Insights: Summary of Ways and Means hearing on "Increasing U.S. Competitiveness and Preventing American Jobs from Moving Overseas"

The House Ways and Means Committee held a hearing today on "Increasing U.S. Competitiveness and Preventing American Jobs from Moving Overseas." Witnesses at the hearing were: Juan Luciano, President and Chief Executive Officer, Archer Daniels Midland Company (ADM); Brian Cornell, Board Chairman and Chief Executive Officer, Target Corporation; William Simon, Former President and Chief Executive Officer, Walmart U.S.; Lawrence B. Lindsey, President and CEO, The Lindsey Group; and Kimberly Clausing, Thormund A. Miller and Walter Mintz Professor of Economics, Reed College.

Chairman Kevin Brady (R-TX), in his opening statement, stressed the need for pro-growth tax reform that strengthens American competitiveness and prevents jobs from moving overseas. At the end of the hearing, he acknowledged concerns that have been expressed about the House GOP Tax Reform Blueprint, but said, "I am heartened by the fact that we all recognize that moving forward with this type of bold change requires thoughtful transition, deliberate transition, and addressing successfully the concerns that we have heard today."

Ranking Member Richard Neal (D-MA), in his opening statement, highlighted the need for tax reforms aimed at the middle class. He said, "Democrats will only support comprehensive tax reform that will ease financial burdens on the middle class and working families. We will not support tax cuts for those at top of the income scale at the expense of the middle class. Our primary focus and top priority in tax reform needs to be putting the middle class first."

He also weighed in on the BAT, saying "Given the many significant economic uncertainties and risks associated with a border adjustment tax, the Committee must evaluate its merits thoroughly and methodically." He said that among the issues lawmakers must consider are: the impact on consumers; whether the dollar will strengthen to offset anticipated increases in consumer prices, and how long such currency adjustments will take; whether the BAT is WTO compliant; and who are the winners and losers under a BAT.

Rep. Neal also requested in his opening statement that the committee consider holding a hearing on how to use the revenue raised in a deemed repatriation in tax reform, saying "I support using repatriation dollars to pay for infrastructure or other productive purposes for the middle class." Chairman Brady did not appear to immediately respond to his request.

Three Republicans Express Reservations About BAT

During the hearing, three Republicans expressed their opposition to or reservations about the BAT. These include: Reps. Erik Paulsen (MN), Jim Renacci (OH), and Mike Kelly (PA).

Rep. Erik Paulsen (R-MN) acknowledged the concerns that Mr. Cornell and some other witnesses expressed about the border adjustment tax, including on its effects on consumers and the retail sector. Rep. Paulsen said, "I cannot support the border adjustability provisions as introduced last year in the Blueprint. I really want to urge this committee to listen, to be educated, and then address these concerns that we have heard as we move forward on reforms."

Rep. Jim Renacci (R-OH) said, "I've been skeptical of the border adjustment as a central element the Blueprint, but I'm trying not to be." He said he does not oppose border adjustments in all contexts, noting that he is a "strong supporter of a more conventional border adjustment consumption tax." He said his concerns are routed in three questions: 1) does border adjustability in the Blueprint pick winners and losers? 2) who will the tax burden ultimately shift to? and 3) is it compliant with our international treaty obligations? He said that the answer to the first two questions hinges on economic theory that currency will adjust to offset the tax. He said that market analysts and currency experts have been skeptical and Wall Street firms have indicated that there is the potential for disruption and volatility in markets. He also acknowledged the potential that the border adjustability element of the Blueprint could be determined to be non-compliant with our trade obligations.

Rep. Kelly expressed concerns about the effect of BAT on consumer prices. He said to Mr. Cornell, "My concern is the final price on the shelf for those folks that pick up the tab on every single thing this government does in their name. So, if you could just tell me the effect on everyday Americans. The global supply chain has changed. If you can tell us how does this affect the price on the shelf and how would it affect consumers? I know we have to pay for these tax cuts but I don't want it to be on the back of everyday Americans." Mr. Cornell responded, "We talk to consumers all the time. I have 30 million shoppers in our stores every single week. These are middle class families on a budget. For those families and look at the implications, we know that their prices will go up on essential items. They'll pay 20% more on apparel, on back-to-school items, on essential items like produce that in the winter we don't grow in the United States."

Summary of Witness Testimony

Mr. Luciano (ADM) spoke in favor of tax reform that lowers the corporate tax rate to 20 percent, converts the current worldwide system of taxation to a territorial tax, and creates a border-adjusted destination-based cash flow tax (DBCFT). In speaking about a border adjustment feature, he said that one of the reasons ADM supports a BAT is "because it eliminates tax disparities on exports that arise due to differences between the U.S. income tax system and the border-adjusted VATs of OECD countries… Stated simply, by being the only major country on a pure income tax system, our exports are systematically disadvantaged because they bear more tax. The Destination Based Cash Flow Tax addresses this imbalance and begins to level the playing field between our tax system and the VAT systems of the rest of the world. If we can eliminate this imbalance, more investment, and more jobs, should come to the U.S."

Mr. Cornell (Target) said that while his company strongly supports tax reform, "We've concluded that the new border adjustment tax would undermine the pro-growth principles in the Blueprint." He noted that Target recently announced a $7 billion investment in the United States, "But under the new border adjustment tax, our rate would more than double, from 35 percent to 75 percent. And we – like many others – would be left with only bad options. It's simple math. If the government takes nearly four out of every five dollars we make. Four out of five. There's no capital to invest and no prospects for growth. He said that his company is not alone in its opposition to the BAT, adding, "More than 500 associations and companies feel the same way."

Mr. Simon (formerly with Walmart) expressed qualified support for a BAT. He said, "I have weighed the considerable challenges this proposal presents to retail with the significant benefits it will deliver to the economy as a whole and have concluded that properly implemented, it is in the best interest of our country for this to be considered."

He stressed the need to address transition concerns associated with implementation of a BAT, saying "Most of the manufacturing capacity that exists in the world, outside of food products, is no longer based in the U.S. Simply applying a 20 percent tax on day one to those products would have a serious impact on the industry and the consumer." He added, "If you move forward with a border adjustment, I would recommend considering a long implementation period with a phase in of the tax impact. Economists forecast that currency impacts would offset all or most of these changes. If that is the case, use the expected value of the dollar to 'trigger' the next phase in the tax rates or some other trigger method." In his written testimony, he outlined steps the retail industry could take to help with the transition.

Mr. Lindsey (The Lindsey Group) expressed support for the House GOP Tax Reform Blueprint. He said it would end three major distortions that have created inefficiencies and bad incentives for the economy. He said it would: 1) end the tax bias on a cash flow basis against investing in long-lived plants and equipment; 2) end the tax bias in favor of debt over equity; and 3) reduce incentives to invest overseas. He said that the DBCFT is simpler than our current tax system and will benefit from currency adjustment that will largely offset the increased tax on imports. While he acknowledged that there will be transition costs associated with a transition to the BAT, "the long-term benefits to U.S. economy are many times any short-term costs involved in transition."

Professor Clausing said that there are several flaws with the business tax component of the House GOP Blueprint. Specially, she said the plan:

- is "likely to generate large economic shocks that would harm American workers and trade-dependent businesses."

- would "impose serious risks to the world trading system and to exporting companies." She said that many legal experts have concluded that the plan would be world trade incompatible and could lead to legal suits from our trading partners.

- would lose revenues at the current proposed tax rates. She said that the Tax Policy Center has estimates that the plan would lose $3 trillion over 10 years. She said that while the BAT proposal would raise revenues initially, it would eventually lose money over time as U.S. trade deficits turn into surpluses.

- would make our tax system less progressive at the current proposed tax rates; and
- is "an untested tax reform that is not ready for primetime."

Members' Questions, Comments

Chairman Brady asked Mr. Lindsey to expand upon his assessment that the House GOP Blueprint would help encourage economic growth and increase wages. Mr. Lindsey said that he believes that the amount wages will rise under the Blueprint will far outweigh any distributional considerations. He said, "I think we will see for the first time since the Kennedy tax cut a reduction in the measures of inequality that we have."

Chairman Brady asked Mr. Simon to discuss approaches and measures that could help bring manufacturing capability and jobs back to the United States Mr. Simon said that several things could help repatriate manufacturing, including providing access to capital that is stashed offshore and allowing expensing instead of depreciation.

Rep. Neal asked Mr. Cornell to expand on concerns he raised about currency responses to border adjustment. Mr. Cornell said his company has been closely examining the issue, and has been told by some of the economists that they have consulted that "there should be grave doubts that exchange rates will smoothly offset the effect of border adjustments."

Several other committee members brought up the issue of currency adjustments and their potential effects on consumer prices, including Reps. Devin Nunes (R-CA) and Kelly, among others. Chairman Brady said that a study by JPMorgan concluded that if the dollar did not adjust at all, prices would only go up by 5 percent. Mr. Lindsey noted that a very conservative estimate (not his) shows that if the dollar adjusted only 65 percent, it would result in a total increase in consumer prices of 1 percent. Mr. Cornell warned that the border adjustment could result in a 20 percent increase in the price of certain products, such as clothing and back-to-school supplies. Professor Clausing noted that exchange rates are very difficult to predict.

Reps. Lloyd Doggett (D-TX) and Mike Thompson (D-CA) questioned the benefits of a one-time tax repatriation holiday, saying that the provision enacted in 2004 did little to create jobs and investments in the United States. Rep. Tom Reed (R-NY) said that the benefits of the 2004 holiday were limited because it was temporary in nature.

Several Democrats raised concerns about the distributional effects of the GOP proposal.

The witness testimony and additional information about the hearing is available on the Ways and Means Committee website at: https://waysandmeans.house.gov/event/hearing-increasing-u-s-competitiveness-preventing-american-jobs-moving-overseas/.