

TAX FAIRNESS: EUROPEAN DIPLOMATS URGE CALIFORNIA TO KEEP WATER'S-EDGE ELECTION

Diplomats from Germany, Luxembourg, Switzerland and the Netherlands arrived in Sacramento May 19, urging California to avoid any changes to the state's water's-edge method of taxing multinational corporations. The representatives were part of an informational hearing held by the Senate Select Committee on California-European Trade.

Speaking on behalf of their respective governments, the diplomats underscored the importance of stability and certainty for European businesses in determining in which foreign markets to invest.

Recent legislation by San Diego Assemblyman Marty Block, sponsored by union-backed lobbyist Lenny Goldberg of the California Tax Reform Association, claims that many corporations that do business in California are using "loopholes" to avoid paying taxes in California.

Nicolas Mackel, from the embassy of the Grand Duchy of Luxembourg, explained that his country is not a "tax haven," in the sense that it is not a low-tax place to do business. He noted that in 2009, the combined minimum federal, state and local corporate tax rate was 28.59 percent. He said: "I hope this will dispel the erroneous impression that Luxembourg might be considered in any serious way as a 'tax haven.' Luxembourg certainly is a paradise sir, but unfortunately not in a fiscal sense."

Mr. Mackel told the committee that Luxembourg businesses have \$132 billion invested in the California economy through their employment of Californians, and purchase of equipment and property in the state. He said that for many California companies seeking to enter the European market, Luxembourg is often identified as a good point of entry, and has become the foreign or regional headquarters for many California companies.

He also said that ever since the United States liberated his country from Nazi rule during the Battle of the Bulge, and joined in founding NATO, America and Luxembourg have "built a strong friendship on multiple levels."

Also emphasizing diplomatic relations, Julius Anderegg, consulate general of Switzerland, said the water's-edge election represents "an important long-standing compromise." He said that changing the method of taxation during hard economic times could be viewed as a "hostile move to the international business community."

Mr. Anderegg said: "Investors don't want to have surprises. It's as simple as that." He explained that many European investors have planned where and when to invest in California based on laws and regulations that have been in place for more than 20 years.

Earlier this year, Switzerland, in working with the United States Treasury and Internal Revenue Service, developed legislation to curb tax evasion in foreign countries and to renegotiate U.S.-Swiss double-taxation treaties. The legislation was formed after many

negotiations and concessions between Swiss bankers, Switzerland and the United States. Parliament is expected to review the legislation this summer.

Similarly, Netherlands Consulate General Mr. Bart van Bolhuis explained that there should be concern regarding "tax havens," but he emphasized that the problem should be resolved in an international context. He said: "Unilateral solutions are not helpful. Water's-edge elections work, so why fix something that is not broken."

According to comments from Johannes Buchholz, of the German-American Chamber of Commerce, many German companies also fear California's hostile business climate. Mr. Buchholz said: "When I have a company that wants to get established on the West Coast, the first question they ask is, 'Isn't this state bankrupt? Can I still do business here?'" He noted that many German companies are well aware of various studies and rankings that say California is the lowest ranking "business friendly" state in the union. Mr. Buchholz said that changing water's-edge would add one more argument against doing business in California.

California's legislation allowing taxpayers to elect how they report income earned either based on a water's-edge apportionment formula or by their worldwide sales, payroll and property, was authored by state Senator Al Alquist in **SB 85** (Chapter 660, 1986). The bill was supported by many foreign governments and foreign companies, as well as domestic businesses and state tax agencies. The bill was opposed by State BOE Member Bill Bennett and Lenny Goldberg, representing the union-backed California Tax Reform Association, who is now sponsoring Assemblyman Block's bill to undo certain provisions of **SB 85**.

Testifying before the committee, Cal-Tax Vice President and General Counsel Michele Pielsticker said that the original goal behind the water's-edge legislation was to stave off an "international trade war." Ms. Pielsticker said: "Something had to be done about mandatory worldwide combined reporting. This was a very long process."

Ms. Pielsticker said that California began reforming unitary taxes in 1977, but it took 10 years for interested parties to reach a compromise and pass legislation. She cited an article from *The New York Times* that quoted an Assembly staffer who said: "It's a miracle bill. Both sides won."