Morgan Lewis

CORPORATE INTEGRATION

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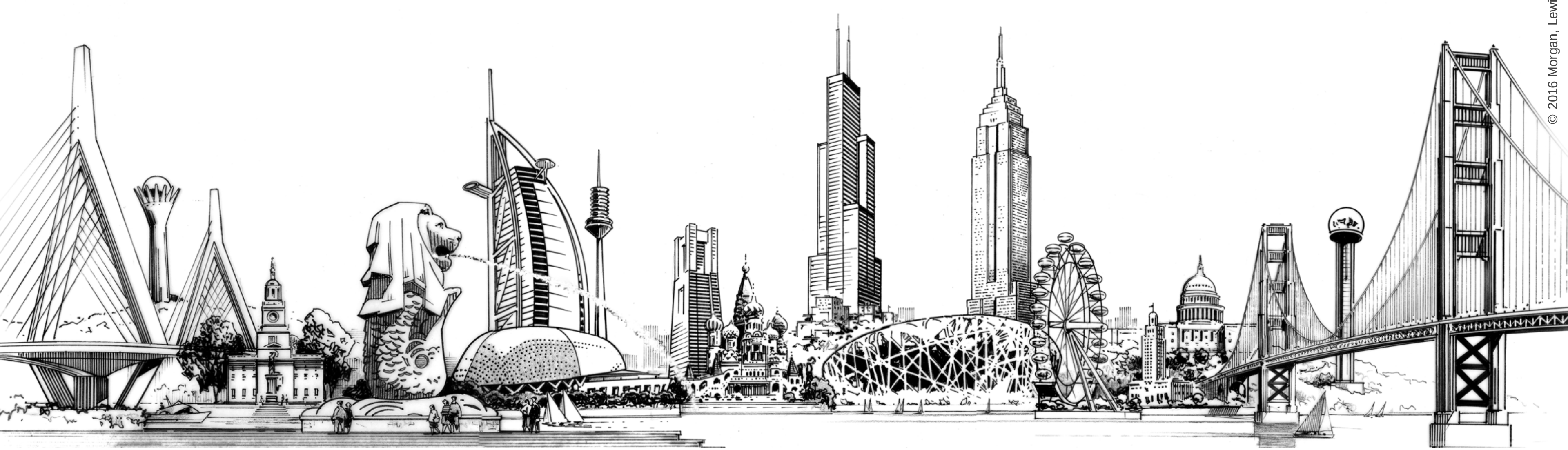

Biography

Alexander L. Reid
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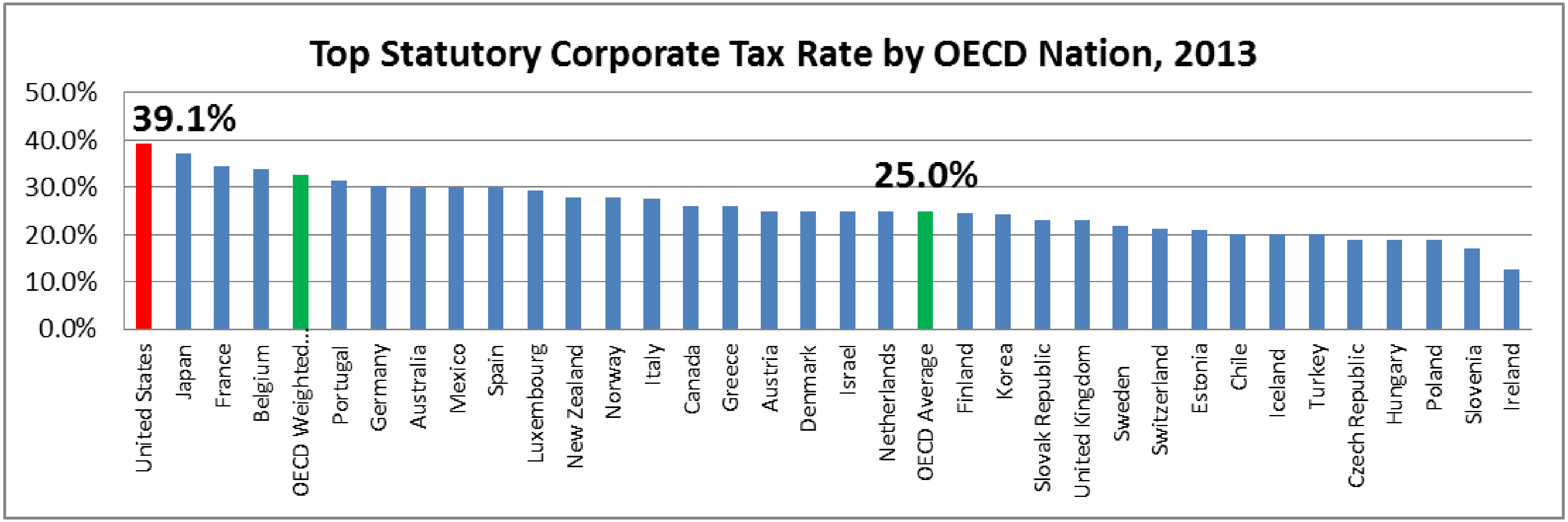
Alex is a tax lawyer whose clients include tax-exempt organizations of all kinds. He advises on transactional matters and also represents taxpayers under audit. He helps organizations improve their governance and enhance their tax compliance, counsels taxpayers seeking administrative guidance from the IRS and Treasury, and assists organizations with legislative matters before the US Congress.

Alex has experience in government as a civil servant, having served as legislation counsel for the Joint Committee on Taxation of the US Congress, where he advised members of Congress and staff regarding tax policy. He also served in the Treasury Department's Office of Tax Policy.

He earned a bachelor of arts from Yale University and juris doctor and legum magister in taxation from New York University School of Law where he served as Editor in Chief of the *New York University Law Review*.

US Statutory Tax Rate Is High

- The US statutory corporate tax rate (including state and federal tax) is high relative to other OECD countries
- This creates an incentive to move corporate earnings abroad.



Source: OECD

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Double Taxation

- Corporate earnings are taxed twice—
  - First at the corporate level
  - Second when distributed to shareholders as dividends
- **Corporate earnings distributed to tax-exempt shareholders (including pension funds) are taxed only once.**

Debt-Equity Distortion

- Corporations may distribute earnings as interest on debt or as dividends on stock
  - Corporations may deduct interest paid, thereby eliminating one level of tax
  - Corporations may not deduct dividends paid
- As a result, corporations have an incentive to issue debt rather than equity.

Distributions to Tax-Exempts

- Tax-exempt debt holders pay no tax on interest or dividends received
  - Corporate earnings distributed as interest to tax-exempt debt holders escape taxation altogether
  - Corporate earnings distributed as dividends to tax-exempt equity holders are subject to one level of tax.

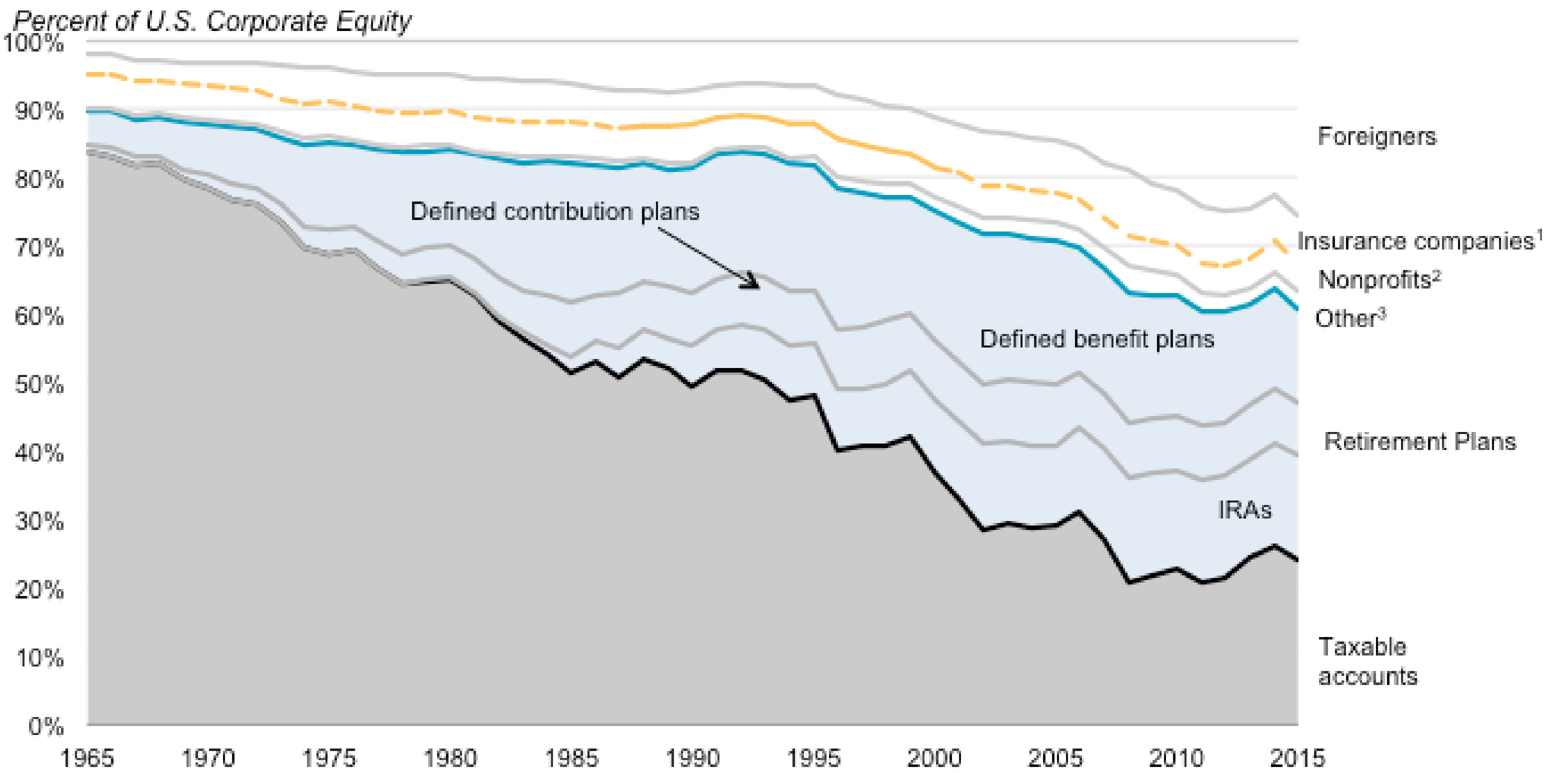
Tax Exempts Own 75% of US Corporate Stock

Source: Rosenthal, Austin, The Dwindling Taxable Share of U.S. Corporate Stock (Urban-Brookings Tax Policy Center, May 16, 2016)

FIGURE 1

Ownership of U.S. Corporate Stock, 1965-2015

Direct and Indirect Holdings



Source: Board of Governors of the Federal Reserve System, "Financial Accounts of the United States;" Investment Company Institute. 2016, "The U.S. Retirement Market, Fourth Quarter 2015;" Barclay Hedge; Preqin; Tax Policy Center calculations.

(1) Stock held in non-taxable segregated reserves to fund annuity contracts and whole life insurance.

(2) Dashed lines indicate TPC estimates

(3) Primarily government holdings, but includes equities in 529 savings plans.

Shareholder Credit Integration Proposal

- Proposal under active consideration:
  - Corporations permitted to deduct interest AND dividends
  - Withholding tax imposed at corporate tax rate
  - Shareholders and debtholders receive dividends and interest net of withholding tax, but are taxed on gross amount
  - Shareholders and debtholders claim tax credit on their returns for their share of the withheld tax.
  - Exempt shareholders and debtholders are unable to claim the tax credit because it is nonrefundable and basketed against taxable dividend and interest income.

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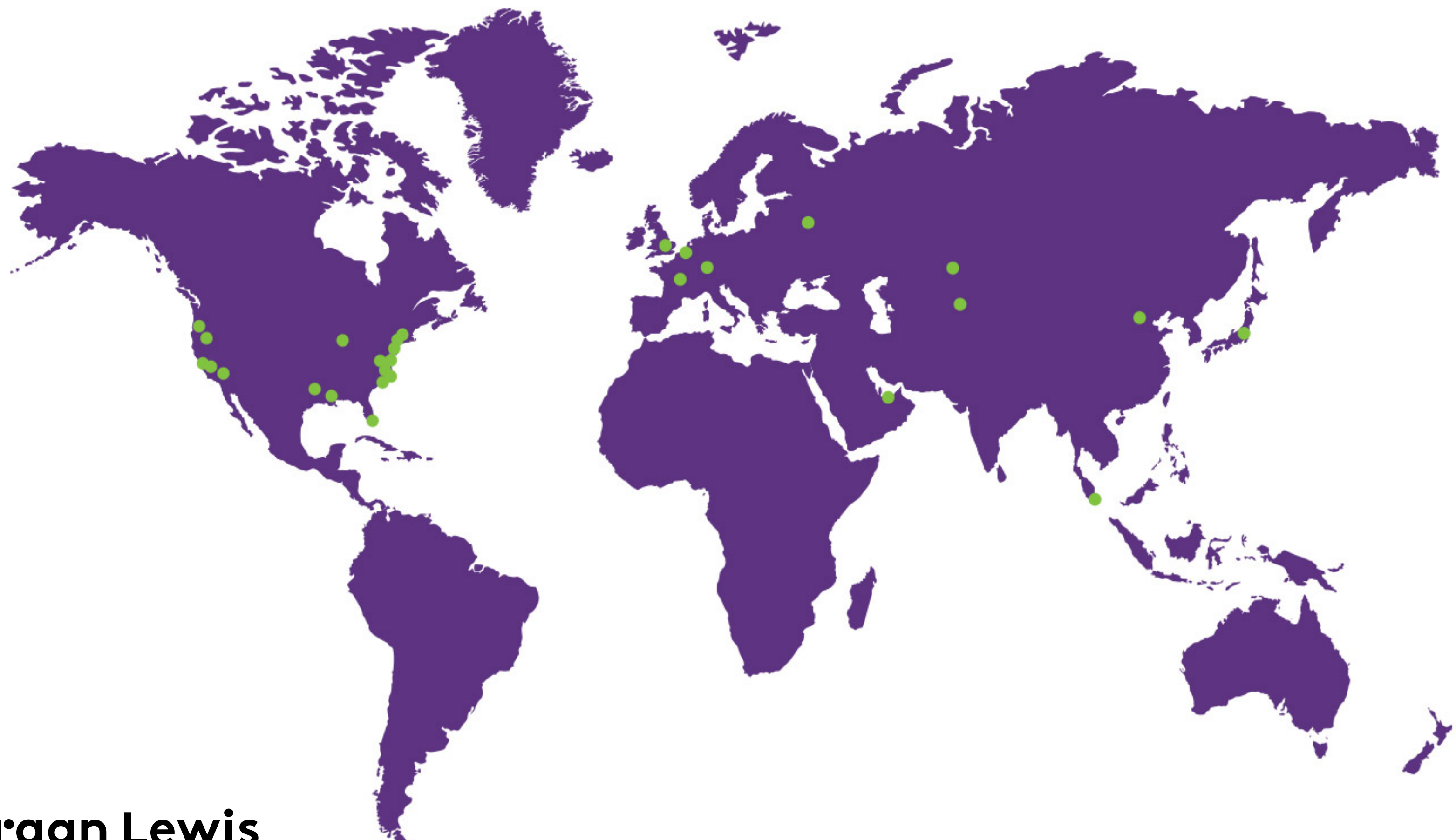

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