PRACTICAL INTERNATIONAL
CORPORATE FINANCE STRATEGIES

THOMSON REUTERS
WORLDTRADE EXECUTIVE

www.wtexecutive.com
The International Business Information Source™

March 31, 2012
Volume 38, No. 6

Man Bites Dog: Obama Proposes a Corporate Tax Rate Reduction

New Provisions for U.S. Companies with Foreign Operations

BY JOSEPH B. DARBY III (GREENBERG TRAURIG LLP)

The classic maxim of the newspaper business, coined by a British newspaper magnate named Alfred Harmsworth, is this: "When a dog bites a man, that is not news, because it happens so often. But if a man bites a dog, that is news." A similar adage is, "You never read about a plane that did not crash."

Now comes President Barack Obama, fresh from proposing new tax hikes on the wealthy, with an out-of-right-field proposal for a reduction in U.S. corporate income tax rates. Hold the presses! A man just bit a dog. THE MAN just bit the bullet. This is what I call a REAL NEWS STORY.

There is, as always, more to this story than the headlines can convey. It is ab-

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UK Government Announces Reform of the UK Competition Regime

BY FRANCES MURPHY, LYNETTE ZAHN AND FRANCESCO LIBERATORE (JONES DAY)

On March 15, 2012, the UK Government announced its plans for reforming the UK competition regime. The Government has stopped short of radically redesigning the competition regime. Although one government body is replacing two, and there are significant changes expected for criminal prosecutions, in large measure the new regime will maintain elements of the current system.

A New Competition Authority

Externally, the most significant change in the new plan is that the UK's Competition Commission (CC) and Office of Fair Trading (OFT) will merge into a single body: the Competition and Markets Authority (CMA). The CMA will be responsible for market investigations, cartel and antitrust cases and merger control as well as a number of functions with respect to the regulated utilities. The CMA will be subject to tighter procedural timetables and improvements in due process for the parties being investigated.

The changes will be introduced gradually, as some proposals are subject to

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solutely true that President Obama is proposing a reduction in the maximum U.S. corporate tax rate, from 35 percent to 28 percent. (Not low enough yet, but at least a step in the right direction.) It is further true that the rate reduction is accompanied by an even more commendable proposal to eliminate many of the expensive and economy-distorting tax incentives that have come to junk up the Internal Revenue Code. (This is seriously good stuff if the proposal is sincere and not just election-year posturing—more on this in a moment.) Most importantly of all, the President's proposal puts this critical and long-over due issue front and center in the national debate.

That's the good news. Now for the REAL news.

Summary of the Proposal

"The "President's Framework for Business Tax Reform" ("Obama Proposal" or "Proposal")[1] would:

1. reduce the maximum U.S. federal corporate income tax rate from 35 percent to 28 percent. That is a step in the right direction, but would still leave U.S. corporate income tax rates (after taking account state-level corporate income taxes) at approximately 33 percent, which is still one of the highest corporate income tax rates in the world.
2. eliminate a large number of current tax incentives, ranging from popular tax credits to accelerated depreciation, used by corporations to reduce their effective income tax rate (as opposed to the nominal maximum corporate tax rate, which gets far more attention than it deserves). The combination of reduced tax rates coupled with far fewer tax incentives is a great idea in principle, but the Proposal does not fully honor or achieve that objective, in part because it adds a host of new tax benefits to replace the ones being eliminated. Overall, despite reducing the maximum tax rate, the Proposal is projected to result in a net increase in U.S. corporate taxes.
3. impose a "minimum tax" that includes (and thus taxes currently) income from foreign subsidiaries of U.S. companies. Many observers believe the U.S. corporate tax system should adopt or otherwise embrace the principles of territorial taxation, and this element of the Proposal moves in exactly the opposite direction, strengthening U.S. worldwide taxation with unpredictable but potentially damaging consequences. This aspect of the Proposal is analyzed in substantial detail, below.

Devil in the Details

The Obama Proposal correctly recognizes that the Internal Revenue Code is a mess: U.S. corporate tax rates are too high (as of April 2012 they will be the highest in the world), and this fact by itself stifles domestic economic growth, encourages U.S. companies to move operations to lower tax jurisdictions overseas, and generally harms the competitiveness of U.S. companies against foreign rivals. Moreover, the Code is stuffed with all manner of gimmicky tax incentives, which are supposed to, in theory, represent important policy priorities of the U.S. government, but which, in practice, mainly serve to funnel money to politically favored constituencies. In addition to wasting money on "political purchases," the proliferation of tax incentives generally distorts the U.S. economy by creating an unlevel playing field, by allowing Congress (instead of the marketplace) to

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Practical International
Corporate Finance Strategies

The International Business Information Source™
(ISSN 1070-9215)

EDITORIAL OFFICE
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part of Thomson Reuters
P.O. Box 761
Concord, MA 01742-0761/USA
(978) 287-0301 Phone
(978) 287-0302 Fax
www.wtexecutive.com

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PUBLISHED TWICE A MONTH FOR SUBSCRIBERS ONLY

SUBSCRIPTION INFORMATION: Annual subscription: US$1405 (add $50 for non–US postage) Single copy: US$65

European General Court Confirms Parental Liability for Competition Law Infringements by 50:50 Joint Ventures

BY PHILIP BENTLEY QC AND PHILIPP WERNER
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The European General Court (GC) has confirmed a European Commission decision to hold chemical companies EI du Pont de Nemours and Dow Chemical jointly and severally liable for a fine imposed on their 50:50 joint venture (JV) for an infringement of European competition law *(EI du Pont de Nemours and Company v Commission T-76/08* and *The Dow Chemical Company v Commission T-77/08).* In light of this judgment, parent companies would be well advised to check that their 50:50 JVs are compliant with EU competition rules.

Parental Liability under EU Competition Law

According to EU competition law, the anti-competitive behavior of a subsidiary may be imputed to the parent company where the subsidiary does not decide independently on its own market conduct but carries out, in all material respects, instructions given to it by its parent company. Thus, a subsidiary that is a legal entity separate from its parent company could be considered as part of the parent company's group, if the parent company exercises a decisive influence on it. In cases of wholly-owned subsidiaries, there is a rebuttable presumption not only that the parent company is able to, but that it does exercise a decisive influence.

In cases where the subsidiary is not wholly-owned, it is, however, for the Commission to show that the parent company is able to, and does, exercise a decisive influence. Until now, it was not clear how the Commission would deal with full-function JVs, in particular 50:50 JVs that were controlled jointly by their parent companies, bearing in mind that "full function" means that the JV operates independently on the market.

Application of EU Rules on Horizontal Agreements Involving 50:50 Full-Function JVs

Dow and Dupont were 50:50 JV partners in DDE. In proceedings relating to the chloroprene rubber cartel, the Commission imposed a fine of EUR 44.25 million on DDE and held Dow and Dupont jointly and severally liable for the fine. In the appeal proceedings, both Dow and Dupont challenged the finding that they were liable for the behavior of the joint venture. Their appeal was rejected and the Commission's decision was upheld by the GC on February 2, 2012.

It should be noted that in a 2005 decision the Commission had considered that there existed a presumption that a jointly controlled, full-function joint venture is autonomous (case COMP/F/38.443 – Rubber Chemicals, paragraph 263). The GC stated that the Commission could reverse this previous assessment without prejudice to the parties.

> **According to EU competition law, the anti-competitive behavior of a subsidiary may be imputed to the parent company, where the subsidiary does not decide independently on its own market conduct but carries out, in all material respects, instructions given to it by its parent company.**

The GC confirmed that in order to establish parental liability for a JV, the Commission needs to show that the parent companies were able to exercise decisive influence and that they did in fact exercise a decisive influence. As to the appreciation of influence, the GC ruled that the Commission could rely on the following elements as evidencing the exercise by these two parent companies of a decisive influence over a full-function, equally owned joint venture:

The strategic decisions (appointment and dismissal of directors, business and strategic plans, annual operating plans, banking policy, capital expenditure, and borrowing) were taken by a Members Committee appointed by Dupont and Dow. As both parties had a *de facto veto* right, they were required to cooperate permanently.

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The Members Committee appointed the top management posts of the JV.

The Members Committee agreed on the closure of a plant in the United Kingdom.

The parent companies exercised their management power over the JV.

After the cartel had ended, the parent companies ordered an internal investigation into whether the JV might have participated in the cartel, thus confirming that the parent companies had the power to require the JV to adopt a specific line of conduct on the market.

The parent companies appointed a chief legal adviser who had been a member of Dupont's legal department and who applied a competition law compliance programme at the JV that was based on the model applied previously at Dupont.

The GC made clear that the range of elements (whether legal or factual) that the Commission may rely on to establish the exercise of a decisive influence is wide, increasing substantially the scope of the parents' liability for their subsidiaries.

The Autonomy of JV under Merger Control Rules: Parental Liability Not Excluded

These cases also recall the difference between the operational autonomy of a full-function joint-venture and its economic autonomy.

Full-function joint ventures must be notified under the European Community Merger Regulation because they are autonomous from an operational point of view, i.e., they have sufficient resources to operate independently on the market. However, this autonomy does not mean that it can be assumed that the JV will decide independently on its own market conduct in a way that would exclude parental liability in the case of an infringement by the JV of EU competition law. Indeed, the parent companies may still take a decisive *economic* influence on the joint venture in taking strategic decisions and may still be liable for the JV's behavior under EU competition rules. ❏

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Canada Revenue Agency's New Audit Approach: "Risk Assessment" Interviews

BY PATRICK LINDSAY AND SAL MIRANDOLA
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What's Happening?

The Canada Revenue Agency (CRA) plans to conduct individual risk-assessment interviews with a select group of 50 large businesses in the near future. These taxpayers face the prospect of being labeled "high-risk," a designation that will likely come with significant costs related to increased audit scrutiny.

It is important for potential interviewees to understand what to expect from this process, and what their rights are, in order to prepare for the interview and determine the most effective way to participate.

CRA's New Audit Approach

The interviews are part of the CRA's new approach to large business audits. Instead of assigning audits based on a taxpayer's gross income,[1] the CRA intends to select audits based on "risk." At the interviews, the CRA is expected to: explain its new audit approach; provide information regarding its initial risk assessment of the taxpayer and identify issues of concern for the next audit cycle; and ask for information regarding the taxpayer's own assessment of its tax risks.

The interviews are part of the first phase of the new risk-based audit approach, which is being introduced gradually over five years. Within five years, the CRA plans to meet with all large file taxpayers to discuss their risk categorization.

Questions to Expect

Letters issued to the selected taxpayers request a meeting to discuss items including "the potential benefits of adopting an engaged approach to compliance." The letter attaches a proposed list of questions for taxpayers, which include:

- How are your tax risks identified, managed, reported and monitored? What are the names of the individuals involved in this process?
- Will you disclose your own analysis of your tax risks?
- Do you have a tax risk management committee? Who is on the committee? Will you provide meeting minutes?
- Describe a situation where you were not compliant and explain what you did.
- Do you use external tax planners? Are any paid on a contingency basis?

The questions invite taxpayers to disclose their own analysis of their tax risks. While most taxpayers may not object to providing the CRA with the necessary records to test the honesty and accuracy of their tax returns, it can be expected that many will take issue with disclosing their own mental impressions regarding their tax risks.

Taxpayers may challenge the reasonableness of the number, scope and availability of the documents requested.

How to Prepare

Taxpayers that participate in the interviews should prepare by:

- Reviewing the CRA interview request letter and considering the questions attached to the letter;
- Discussing the scope of the CRA's authority to compel answers to the questions and decide in advance how much information to provide at the meeting;
- Reviewing the internal processes for assessing tax risk and consider what information the CRA could compel the taxpayer to produce;
- Considering which individuals should attend, what materials to bring to the meeting, if any, and who will take meeting minutes; and
- Preparing questions for the CRA regarding the new risk assessment audit process including the benefits, costs, and specific changes the taxpayer can expect.

The most likely area of disagreement between the taxpayer and the CRA involves how much information the taxpayer should provide regarding its own assessment of its tax risks. As such,

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we discuss below: perspectives of the CRA and taxpayers on this issue; the scope of the CRA's authority to compel taxpayers to produce records; and the impact of the CRA's request for taxpayer's own tax risk assessments.

CRA: Taxpayers Must Self-Audit

The CRA's position is that taxpayers are obligated to disclose "concerns with regard to tax at risk" to assist the CRA to "identify audit issues."[2]

In other words, taxpayers must self-audit and disclose results to the CRA. The extent to which the CRA can compel disclosure of a taxpayer's own assessment of tax risks has not been tested in Canada. In the United States, the Internal Revenue Service has taken court action against taxpayers that declined to disclose such information, with mixed results.[3]

The extent to which the CRA can compel disclosure of a taxpayer's own assessment of tax risks has not been tested in Canada.

From the CRA's perspective, the audit process would be more effective and cost-efficient if taxpayers simply disclosed their own assessment of their tax risks; "The CRA's goal is to develop a useful and cost-effective program to better target its compliance efforts."[4]

Taxpayers: Must I Tell my Adversary Where I am Vulnerable?

Tax litigation is inseparable from the audit process because information gathered during an audit can be used against taxpayers in litigation. The CRA litigates tax issues regularly using the largest law firm in the country, the Department of Justice. As such, any requests for information from the CRA need to be considered knowing that the CRA has a dual role as both auditor and adversary.

The CRA's Authority To Access Records

Under the CRA's primary audit power, it has broad authority to "inspect, audit or examine the books and records of a taxpayer."[5] This authority is necessary for the CRA to carry out the purpose for which it exists – assessing taxpayer's accuracy and honesty within a self-assessment system. This authority imposes obligations on taxpayers to: maintain and disclose proper books and records; provide "all reasonable assistance"; and answer "all proper questions."[6]

Taxpayers should be aware that the CRA frequently asks for information that it cannot compel taxpayers to provide. For example, the CRA often requests access to legal opinions that are protected from disclosure by solicitor-client privilege.[7] The CRA also requests information for the purpose of auditing unnamed persons (for example, a client list), even though the CRA has no authority to demand such information without judicial authorization.[8] Taxpayers should consider the limits of the CRA's authority when considering an information request.

Since "risk-assessment" interviews are a new process and the scope of the compliance obligation is unclear, we expect considerable discussion between the CRA and taxpayers regarding the appropriate level of disclosure.

Limits on the CRA's Authority to Access Records

Limitations on the CRA's authority to compel taxpayers to produce records include: solicitor-client privilege; purpose; reasonability; and relevance. Each limitation is discussed briefly below.

Privilege

The most important limitation on the CRA's ability to compel the production of information is the solicitor-client privilege. Accountants and other professionals do not have this protection, and the CRA has made it clear that it can and will demand to see accountants' working papers and similar tax-related documentation where it chooses to do so.[9]

The current interviews are part of gradual changes in CRA audit practices that have evolved over the past several years. In response to these changes, many taxpayers have organized their tax risk assessment process so that many records are subject to solicitor-client privilege. In such cases, the taxpayers cannot be compelled to produce records that are properly subject to privilege. In some cases, privilege other than traditional solicitor-client privilege may apply, such as where legal advice is sought in anticipation of litigation. Where taxpayers assert privilege, the CRA may request sufficient information in order to assess whether they wish to challenge the privilege claim. The focus in such privilege disputes is often: (i) whether the records at issue were produced as part of a solicitor-client relationship; and (ii) where privileged records were provided to a third party, whether privilege was waived.

Most large businesses consider how to manage their information flow so as to create and preserve solicitor-client privilege where possible. The CRA interview questions directed at accessing the taxpayers' own tax risks assessment are likely to result in large businesses analyzing their process for identifying tax-risks and considering whether that process should be modified so that solicitor-client privilege applies to more records.

Purpose

The CRA exists to verify taxpayers' accuracy and honesty within a self-assessing system, which is a distinctly "regulatory" function. The powers granted to CRA are limited to the carrying out of this regulatory function, as opposed to a policing or legislative function.

The CRA has, on occasion, tried to use its regulatory powers to carry out a policing function. In these cases, where the CRA demands records for the primary purpose of advancing a criminal investigation (i.e., tax evasion), the CRA has no authority to compel a response. Courts have confirmed that CRA's regulatory powers are not available where the CRA is carrying out a different function.10 Similarly, CRA document demands that are primarily directed at impeding a particular business activity have been overturned on the basis that they do not come within the "purpose" test of the CRA's regulatory powers.[11]

Reasonability

Any CRA request must provide a reasonable time to comply.[12] In addition to challenging the reasonableness of the time given to comply, taxpayers may challenge the reasonableness of the number, scope and availability of the documents requested. Often CRA requests are necessarily over-broad because the CRA does not have the benefit of knowing what records the taxpayer maintains. Where the scope is perceived as unreasonably broad, discussions with the CRA are needed to try to reach a suitable compromise. Where the CRA compels the production of records, such demand is a "seizure" within the meaning of the Canadian Charter of Rights and Freedoms.[13]

Since the Charter prohibits seizures that are "unreasonable," any requests must be reasonable in order to be enforceable. The vast majority of the CRA's requests for information are clearly reasonable. For example, a request for documents or information necessary to complete an audit is clearly reasonable. A demand to disclose a summary of potential uncertainties in one's tax filings may be considered unreasonable.

Relevance

The CRA is granted authority to "administer and enforce the Act."[14] As such, the CRA can only compel the production of records or information relevant to this purpose. In the vast majority of cases, relevance is clear and the CRA is entitled to the information requested. However, where relevance is unclear, it is important to consider whether this relatively low threshold is met. Where disputed, the Minister need only show that the requested records "may be relevant."[15]

The CRA frequently asks for information that it cannot compel taxpayers to provide.

Taxpayers may question the extent to which their own mental impressions are "relevant." The CRA's job is to gather the necessary factual information and to form its own view as to whether the law has been complied with. Where the CRA has been provided with all of the information necessary to form that view as to the accuracy of the taxpayer's returns as filed, it is not obvious that the taxpayer's own impressions are "relevant" to the administration or enforcement of the Act. This question has not yet been considered by a Canadian court.

Policy Note: CRA Access Will Impact Financial Reporting

There is an important public policy reason for large businesses to carefully and thoroughly analyze their tax risk. We all recall when public confidence in financial reporting collapsed after the bankruptcy of Enron and others. To rebuild public confidence, reporting issuers faced more stringent financial reporting standards, including an obligation to increase the quality and quantity of records related to the calculation of tax risk.

The records that the CRA now seeks include records generated in connection with the public policy goal of ensuring large businesses accurately calculate tax risks such that the financial statements accurately depict the financial position of the business. In order to calculate tax at risk, taxpayers must consider the strengths and weaknesses of their legal position, including the strength of witnesses and other evidence in the event that uncertain issues are litigated.

If the CRA can access records related to a

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taxpayer's own risk assessment, the quality and quantity of records maintained in connection with internal tax risk will decline. As noted by the United States Court of Appeal, if tax advisors who identify "uncertainties in their clients' tax returns know that putting such information in writing will result in discovery by the IRS, they will be more likely to avoid putting it in writing, thus diminishing the quality of representation. [Access to the records by the IRS] will have ramifications that will affect the form and detail of documents" prepared when assessing tax risks.[16] The same considerations apply in Canada and the extent to which the CRA can access taxpayer records will impact the manner in which such records are prepared and maintained. ❏

1 Currently, taxpayers with gross income exceeding $250 million are assigned a large case file manager and a team of auditors who together complete an annual audit. Taxpayers with gross income from $20 million to $250 million are selected for audit based on a complexity rating and are assigned to a single auditor.

2 Canada Revenue Agency Technical Statement "*Acquiring Information from Taxpayers, Registrants and Third Parties*," June 2, 2010, http://www.cra-arc.gc.ca/tx/tchncl/cqrngnfrmn/menu-eng.html, at para 5.

3 *See*, for example: *U.S. v. Deloitte LLP*, 2010 WL 2572965 (D.C. Cir. June 29, 2010) and v. *Textron Inc.*, 577 F.3d 21 (1st Cir. 2009), cert. denied, 2010 WL 2025148 (May 24, 2010). Many corporations in the United States with assets in excess of $100 million must file a schedule identifying uncertain tax positions, *see*: http://www.irs.gov/pub/irs-utl/df1120.pdf.

4 Canada Revenue Agency, Income Tax Technical News No. 34, (April 27, 2006), available at http://www.cra-arc.gc.ca/E/pub/tp/itnews-34/README.html.

5 Section 231.1 of the *Income Tax Act* (Canada) (the "Act").

6 Sections 230, 231.1 and 231.2 of the Act.

7 Boilerplate language used in requirements issued by the CRA often includes a request for legal opinions (without notice to taxpayers that privilege may apply) and contains a caution that criminal prosecution may occur if the requested information is not disclosed.

8 Subsection 231.2(2). The CRA can generally compel such information to be produced after obtaining judicial authorization: *Artistic Ideas v. Canada*, [2005] 2 CTC 25 (FCA).

9 *See*, for example, Suarez, "Canada Updates Policy on Accessing Working Papers," *Tax Notes International*, Vol. 55, no. 3, July 20, 2009 at p. 172.

10 *See* for example: *R. v. Jarvis*, [2003] 1 CTC 135 (SCC) and *R. v. Ling*, [2002] SCR 214.

11 *See* for example: *M.N.R. v. RBC Life Insurance Company et al.*, 2011 FC 1249 at para. 62 where J. Tremblay-Lamar writes: "It was not open to the Minister to seek ex parte authorization under the pretence of verifying compliance with the Act when her true purpose was to achieve through audits what the Department of Finance refused to do through legislative amendment."

12 Subsection 231.2(1) of the Act. *See also R. v. MacDonald*, [2005] 5 CTC 77 (BC PC).

13 *Canadian Charter of Rights and Freedoms*, Part I of the *Constitution Act, 1982* being Schedule B to the Canada Act 1982 (U.K.), 1982, c. 11, s. 8.

14 Sections 231.1 and 231.2 of the Act.

15 *See* for example: *1144020 Ontario Ltd. v. M.N.R.*, [2005] 3 CTC 310 (FCTD) and *Fraser Milner Casgrain LLP v. M.N.R.*, [2002] 4 CTC 210 (FCTD).

16 U.S. v. Textron Inc., 2009 U.S. App. LEXIS 1538, at p 36-37.

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Pacific Exchange Rate Services Exchange Rates for the Dollar as of March 22, 2012

The table below gives the rates of exchange for the U.S. dollar against various currencies as of March 22, 2012. All currencies are quoted in foreign currency units per U.S. dollar except in certain specified areas. All rates quoted are indicative. They are not intended to be used as a basis for particular transactions. Pacific Exchange Rate Services (http://pacific.commerce.ubc.ca) does not assume responsibility for errors.

	Currency	Value of U.S. Dollar	Country	Currency	Value of U.S. Dollar	Country	Currency	Value of U.S. Dollar
Afghanistan	Afghani	49.4	Georgia	Lari	1.639	Norfolk Islands	Aus. Dollar	0.9633
Albania	Lek	106.05	Germany	Euro*	1.3169	Norway	Krone	5.779
Algeria	Dinar	74.645	Ghana	Cedi	1.777	Oman Sultanate	Rial	0.3851
Andorra	Euro*	1.3169	Gibraltar	Br. Pound*	1.5805	Pakistan	Rupee	90.818
Angola	Kwanza	93.19	Greece	Euro*	1.3169	Panama	Balboa	1.00
Antigua	E.Car. $	2.7	Greenland	Dan. Krone	5.6462	Papua N.G.	Kina	2.0622
Argentina	Peso	4.3665	Grenada	E.Car. $	2.7	Paraguay	Guarani	4295.00
Armenia	Dram	387.75	Guadeloupe	Euro*	1.3169	Peru	Nuevo Sol	2.6705
Aruba	Guilder	1.79	Guam	US$	1.00	Philippines	Peso	43.035
Australia	Dollar	0.9633	Guatemala	Quetzal	7.75	Pitcairn Island	NZ Dollar	1.2356
Austria	Euro*	1.3169	Guinea Republic	Franc	7105.00	Poland	Zloty	3.1601
Azerbaijan (new)	Manat	0.76	Guinea Bissau	CFA Franc	499.31	Portugal	Euro*	1.3169
Azores	Euro*	1.3169	Guyana	Dollar	201.50	Puerto Rico	US$	1.00
Bahamas	Dollar	1.00	Haiti	Gourde	40.995	Qatar	Riyal	3.641
Bahrain	Dinar	0.377	Heard/McDonald Is.	Aus. Dollar	0.9633	Rep. Yemen	Rial	210.34
Bangladesh	Taka	81.78	Honduras	Lempira	19.06	le de la Reunion	Euro*	1.3169
Barbados	Dollar	2.00	Hong Kong	Dollar	7.7655	Romania	Leu	3.3202
Belarus	Ruble	8050.00	Hungary	Forint	222.53	Russia	Ruble	29.406
Belgium	Euro*	1.3169	Iceland	Krona	126.54	Rwanda	Franc	607.08
Belize	Dollar	1.9135	India	Rupee	51.218	Samoa (American)	US$	1.00
Benin	CFA Franc	499.31	Indonesia	Rupiah	9188.80	San Marino	Euro*	1.3169
Bermuda	Dollar	1.00	Iran	Rial	12303.00	Sao Tome/Principe	Dobra	18595.00
Bhutan	Nguitrum	51.218	Iraq	Dinar	1165.00	Saudi Arabia	Riyal	3.7503
Bolivia	Boliviano	6.910	Ireland	Euro*	1.3169	Senegal	CFA Franc	499.31
Bosnia Herzegovina	Konv. Marka	1.380	Israel	New Shekel	3.7514	Serbia/Montenegro	Yug. N. Dinar	84.40
Botswana	Pula	7.2993	Italy	Euro*	1.3169	Seychelles	Rupee	14.104
Bouvet Island	Krone	N/A	Jamaica	Dollar	86.725	Sierra Leone	Leone	4350.20
Brazil	Real	1.8232	Japan	Yen	83.135	Singapore	Dollar	1.2664
Brunei	Dollar	1.2671	Johnston Island	US$	1.00	Slovakia	Koruna	22.878
Bulgaria	Lev	1.4851	Jordan	Dinar	0.7081	Slovenia	Tolar	N/A
Burkina Faso	CFA Franc	499.31	Kazakhstan	Tenge	147.75	Solomon Is.	Solomon$	7.0766
Burundi	Franc	1402.80	Kenya	Shilling	83.15	Somali Rep.	Shilling	1627.00
Cameroun	CFA Franc	499.31	Kiribati	Aus. Dollar	0.9633	South Africa	Rand	7.7227
Canada	Dollar	0.9986	Korea, North	Won	118.18	Spain	Euro*	1.3169
Cape Verde Islands	Escudo	83.72	Korea, South	Won	1130.00	Sir Lanka	Rupee	130.25
Cayman Islands	Dollar	0.82	Kuwait	Dinar	0.2786	St. Helena	Br. Pound*	1.5805
Cent. Af. Republic	CFA Franc	499.31	Kyrgyzstan	Som	49.867	St. Kitts	E. Car. $	2.7
Chad	CFA Franc	499.31	Laos	Kip	7991.00	St. Lucia	E. Car. $	2.7
Channel Islands	Br. Pound*	1.5805	Latvia	Lat	0.529	St. Pierre/Miq'lon	Euro*	1.3169
Chile	Peso	487.25	Lebanon	Pound	1501.50	St. Vincent	E. Car. $	2.7
China	Renminbi	6.2994	Lesotho	Maloti	7.7235	Sate of Cambodia	Riel	4001.00
Christmas Islands	Aus. Dollar	0.9633	Liberia	Dollar	73.50	Sudan	Dinar	N/A
Cocos Islands	Aus. Dollar	0.9633	Libya	Dinar	1.2584	Suriname	Dollar	3.3
Colombia	Peso	1759.60	Liechtenstein	Sw. Franc	0.9152	Swaziland	Lilangeni	7.7235
Comoros Rep.	Franc	373.86	Lithuania	Litas	2.6217	Sweden	Krone	6.7686
Congo Republic	CFA Franc	499.31	Luxembourg	Euro*	1.3169	Switzerland	Franc	0.9152
Congo Dem Rep.	Franc	N/A	Macau	Pataca	7.9982	Syria	Pound	57.444
Costa Rica	Colon	509.88	Macedonia	Dinar	43.40	Taiwan	Dollar	29.561
Cote d'Ivoire	CFA Franc	499.31	Madagascar	Franc	8547.00	Tajikistan	Somoni	N/A
Croatia	Kuna	5.71	Madeira	Euro*	1.3169	Tanzania	Shilling	1592.00
Cuba	Peso	1.00	Malawi	Kwacha	166.40	Thailand	Baht	30.83
Cyprus	Pound	0.4447	Malaysia	Ringgit	3.0827	Togo Rep.	CFA Franc	499.31
Czech Repub.	Koruna	18.79	Maldive Is.	Rufiyan	15.370	Tokelau	NZ $	1.2356
Denmark	Krone	5.6462	Mali Republic	CFA Franc	499.31	Tonga Island	Pa'anga	1.56
Djibouti	Franc	177.72	Malta	Lira	0.326	Trinidad/Tobago	Dollar	6.35
Dominica	E.Car. $	2.7	Martinique	Euro*	1.3169	Tunisia	Dinar	1.5099
Domi. Rep.	Peso	39.16	Mauretania	Ouguiya	295.00	Turkey	Lira	1.8128
Dronning Maud.	Nor. Krone	5.779	Mauritius	Rupee	29.05	Turkmenistan (new)	Manat	2.78
East Timor	US$	1.00	Mexico	New Peso	12.804	Turks & Caicos	US$	1.00
Ecuador	US$	1.00	Moldova	Lei	11.84	Tuvalu	Aus. Dollar	0.9633
Egypt	Pound	6.0367	Monaco	Euro*	1.3169	Uganda	Shilling	2487.00
El Salvador	Colon	8.7475	Mongolia	Tugrik	1326.00	Ukraine	Hryvnia	8.0284
Eq'tl Guinea	CFA Franc	499.31	Montserrat	E.Car. $	2.7	United Kingdom	Br. Pound*	1.5805
Eritrea	Nafka	13.63	Morocco	Dirham	8.4742	Uruguay	Peso	19.52
Estonia	Kroon	11.882	Mozambique (new)	Metical	25.83	U.A.E.	Dirhan	3.673
Ethiopia	Birr	17.459	Myanmar	Kyat	6.4342	Uzbekhistan	Som	1839.40
European EMU	Euro*	1.3169	Namibia	Dollar	7.14	Vanuatu	Vatu	95.525
Faeroe Islands	Dan. Krone	5.6462	Nauru Is.	Aus. Dollar	0.9633	Vatican City	Euro*	1.3169
Falkland Islands	Br. Pound*	1.5805	Nepal	Rupee	81.88	Venezuela	Bolivar	4.29
Fiji	Dollar	1.779	Neth. Antilles	Guilder	1.79	Vietnam	Dong	20860.00
Finland	Euro*	1.3169	Netherlands	Euro*	1.3169	Virgin Islands BR	US$	1.00
Fr. Pacific Islands	Franc	90.684	New Zealand	Dollar	1.2356	Virgin Islands US	US$	1.00
France	Euro*	1.3169	Nicaragua	Cordoba	23.22	West Samoa	Tala	2.02
French Guiana	Euro*	1.3169	Nieue	NZ Dollar	1.2356	Zambia	Kwacha	5325.00
Gabon	CFA Franc	499.31	Niger Rep.	CFA Franc	499.31	Zimbabwe	Dollar	N/A
Gambia	Dalasi	29.695	Nigeria	Naira	157.50			

(N/A) Not Available * U.S. Dollar per national currency unit

Corporate Audit Rotation Rules Country-by-Country

BY REUTERS

The U.S. overseer of corporate auditors brought accounting leaders together this month to help it decide whether to limit the number of years an auditor can work for the same company.

The U.S. overseer of corporate auditors brought accounting leaders together this month to help it decide whether to limit the number of years an auditor can work for the same company.

If the Public Company Accounting Oversight Board adopts mandatory term limits for audit firms, the United States would become the largest country by far to embrace the idea.

The European Commission is also considering a draft law that would require auditors to switch after six years.

Here are some of the largest countries that have approved some form of audit firm rotation:

- *BRAZIL* - Beginning in 2012, five-year rotation for non-bank listed companies, 10 years if a company has a statutory audit committee.
- *CHINA* - Five-year rotation for state-owned entities and financial institutions.
- *CROATIA* - Seven-year rotation for banks; four years for insurance and leasing companies.
- *ECUADOR* - Five-year rotation for financial institutions; six years for insurance companies.
- *INDIA* - Four-year rotation for banks and insurance companies; two years for provident trusts; four or five years for public sector entities.
- *INDONESIA* - Six-year rotation for public and private companies.
- *ISRAEL* - Two, three-year rotation periods for government companies, with some extensions possible.
- *ITALY* - Nine-year rotation for all listed companies and public interest entities.
- *MOROCCO* - Six-year rotation for all banks; 12-year rotation for listed companies.
- *PAKISTAN* - Five-year rotation for financial institutions and insurance companies.
- *POLAND* - Five-year rotation for insurance companies.
- *PORTUGAL* - Eight- to nine-year rotation recommended for listed companies, on a "comply or explain" basis.
- *QATAR* - Five-year rotation for banks and Qatar shareholding companies.
- *SAUDI ARABIA* - Five-year rotation for joint stock-listed companies except banks; banks rotate audit partners upon request from Central Bank.
- *SLOVENIA* - Five-year audit partner or firm rotation recommended for public companies, five years required for insurance and investment management companies.
- *TURKEY* - Eight-year rotation for banks; seven years for insurance companies; five years for energy companies and all listed companies, with some exceptions.
- *UKRAINE* - Seven-year rotation for banks; five years for national bank.
- *VENEZUELA* - Three-year rotation for banks beginning in 2014. ❑ – *(Source: Deloitte)*

Competition

***UK Competition Regime*, from page 1**

Parliamentary approval. It is anticipated that the CMA will be fully operational by April 2014. Until then, the OFT and the CC will continue to exist and perform their current functions.

Market Investigations

Currently under the UK's Enterprise Act, the OFT has the power to refer markets to the CC for investigation, where the OFT has reasonable grounds for suspecting that any feature of a market is anticompetitive. Under the new regime, the CMA will carry out these markets inquiries directly, without need for a referral. Market participants will benefit from the introduction of statutory time limits, which will reduce the duration of the process from the sixty-seven months currently to a maximum of 24 months.

The CMA will also take over from the CC and the OFT their roles in determining references from the Competition Appeal Tribunal in price control cases in regulated industries, such as the telecoms sector, as well as in other regulatory appeal processes.

Antitrust Investigations

The procedures for the investigation of antitrust violations will be improved. At the outset of each investigation, the CMA will be required to publish a case-specific timetable, to make greater use of state of play meetings, to improve engagement with the parties, and to provide the parties under investigation with a copy of the draft penalty calculation, giving them an opportunity to make representations on the appropriateness of the penalty before it is imposed.

Criminal penalties for failure by an individual to comply with CMA information requests will be replaced with civil penalties. The CMA will require a warrant from the CAT (as well as the High Court and Court of Session) to enter premises by force. The CMA will be given additional powers to require a person to answer questions similar to those available in criminal proceedings.

Under the Competition Act 1998, the OFT has been authorized to impose interim measures where there is a risk of "serious and irreparable damage" being caused by a suspected antitrust violation. Interim measures allow the OFT to enjoin conduct pending conclusion of an investigation. However, this tool has hardly been used, because it is hard to prove "serious and irreparable damage." The bar now will be lower, to require only a "perceived need to act for the purposes of preventing significant damage to a particular person or category of person."

For criminal cartel offences, which now require that an individual must have "dishonestly" agreed with one or more other persons to engage in cartel activities, the dishonesty element will be removed. To establish criminal cartel activity, the CMA will need only prove the mental elements of intent to enter into an agreement and to operate the arrangement in question. The Government's view is that the inclusion of the dishonesty element in the cartel offence has inhibited the prosecution of cases (only two cartels have been prosecuted since 2003) and anticipates that the change to the law will improve enforceability and increase deterrence, bringing levels closer to what was intended when the criminal cartel offence was introduced.

Merger Control

Contrary to expectations that the Government would introduce a mandatory merger notification regime, the Government has decided to keep a voluntary regime. Accordingly, merging parties will continue to be able to take a view as to whether to submit or not a notification to the CMA before completion. However, the CMA will have the power to investigate completed mergers and to prevent the merging parties from completing their transaction at any stage of a post-closing investigation, if it has grounds to suspect that implementing the transaction would prejudice the outcome of an investigation. Existing criminal penalties for failure to comply with an order to suspend the implementation of a merger will be replaced with civil penalties of up to 5% of the merging parties' aggregate group worldwide turnover.

Currently problematic mergers are referred by the OFT to the CC for an in depth review. In order to keep this peer review process, going forward the CMA Board will be responsible for Phase 1 investigations and a panel of experts appointed by the CMA will be responsible for Phase 2 decisions. The time limits for Phase 1 investigations and Phase 2 investigations respectively remain substantially unchanged.

Effective October 2012, merger control fees will be increased from a maximum of £90,000 to a maximum of £160,000.

Conclusion

The most significant of these reforms is, for the criminal cartel offence, removing the requirement that dishonesty be proven. That change will make it much easier for the CMA to pursue prosecutions against individuals it suspects are involved in price fixing, customer sharing, or market allocation arrangements. An increase in prosecutions is therefore to be anticipated.

The most significant of these reforms is, for the criminal cartel offence, removing the requirement that dishonesty be proven.

The amalgamation of the OFT and the CMA into a single new authority has been billed as the creation of a new organization that has the potential to make better use of public resources, to enhance overall consistency and predictability for business and to be a strong voice for the benefits of competition in the UK and internationally. Given that much of the structure of investigations remains the same, in particular for mergers, only time will tell if the CMA is able to achieve these aims. ❏

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Tax Rate Reduction, from page 2

allocate resources, and by adding massive complexity and cost to the tax compliance process.

The fact that President Obama proposed any reduction in corporate income tax rates is impressive and even politically courageous, given his ongoing calls for an increase in personal income taxes on the wealthiest 1 percent of Americans. It is also fair to acknowledge that his proposed cuts on the tax-incentive side of the ledger are pretty substantial, even though he undercuts his efforts with a proliferation of new tax subsidies, particularly for alternative energy and manufacturing. The Proposal may be more about political posturing than about a serious legislative effort in 2012—increasing overall corporate taxes is just a non-starter in 2012, even for many Democrats—but the good news is that this proposal is reminiscent of a document, issued in 1984 by President Reagan, called "Tax Reform for Fairness, Simplicity and Economic Growth." That document morphed into the Tax Reform Act of 1986, the fairest and best version of the Internal Revenue Code ever enacted by the U.S. government. One can hope that the Obama Proposal will have a similar seminal effect in the area of corporate tax reform.

The Proposal offers far-reaching and relatively radical new provisions addressing international tax and the taxation of U.S. companies with foreign operations.

Reform and Elimination of Tax Incentives and Subsidies

The following is a verbatim detailed summary from the Proposal of the tax incentives that the President would like to eliminate (or consider eliminating). Editorial comments, where appropriate, are set forth in italics after each item.

- ***Eliminate Dozens of Business Tax Loopholes and Tax Expenditures.*** The President's plan would start from a presumption that we should eliminate all tax expenditures for specific industries, with the few exceptions that are critical to broader growth or fairness. The following are a few examples of specific reductions in tax expenditures and loophole closers that should be part of any reform:
- ***Eliminate "last in first out" accounting.*** Under the "last-in, first-out" (L1IFO) method of accounting for inventories, it is assumed that the cost of the items of inventory that are sold is equal to the cost of the items of inventory that were most recently purchased or produced. This allows some businesses to artificially lower their tax liability. The Framework would end LIFO, bringing us in line with international standards and simplifying the tax system.

  [Comment: LIFO is designed to eliminate or at least reduce "fake" income caused by mere inflation in the cost of goods—you measure your income based on what it actually costs currently to buy inventory or materials that go into creating inventory. Eliminating LIFO has the questionable consequence of rewarding the government with extra tax revenues solely for creating inflation. That said, almost every tax subsidy in the Code has at least some rationale or justification, so if the compact is to reduce the tax rate and eliminate almost all tax subsidies, then provisions like LIFO will have to go.]
- ***Eliminate oil and gas tax preferences.*** The tax code currently subsidizes oil and gas production through tax expenditures that provide preferences for these industries over others. The Framework would repeal tax preferences available for fossil fuels. This includes, for instance, repealing the expensing of intangible drilling costs, a provision that allows oil companies to immediately write-off these costs rather than recovering the cost over time as for most capital investments in other industries. This also includes repealing percentage depletion for oil and natural gas wells, which allows certain oil producers and royalty owners to recover the cost of oil and gas wells based on a percentage of the income they earn from selling oil and gas from the property rather than on the exhaustion of the property. Percentage depletion allows deductions that can exceed the cost of the property.

  [Comment: Obama is unapologetically opposed to fossil fuels, so this is easy for him. On the other hand, the trade-off for lower tax rates requires eliminating industry-specific subsidies, so this favoritism should go (along with many others).]
- ***Reform treatment of insurance industry and products.*** The tax code currently allows insurance to be used as a form of tax shelter for major corporations. In particular, corporations can invest in life insurance for their officers, directors, or employees, benefit from "inside build up" (gains on that investment) that are tax-deferred or never taxed, and finance that investment through debt that allows the corporation to take interest deductions earlier than any gain realized on the life insurance. The Framework would close this loophole and not allow interest deductions allocable to life insurance policies unless the contract is on an officer, director, or employee who is at least a 20 percent owner of the business. The Framework would also make a number of other reforms to the treatment of insurance companies and products to improve information reporting, simplify tax treatment, and close loopholes.

  [Comment: Insurance tax reform is too complicated a topic for this article, but corporate tax reform in principle should touch all industries.]
- ***Taxing carried (profits) interests as ordinary***

income. Currently, many hedge fund managers, private equity partners, and other managers in partnerships are able to pay a 15 percent capital gains rate on their labor income (on income that is known as "carried interest"). This tax loophole is inappropriate and allows these financial managers to pay a lower tax rate on their income than other workers. The Framework would eliminate the loophole for managers in investment services partnerships and tax carried interest at ordinary income rates.

[Comment: It is absolutely true that many hedge fund managers are paying a 15 percent tax rate on their "labor income," meaning their return and reward for managing the fund. This no doubt seems very fair to hedge fund managers, but is decidedly less popular with the general electorate, and so this proposed modification is low-hanging fruit in any tax reform proposal.]

- ***Eliminate special depreciation rules for corporate purchases of aircraft.*** This would eliminate the special depreciation rules that allow owners of non-commercial aircraft to depreciate their aircraft more quickly (over five years) than commercial aircraft (seven years).

  [Comment: Obama, who jets everywhere all the time in a taxpayer-supported Boeing 747 called Air Force One, loves to bash executives who use "corporate jets." If this provision means he can no longer drone on about this stunningly hypocritical subject then please enact this modification right away—like, this afternoon.]
- ***Reform the Corporate Tax Base to Invest Savings in Cutting the Tax Rate and Reducing Harmful Distortions.*** This Framework lays out a menu of options that should be under consideration in reform. At least several of these would be necessary to get the rate down to 28 percent:
- ***Addressing depreciation schedules.*** Current depreciation schedules generally overstate the true economic depreciation of assets. Although this provides an incentive to invest, it comes at the cost of higher tax rates for a given amount of revenue. In an increasingly global economy, accelerated depreciation may be a less effective way to increase investment and job creation than reinvesting the savings from moving towards economic depreciation into reducing tax rates.

  [Comment: Investing in productivity and efficiency is generally viewed as a good idea, and some observers believe companies should be able to write off all expenditures in the year paid—the income earned for that year goes right back out the door to buy the equipment, there is often little or no cash left over to pay taxes unless the purchase is fully deductible under Code Section 179, and so the depreciation rules often put a huge stranglehold on young, growing businesses. The whole point of lowering tax rates, e.g., to 20 percent, is so that no one has an incentive to spend a dollar wastefully—who is going to buy unnecessary equipment if 80 cents is out of their own pocket and only 20 percent is subsidized by the government? That is, or should be, the whole point of the Proposal.]
- ***Reducing the bias toward debt financing.*** A lower corporate tax rate by itself would automatically reduce but not eliminate the bias toward debt financing. Additional steps like reducing the deductibility of interest for corporations should be considered as part of a reform plan. This is because a tax system that is more neutral towards debt and equity will reduce incentives to over-leverage and produce more stable business finances, especially in times of economic stress. In addition, reducing the deductibility of interest for corporations could finance lower tax rates and do more to encourage investment in the United States than keeping rates higher or paying for the rate reductions in other ways.

A lower corporate tax rate by itself would automatically reduce but not eliminate the bias toward debt financing.

  [Comment: Great issue to raise. Double taxation strongly encourages debt financing rather than equity financing. However, the proposed "cure" sounds far less promising. The "easy" solution is to create a single level of tax on corporate profits, but the Proposal instead wanders off to try and make interest non-deductible (in effect, advocating double taxation of debt funding, rather than single taxation of equity funding.) Not clear why that makes any sense at all.]
- ***Establishing greater parity between large corporations and large non-corporate counterparts.*** Establishing greater parity between large corporations and their large non-corporate counterparts should be considered as a way to help improve equity, reduce distortions in how businesses organize themselves, and finance lower tax rates. A variety of ways to do this have been proposed, including ones discussed in the 2005 report of President Bush's Advisory Panel on Tax Reform,[2] and in reform options developed by President Obama's Economic Recovery Advisory Board in 2010.[3] It is essential that any changes in this area should not affect small businesses.

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[Comment: Too vague a proposal to merit much comment, other than to note that creating "equity" and "level playing field" between taxpayers similarly situated economically is always a good idea, often translated horribly in practice into policies that have the exactly opposite effects.]

International Taxation and the "Minimum Tax"

The Proposal offers far-reaching and relatively radical new provisions addressing international tax and the taxation of U.S. companies with foreign operations. At the moment, the U.S. imposes worldwide taxation on its citizens, including all corporations formed under U.S. law.

The Obama Administration has made it clear that it would like to slam the door on almost any form of IP migration.

However, during the 1990s and early 2000s, the U.S. often "mimiced" territorial taxation thanks the congenial interpretation and enforcement of various tax rules, including migration of intellectual property (IP) offshore through cost-sharing agreements, and the interpretation and application of the Subpart F Rules[4] and the PFIC Rules[5] (the Anti-Deferral Rules), such that the U.S. had de facto territorial taxation.

In other words, a U.S. corporation could set up its active foreign operations so that it paid foreign tax (often in low-tax jurisdictions) on non-U.S. income, and paid U.S. tax only on its U.S. income. U.S. companies essentially operate as economic "twins" with U.S. income funding U.S. operations and foreign income funding foreign operations. The huge drawback of this convoluted taxation scheme is that any "foreign" income brought back to the U.S. is immediately taxed at 35 percent[6] and so this makes for an awkward operational structure, to say the least. (Note: In 2005, when the U.S. for one year allowed foreign profits to be brought back to the U.S. at just a 5 percent tax, a remarkable $600 billion sloshed back into the U.S. economy.)

The Obama Administration has made it pretty clear all along, such as in its annual "Greenbook" proposals,[7] that it would like to slam the door on almost any form of IP migration in order to keep these valuable, income-producing assets solely within U.S. tax jurisdiction, and would also like to more fully embrace worldwide taxation as government tax policy. The Proposal reflects these policies objectives by offering the following provisions:

- ***Require Companies to Pay a Minimum Tax on Overseas Profits.*** The President believes we must prevent companies from reaping the benefits of locating profits in low-tax countries, put the United States on a more level playing field with our international competitors, and help end the race to the bottom in corporate tax rates.

Specifically, under the President's proposal, income earned by subsidiaries of U.S. corporations operating abroad must be subject to a minimum rate of tax. This would stop our tax system from generously rewarding companies for moving profits offshore. Thus, foreign income deferred in a low-tax jurisdiction would be subject to immediate U.S. taxation up to the minimum tax rate with a foreign tax credit allowed for income taxes on that income paid to the host country. This minimum tax would be designed to balance the need to stop rewarding tax havens and to prevent a race to the bottom with the goal of keeping U.S. companies on a level playing field with competitors when engaged in activities which, by necessity, must occur in a foreign country.

[Comment: The proposed minimum tax would substantively eviscerate Subpart F and would make foreign activities of U.S. corporations immediately taxable to some (apparently significant) degree. However, that is likely to have immediate adverse consequences to the U.S. economy: U.S. companies would be placed at a competitive disadvantage in all foreign markets, due to paying significantly higher tax rates than their foreign competitors, and eventually the foreign competitors are likely to prevail—and then buy up all the U.S. companies. That is not a winning national strategy for the U.S. The more practical solution solution would be either to accept and embrace the de facto territorial system adopted by the U.S. the past twenty years, or go to a true territorial system. This is the position advocated by the U.S. Chamber of Commerce, among many others.]

- ***Remove tax deductions for moving productions overseas and provide new incentives for bringing production back to the United States.*** The tax code currently allows companies moving operations overseas to deduct their moving expenses—and reduce their taxes in the United States as a result. The President is proposing that companies will no longer be allowed to claim tax deductions for moving their operations abroad. At the same time, to help bring jobs home, the President is proposing to give a 20 percent income tax credit for the expenses of moving operations back into the United States.

[Comment: It is entirely reasonable that expenses and costs attributable to foreign operations should not be deductible against the U.S. taxable income attributable to U.S. operations. This problem arises in significant part because we have a "faux" territorial tax rather than a true territorial tax system at the present time, and so expenses attributable to foreign operations can pretty easily end up deductible on the U.S. tax return. As a practical matter, either form of territorial taxation, meaning either the current faux territorial system with appropriate fixes (like this) or a true territorial system, would be sensible and acceptable alternatives. On the second element of this proposal, the 20 percent tax credit for "moving back," a likely problem is that companies would "game" this credit by moving U.S. operations offshore for the sole purpose of then moving back and getting the 20 percent credit. A much better idea is the core idea of the Proposal: reduce U.S. tax rates dramatically and then the U.S. will not need a 20 percent credit—the jobs will come flooding back, assuming they can be performed in the U.S. in an economically competitive manner.]

- ***Other reforms to reduce incentives to shift income and assets overseas.*** The Framework would also clean up the international tax code and reduce incentives and opportunities to shift income and assets overseas. For example, as noted above, U.S. companies may use accounting rules or aggressive transfer pricing to shift profit offshore. This is particularly true in the case of profits associated with intangible assets (assets like intellectual property). The Framework would strengthen the international tax rules by taxing currently the excess profits associated with shifting intangibles to low tax jurisdictions. In addition, under current law, U.S. businesses that borrow money and invest overseas can claim the interest they pay as a business expense and take an immediate deduction to reduce their U.S. taxes, even if they pay little or no U.S. taxes on their overseas investment. The Framework would eliminate this tax advantage by requiring that the deduction for the interest expense attributable to overseas investment be delayed until the related income is taxed in the United States.

[Comment: The first part of this proposal is to try and "glue" intangible assets to the ground in the U.S. and it won't work. The simple side-step is to do all IP development in (or at least fund it from) another country and don't let it ever "belong" to the U.S. The second part of the proposal, which is to allocate costs and expenses appropriately to foreign activities, is exactly correct, in order to rationalize the current faux territorial tax system. However, the best answer is to implement the Proposal in a serious way, drop

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The Proposal offers special attention and tax relief to "manufacturing" activities.

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rates substantially, and then the incentives to move offshore largely disappear. Bear in mind that eliminating tax incentives to move offshore is a good thing; on the other hand, the U.S. should not try to discourage or prevent U.S. companies from conducting overseas operations that cannot be carried on competitively or efficiently in the U.S.]

Under the proposal, income earned by subsidiaries of U.S. corporations operating abroad must be subject to a minimum rate of tax.

Manufacturing Subsidies and Incentives

The Proposal offers special attention and tax relief to "manufacturing" activities, including the following provisions:

- ***Effectively cut the top corporate tax rate on manufacturing income to 25 percent and to an even lower rate for income from advanced manufacturing activities by reforming the domestic production activities deduction.*** Reflecting manufacturing's key role in innovation and the intense international competition facing the sector, the President's Framework would reform the current domestic production activities deduction. It would focus the deduction more on manufacturing activity, expand the deduction to 10.7 percent, and increase it even more for advanced manufacturing. This would effectively cut the top corporate tax rate for manufacturing income to 25 percent and even lower for advanced manufacturing.

  [Comment: Lower tax rates and no special treatment seem like a much better policy approach than an industry-targeted subsidy. First of all, defining what constitutes "manufacturing" is a surprisingly complicated and difficult exercise—look at the very unsatisfactory attempts to define it in connection with the "manufacturing" exception contained in subpart F and the related regulations. The so-called Bausch & Lomb[8] test in this area of law has been described by a smart friend with a mordant wit as meaning "doing anything that makes you breathe hard." Having a special category called "advanced manufacturing" is even more doubtful a proposition: Suffice it to say that, if history is any guide, then over time Congress will likely decide that everything is "advanced" manufacturing.]

Conclusion

There is a lot to quibble about in the details of the Proposal, but corporate tax reform has become an urgent priority of the U.S. and now is the time to start the discussion. It may be overly optimistic to compare this Obama Proposal to the Reagan proposal of 1984 (also an election year) but the fact remains that Reagan followed up and turned his proposal into historic tax legislation, and one can at least hope for similar follow-up this time as well.

Many of the specific ideas in the Obama Proposal are flawed, and in some cases are just flat wrong or wrong-headed, but the one great idea embodied in the Proposal is exactly right: The time for serious U.S. corporate income tax reform in now upon us. ❑

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1 A Joint Report by the White House and the Department of the Treasury, issued February 22, 2012. See www.treasury.gov/press-center/news/pages/02222012-tax.aspx.
2 President's Advisory Panel On Tax Reform, Simple, Fair, and Pro-Growth: Proposals to Fix America's Tax System 129 (2005).
3 President's Economic Recovery Advisory Board, supra note 2, at 74-77.
4 Code Section 951 et. seq.
5 Code Section 1291 et. seq.
6 See Darby, Joseph B III. "A Dollar is a Dollar is a Dollar," Practical US/Domestic Tax Strategies, March 2006 Vol. 6, No. 3, p. 2.
7 See Darby, Joseph B III, "Proposed Tax Changes in 2011 Budget," Practical US/Domestic Tax Strategies, April 2010, Vol. 10, No. 4, p. 2.
8 71 TCM 2031 (1996), TC Memo 1996-57.

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