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U. S. Senate Committee on Finance
International Tax Working Group

Introduction and Overview of Liberty Mutual Insurance ("Liberty Mutual")

Liberty Mutual is pleased to submit comments to the International Tax Working Group on issues important to the worldwide property and casualty business.

Liberty Mutual is a U.S. headquartered, diversified, global insurer. We employ 50,000 employees across 900 offices and operate in 30 countries.

In terms of size, Liberty Mutual ranks 76th among Fortune 500 Companies. We also are the:

- 3rd largest property and casualty insurance writer in the U.S.;
- 3rd largest commercial lines writer in the U.S.;
- 5th largest personal lines writer in the U.S.; and
- 6th largest global property and casualty insurer in the U.S.

Worldwide revenue for 2014 was $39.6 billion (78% U.S./22% Foreign). Like other property/casualty insurers, Liberty Mutual's profitability is cyclical and highly affected by catastrophes ($2.7 billion, $1.9 billion, $1.3 billion, and $1.6 billion catastrophe losses occurred in 2011, 2012, 2013, and 2014, respectively).

In the foreign countries where Liberty Mutual operates, business operations and investments are not fungible. Liberty Mutual is subject to numerous regulatory requirements overseas, which include:

- Generally, in Latin and South America, assets must be invested in local issuances *(e.g.,* bonds).

- Departments that manage insurance information *(e.g.,* Claims and Underwriting) must be staffed both by local management and local employees. This is the case in Latin and South America and Poland.

- Books and records must be maintained locally and, typically, in the local language and in the legal currency of the country.

- Solvency II (a European Union Directive that harmonizes European Union insurance regulation similar to Basel II for banking) is designed to ensure that European Union insurers have sufficient capital to reduce the risk of insolvency. Once in effect, this is likely to result in more stringent capital requirements for insurers doing business in Europe.

To the extent permitted by local regulations, Liberty Mutual manages and/or supports foreign operations through centralized U.S. functions and employees (*e.g.,* stewardship, investment management, and IT). Liberty Mutual currently negotiates and issues debt in the U.S. through its U.S. holding company (or its U.S. insurance companies).

Tax Reform Priorities

From Liberty Mutual's perspective, tax reform should address the following matters:

- There should be a competitive U.S. tax rate (lower than 35%);

- There should be a worldwide or territorial regime that is competitive with other major countries in which Liberty Mutual does business;

- A repatriation tax, if any, should recognize that insurers cannot repatriate capital because capital is required to be maintained under local regulatory requirements; and

- Both the Active Financing Exception and Look-Through rules should be made permanent.

Current International Tax Regime

The U.S. is one of the few countries to tax worldwide income, and the U.S. statutory tax rate is the highest among OECD countries. Both deferral tax provisions and foreign tax credit provisions minimize the impact of double taxation on U.S. corporations doing business overseas.

The current Active Financing Exception (AFE) is critical to maintaining a level playing field with other non-U.S. insurers doing business in foreign countries. This is largely because investment income and invested assets sufficient to cover future insurance payments both for known claims and unknown contingencies are required by local regulators to be maintained in the host country. Without the Active Financing Exception, U.S. taxation of foreign active finance income would result in an additional tax cost and competitive disadvantage for U.S.-based multinationals. The current practice of extending the AFE, from time to time, on a temporary basis, results both in financial and business uncertainty.

The current Look Through provisions are critical to enabling U.S. corporations to redeploy capital overseas (from one foreign location to another) within the current worldwide taxation and deferral regimes. Unlike other industries, insurance companies cannot utilize "check the box" structuring opportunities. U.S.-based insurance companies would be at a competitive disadvantage with respect to funding foreign growth or acquisitions if they did not have the ability to redeploy capital from one foreign jurisdiction to another without incurring U.S. tax. Without the Look Through provisions, it would be less costly to fund foreign growth with U.S. capital than it would be to fund the same growth with existing, overseas capital. The result would be an erosion of funds available to invest in the U.S.

The temporary status of the Look Through rules results in business uncertainty. The ability of insurers to remit foreign earnings to the U.S. is subject to local regulatory approval that may not be received in a timely manner.

Historically, U.S. property and casualty insurers with significant U.S. losses lost the use of foreign tax credits due to their expiration. This resulted in some level of double taxation. However, the increased foreign tax credit carry forward period (from 5 to 10 years), and the overall domestic loss provisions (both enacted in 2004) have mitigated the potential for double taxation. These provisions should be retained under any regime that includes a foreign tax credit provision to mitigate instances of double taxation.

International Tax Reform

The territorial tax regimes that have been proposed thus far generally include some level of double taxation through a proposed participation exemption of less than 100%, coupled with the elimination of the foreign tax credit regime. It should be noted that any level of double taxation in excess of that imposed by other countries will result in a competitive disadvantage to U.S.-based insurers. Furthermore, proposals that are silent on the treatment of active financing income leave open the possibility that investment income of insurers earned overseas will be subject to tax in the U.S.

International tax proposals typically have included a transition tax that would be imposed on unrepatriated earnings as of a certain effective date, regardless of whether the earnings are available for dividends (or required to remain in the local country pursuant to insurance regulatory requirements). What this means for U.S. insurers is that there would be a material, one-time U.S. tax cost coupled with limited ability to repatriate the related foreign capital.

Proposals may include limitations on the deductibility of interest on U.S. debt or other U.S. expenses that support foreign operations. The most cost-effective debt typically is negotiated at the parent organization (*i.e.,* in the U.S. for U.S.-based, global insurers), particularly for regulated insurers. A U.S. parent organization also will invest in U.S. jobs in order to centralize global functions or establish "centers of excellence" in the U.S. Thus, disallowance of any financing or centralized functional expenses incurred in the U.S. would result in a competitive disadvantage for U.S.-based insurers.

Liberty Mutual is relatively indifferent between a worldwide system of taxation with an efficient tax credit mechanism where U.S. rates are in line with other countries and a territorial system. Under either system, we support proposals (introduced by Rep. Neal and others, and contained in the Administration's FY 2016 Budget) to limit deductions for reinsurance premiums paid by a U.S. insurance company to its foreign affiliates. These proposals make sense because reinsurance transactions with affiliates that are not subject to U.S. Federal income tax on insurance income can result in substantial U.S. tax advantages over similar transactions with entities that are subject to tax in the U.S. The excise tax on reinsurance policies issued by foreign insurers is not always sufficient to offset this tax advantage. These tax advantages create an inappropriate incentive for foreign-owned domestic insurance companies to reinsure U.S. risks with foreign affiliates.

Closing

We appreciate this opportunity to submit our comments on tax reform to the Senate Finance Committee International Tax Working Group. We would be pleased to meet with Members of the Working Group or staff to discuss any of these matters.