counterparts. Strong growth of U.S. companies results in substantially more and better paying jobs for American workers now and for future generations of American citizens.

Business Roundtable is an association of chief executive officers of leading U.S. companies with more than $5 trillion in annual revenues and more than 12 million employees. Member companies comprise nearly a third of the total value of the U.S. stock markets and pay more than 60 percent of all corporate income taxes paid to the federal government. Annually, they return more than $167 billion in dividends to shareholders and the economy. Business Roundtable companies give more than $7 billion a year in combined charitable contributions, representing nearly 60 percent of total corporate giving. They are technology innovation leaders, with more than $111 billion in annual research and development spending – nearly half of all total private R&D spending in the U.S. Business Roundtable companies have a significant multiplier effect on the U.S. economy through the many small and medium-sized businesses serving as their suppliers and by the spending of their employees.

Because of the breadth of companies represented by Business Roundtable members -- spanning industries as diverse as energy, manufacturing, consumer goods, high-tech, transportation, communications, healthcare, retail, finance, and other services -- our CEOs have a keen insight into the factors that are required to ensure strong growth throughout the nation's economy.

With respect to taxes, our members believe the following three principles are essential to promoting greater economic growth, creating jobs, and achieving a higher standard of living for all Americans:

1. Competitive corporate tax rates are needed to improve the ability of American companies to expand and create jobs.

2. The U.S. system of international taxation needs to provide U.S.-headquartered companies the same ability to compete internationally as the tax systems of our major trading partners provide for their companies.

3. An expanded and permanent R&D tax incentive is necessary to maintain the United States as an attractive location for innovation and research.

Tax reform guided by these principles, while maintaining incentives for domestic investment through a competitive and pro-growth capital cost recovery system, will enhance the attractiveness of the United States as a location for American companies to be headquartered and for increased investment and production of goods and services. A tax system designed around these principles will foster job creation, stimulate economic growth, and result in a higher standard of living for all Americans.

Below we provide more detail on these essential principles for economic growth.

1. A Competitive Corporate Tax Rate

It is well known that the U.S. corporate tax rate, which after the 1986 Tax Reform Act became one of the lowest in the world, is now the second highest among the 30 OECD countries. The high U.S. corporate tax rate diminishes investment in the United States and leads to fewer jobs and lower wages for American workers. A sustained economic recovery requires significant job growth in the United States. A competitive corporate tax rate is critical to this recovery.

The average combined (federal and state) U.S. corporate statutory tax rate is 39.1 percent in 2009 (comprised of a 35 percent federal rate and an average 6.3 percent deductible state income tax). The U.S. rate is 50 percent higher than the average combined corporate statutory tax rate of the other 29 OECD countries in 2009 -- 25.9 percent. Weighting OECD countries by GDP, the U.S. rate is 30 percent higher than the weighted-average corporate tax rate of the other 29 countries -- 30.1 percent (**Figure 1**).[1]

The high statutory tax rate of U.S. companies translates into a higher effective tax rate for U.S. companies relative to their foreign competitors. A recent comprehensive cross-country study of financial statement information by accounting researchers Kevin Markle and Douglas Shackelford found that U.S. corporations have above average effective tax rates, higher than all other trading partners except Japan and Germany during the study period.[2] For example, worldwide American companies were shown to have effective tax rates of 30 percent between 2003 and 2007, compared to 39 percent for Japan, 33 percent for Germany, 28 percent for France and the United Kingdom, 26 percent for Canada, and 18 percent for China. .

A significant reduction in U.S. corporate statutory tax rates is needed to be competitive with the tax systems of our major trading partners. Holding state tax rates constant, the U.S. federal statutory rate would need to decline to about 20.9 percent in order to match the average non-U.S. OECD rate of 25.9 percent. Alternatively, to match the GDP-weighted average non-U.S. OECD rate of 30.1 percent, the U.S. federal statutory tax rate would need to decline to about 25.4 percent.

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[1] OECD Tax Database http://www.oecd.org/ctp/taxdatabase

[2] Kevin Markle and Douglas Shackelford, "Do Multinationals or Domestic Firms Face Higher Effective Tax Rates?" National Bureau of Economic Research, June 2009.

Statutory tax rates have fallen considerably in the rest of the world over the past decade and continue to decline. Canada, for example, has reduced its corporate rate by over 3 percentage points between 2007 and 2009 and is scheduled to lower its rate by an additional 4 percentage points between 2009 and 2012 -- for a total reduction of 7 percentage points between 2007 and 2012. The United States can not afford to sit still while the rest of the world garners an increasing share of economic activity.

High corporate tax rates discourage investment and result in lower wages for American workers. Lower corporate tax rates would make the United States a more attractive location for investment for both U.S. and foreign companies. Increased investment would result in more jobs and more opportunity for American workers. Higher productivity of workers made possible by this increased investment would increase wages and result in higher living standards for American workers.

2. A Competitive International Tax System

The world has become significantly more integrated. Reductions in the cost of communication and transportation and falling trade and investment barriers have opened the door to competition on a truly global scale. American corporations and American workers stand to benefit from the economic growth and higher living standards made possible by these new markets for growth.

American companies with overseas operations provide substantial benefits to the American economy. In 2007, worldwide American companies in all industries employed 22 million workers in the United States and supported more than 41 million U.S. jobs through their supply chains and spending by the people they employed directly or indirectly.[3] The global activities of U.S.-headquartered companies are concentrated in the United States. Employees in the United States accounted for two-thirds of the employment of worldwide American companies. Approximately 70 percent of the value added of worldwide American companies was created in the United States in 2007.[4] Worldwide American companies made 74 percent of their capital expenditures in the United States in 2007. Worldwide American companies undertook 85 percent of their research and development expenditures in the United States.

While worldwide American companies have a decidedly U.S. composition, the future growth of these companies is staked on expanding into the foreign markets that represent 95 percent of the world's consumers. Foreign operations of worldwide American companies open up new markets for sales of American-made goods and services. Approximately 89 percent of the foreign production of worldwide American companies is sold to foreign customers. As American companies expand abroad, they expand at home. Worldwide American companies account for 49 percent of all exports from the United States. Each 10 percent increase in sales

[3] Business Roundtable analysis based on data from Bureau of Economic Analysis.
[4] See "U.S. Multinational Companies: Operations in the United States and Abroad in 2007," *Survey of Current Business*, August 2009.

by overseas affiliates of worldwide American companies increases their U.S. exports to these affiliates by 6.5 percent and increases their research and development expenditures in the United States by 5 percent.[5]

Worldwide American companies face substantial international competition. Whereas in 1960, 18 of the world's 20 largest companies were headquartered in the United States, in 2008 only 7 were U.S. based. The ability of worldwide American companies to compete successfully requires a level playing field with their foreign-headquartered counterparts. U.S. companies -- unlike their typical foreign competitors -- owe tax on their foreign earnings both in the foreign country in which they are earned and at home when paid back to the parent company. In contrast, most of the world has adopted "territorial" tax systems under which foreign earnings are not subject to tax at home. Within the OECD, 25 of the 30 countries have adopted territorial tax systems, with Japan and the United Kingdom adopting territorial tax systems in 2009 (**Table 1**).

The United States is now an anomaly -- the only high tax rate country in the OECD that subjects its companies to an additional level of tax when foreign earnings are paid back to the parent company.[6]

The Administration has proposed in its 2010 Budget further tax increases on worldwide American companies. These taxes would significantly increase the tax burden on overseas operations and could have significant unintended consequences that will reduce the competitiveness of U.S. companies relative to their foreign competitors.

The rules proposed by the Administration are without parallel elsewhere in the world:

- They would disallow deductions for expenses incurred in the United States for interest and headquarters' expenses when a U.S. company does not currently repatriate all of its foreign earnings. No other country to our knowledge imposes any similar limit on deductibility of expenses.[7] The proposals would make it more costly to undertake high-wage headquarters activities in the United States. They would also raise the cost of using debt to finance capital expenditures in the United States, likely reducing domestic investment. Strikingly, the proposals would have no effect on the cost of debt finance for foreign-headquartered companies borrowing in the United States.

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[5] Mihir Desai, C. Fritz Foley, and James R. Hines, Jr., "Domestic Effects of the Foreign Activities of US Multinationals," *American Economic Journal: Economic Policy*, February 2009

[6] The four other OECD countries not using a territorial tax system are Ireland, Korea, Mexico and Poland. The average corporate tax rate in these four countries is 20.9 percent, with Ireland having the lowest rate at 12.5 percent and Mexico having the highest rate at 28 percent. Given their significantly lower corporate rate, companies based in these countries would face a much lower domestic tax, if any, relative to a U.S. company upon receipt of foreign earnings.

[7] In certain territorial countries, interest on debt directly traceable to exempt foreign income, such as debt used to acquire a foreign subsidiary, may be disallowed. Such a case is distinguished from the Administration's proposal which would apply to all debt, without regard to its uses.

- The proposals would reduce the ability to receive a full tax credit on foreign earnings received from countries with higher than average tax rates. As a result, the proposal would create new impediments that would discourage repatriations of foreign earnings to the United States.

- The proposals would also create inefficiencies that would result in higher tax payments by U.S. companies to foreign governments on their foreign operations, they would reduce the ability of American companies to redeploy cash between foreign operations on the same tax terms as their foreign competitors, and they would reduce the ability of American companies to grow and integrate foreign acquisitions.

In sum, the Administration's international tax proposals would create additional tax disadvantages for American companies relative to their foreign competitors and reduce the competitiveness of American companies in foreign markets.

At a time when we need to promote the growth of U.S. companies both here and abroad by providing a more competitive tax system for U.S. companies, the proposals would go in the opposite direction by creating new barriers to their growth and significantly reducing the ability of U.S. companies and U.S. workers to compete globally. As a consequence, the U.S. economy would suffer from the significant loss of good-paying U.S. jobs, and the reduced role of worldwide American companies in international commerce would lead to a decline in U.S. world leadership.

3. Competitive Incentives for Research and Innovation

Technological advances made possible by research and development in the United States are responsible for a significant share of U.S. economic growth. Innovation brings new jobs for the American workers. As noted by the Council of Economic Advisers, in 2003 a quarter of American workers were in jobs that were not even listed among the Census Bureau's Occupation codes in 1967.[8] In a knowledge-based economy, continual innovation is required to sustain a competitive advantage. American industry supports two-thirds of R&D spending in the United States.

While private industry is the main source of R&D and innovation in the U.S. economy, economists recognize that industry will tend to undertake too little R&D because much of the return to those investments cannot be fully appropriated by those who undertake it. R&D activities generate classical "spillover" benefits to the economy, with the result that the total benefit from R&D exceeds the return to private innovators. One recent study concluded that a conservative measure of the social rate of return to R&D investments is 30 percent and optimal

[8] Council of Economic Advisers, "Preparing the Workers of Today for the Jobs of Tomorrow," July 2009.

spending on R&D is more than two to four times greater than actual spending in the United States.[9]
Government support for U.S. R&D is therefore critical to achieving efficient levels of R&D in the U.S. economy, increasing worker productivity, and propelling U.S. economic growth. R&D in the United States is supported by direct federal spending and through the R&D tax credit. Despite being a provision of the tax code since 1981, the R&D tax credit has always been enacted on a temporary basis, creating uncertainty for business whether the support provided by the credit can sustain long-term investment plans. Under current law, unless extended, the R&D tax credit will expire at the end of 2009.

Other nations recognize the importance of providing support through the tax system for R&D. An OECD study finds that the United States ranks low in the degree of tax benefit provided through the tax system for R&D -- ranking 23rd out of 38 countries.[10] Countries with greater tax benefits for R&D include many OECD countries, including Canada, France, Japan, Korea, Mexico, and the United Kingdom, as well as quickly growing economies, including Brazil, India and China.

It is essential that the United States provide sufficient support to R&D to ensure that the technological edge of the U.S. economy is sustained. Business Roundtable supports an expanded and permanent R&D tax incentive to maintain the United States as an attractive location for innovation and research.

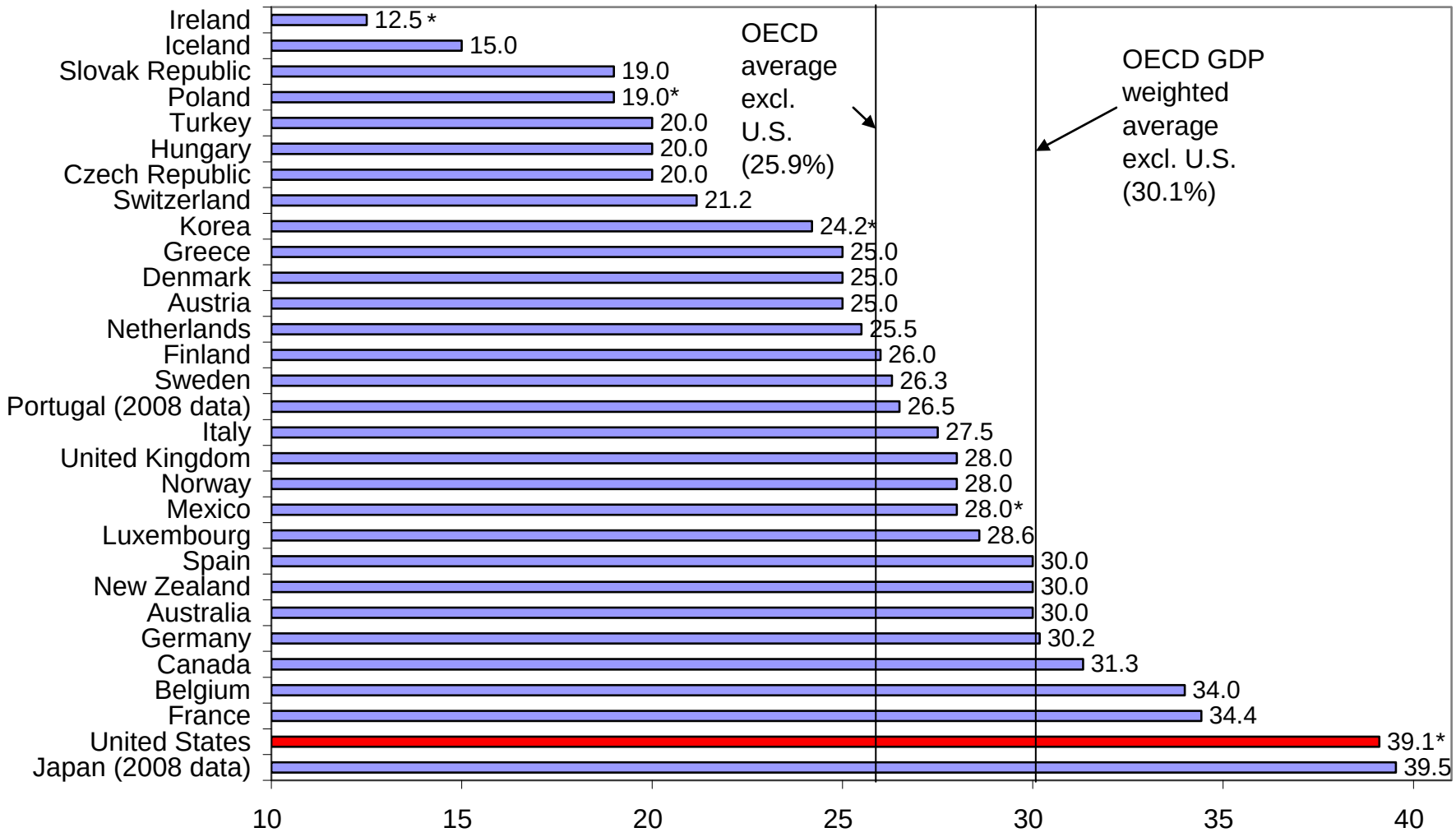
4. Summary

It is critical to modernize U.S. tax policy to allow American workers and companies to compete effectively at home and abroad, promote economic growth, create jobs, and achieve a higher standard of living for all Americans. The principles set forth in this submission provide the key design features necessary to achieve these important objectives.

[9] Charles I. Jones and John C. Williams, "Measuring the Social Return to R&D," Board of Governors of the Federal Reserve System, 1997.
[10] OECD, "Science, Technology and Industry Scoreboard 2007."

FIGURE 1

Combined (Federal and State) Corporate Income Tax Rate, OECD Countries, 2009



*Indicates country taxes worldwide income. All other OECD countries have territorial systems.

Source: Tax rates from OECD Tax Database, 2009; 2007 GDP weights

TABLE 1
OECD Home Country Tax Treatment of Foreign-Source Dividend Income Received by Resident Corporations

Territorial	Worldwide Taxation
1. Australia	1. Ireland
2. Austria	2. Korea
3. Belgium	3. Mexico
4. Canada	4. Poland
5. Czech Republic	**5. United States**
6. Denmark	
7. Finland	
8. France	
9. Germany	
10. Greece	
11. Hungary	
12. Iceland	
13. Italy	
14. Japan	
15. Luxembourg	
16. Netherlands	
17. New Zealand	
18. Norway	
19. Portugal	
20. Slovak Republic	
21. Spain	
22. Sweden	
23. Switzerland	
24. Turkey	
25. United Kingdom	

Note: In general, tax treatment depends on qualifying criteria (e.g., minimum ownership level, minimum holding period, the source country, the host country tax rate). The table reports the most generous treatment of foreign direct dividends in each case.