Dear Chairman Baucus and Ranking Member Grassley:

The American Benefits Council (the "Council") is writing to express our opposition to a provision contained in H.R. 6049 (the Renewable Energy and Job Creation Act of 2008, as passed by the House of Representatives) [S. 3125 (the Energy Independence and Tax Relief Act of 2008, as introduced by Senator Baucus)] that would impose substantial tax penalties on non-abusive compensation practices. This proposal goes much farther than is necessary to address any perceived abuses and could have unintended consequences that would be very harmful to many U.S. workers and employers.

The Council’s more than 250 members include primarily major U.S. employers that provide employee benefits to active and retired workers, and do business in most, if not all, states. The Council’s membership also includes organizations that provide services to employers of all sizes regarding their employee benefit programs. Collectively, the Council’s members either directly sponsor or provide services to retirement and health benefit plans covering more than 100 million Americans.

Section 401 of H.R. 6049 [S. 3125] would require that amounts deferred under nonqualified deferred compensation plans maintained by certain foreign entities be included in income when there is no substantial risk of forfeiture with respect to the compensation (i.e., upon vesting). Although the provision is apparently targeted at hedge fund managers operating in offshore tax havens, its scope is much broader and it likely would apply to employers in all industries. Moreover, the provision inexplicably treats performance-based compensation and various types of equity compensation as nonqualified deferred compensation -- even where such compensation is not considered
nonqualified deferred compensation under the very broad definition in Code section 409A -- and would apply an interest charge and 20 percent penalty to performance-based compensation. This provision is significantly flawed, as we discuss in more detail below.

It is extremely broad and would apply to non-abusive compensation practices. The provision could apply to various types of compensation paid to U.S. taxpayers working outside of the U.S. for a foreign company – including a foreign subsidiary of a U.S. multinational – where the foreign company does not satisfy a test under which "substantially all of its income" must be subject to a "comprehensive foreign income tax." This provision could trigger immediate taxation and penalties in instances where there is no comprehensive income tax treaty between the U.S. and the foreign country or countries where the company does business (e.g., companies doing business in Brazil and most other South American countries, most African countries, and many Asian countries, including Hong Kong, Singapore, and Vietnam). Even where there is a comprehensive treaty with the U.S., the provision would apply if not substantially all of the foreign company’s income is subject to a treaty country’s tax system (e.g., because the country has a territorial tax system).

It targets equity compensation. The provision’s expanded definition of nonqualified deferred compensation would apply to stock appreciation rights (SARs) issued at fair market value and restricted stock units (RSUs) that pay out upon (or shortly after) vesting, both of which are exempt from Code section 409A. It is not clear what policy rationale is served by effectively outlawing the issuance of these non-abusive forms of equity compensation to U.S. taxpayers working for companies subject to the provision.

It targets performance-based compensation. The proposal would apply to performance-based programs that are exempt from section 409A because any bonus is paid shortly after the performance conditions are satisfied. Moreover, the proposal would impose an interest charge and a 20 percent penalty on amounts that are not reasonably determinable at the time of vesting, including where a performance bonus is not determinable because it is dependent upon the satisfaction of pre-established, objective performance criteria. It is not clear what policy rationale is served by effectively outlawing pay-for-performance programs with respect to U.S. taxpayers working for companies subject to the provision.

It would create great uncertainty and would be virtually impossible to administer. To determine whether the provision applies, a company would need to (among other things) determine (1) how internationally mobile U.S. taxpayers are paid, (2) whether any compensation comes from a foreign company, (3) whether any such compensation is treated as deferred compensation under the very broad definition in the provision, and (4) whether substantially all of the income of any foreign company paying the compensation is subject to a comprehensive foreign income tax.
**It is retroactive.** Apparently to drive more revenue into the 10-year budget window, the provision would apply even to amounts deferred for services performed before 2009 to the extent the amounts are not otherwise included in income before 2018.

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For the foregoing reasons, we urge you to reject this provision as currently drafted. Thank you in advance for taking our views into consideration.

Sincerely,

James A. Klein  
President