IN MEMORIAM

How to win friends and influence people while working in government

HARRY GRUBERT
1937–2017

BY IKE BRANNON

How does a bureaucrat have a lasting effect in his issue area? It is a delicate dance, to be sure. Most never try. Their ambitions do not lend themselves to anything nearly that grandiose, instead being content to stick to their knitting, collect a paycheck, and retire the moment they are eligible. Others let their passion—and ego—drive them to bend rules and propriety in pursuit of an agenda that is not necessarily what is best for society.

However, having a sizeable and positive effect on society as a bureaucrat is possible, and I have seen it done. The few I've known who have accomplished this shared a few common traits: a fierce intellect, the ability to do the hard work necessary to learn their discipline, an uncommon modesty, and patience.

Ed Clarke, who worked for the Office of Management and Budget for 30 years, did so by studying how we regulate the economy and asking how we can improve the quality of our cost-benefit analysis. (See "The Fruits of a Failed Dissertation," Winter 2013–2014.)

In the summer of 2017, another wildly influential bureaucrat named Harry Grubert passed away. Grubert was an economist for the Treasury Department and was one of the world's leading experts on the tricky business of how to tax multinational corporations. His thoughts on the subject came to be valued by governments, nongovernmental organizations, scholars, and even multinationals.

Shifting tax burdens / The basic problem with taxing multinationals is that most of them find it worth their while to shift their profits across jurisdictions so as to arbitrage differences in corporate tax rates. For instance, if the United States has a much higher rate than Canada, it makes sense for a multinational with operations in both places to book more profits to Canada and less to the United States.

There are myriad ways to do this. For instance, if a company's Canadian operations make inputs for a product that's completed in the United States, the firm can try to establish a high implicit "price" for those parts, which in the tax books raises its Canadian profits and reduces its U.S. profits. More often the firm achieves this by sending intangibles offshore at an aggressively low price or else by shifting risk offshore when the company has a hunch about how the risk will play out. Another trick is for a parent company to create high-interest-rate loans from a low-tax subsidiary to a high-tax subsidiary, which also effectively moves profits from a high- to a low-tax jurisdiction.

Libertarians would argue that tax rates should be as low as possible in order to minimize the incentives for such non-economic activities, or—failing that—that the tax code at least be kept simple in order to eliminate the mechanisms by which companies reduce or evade taxes, because such behavior can lead to the need for higher tax rates to cover the lost revenues.

Treasury's crack legal staff is well aware of such shenanigans; many staffers come from law firms that devised such tricks. While they do yeoman's working trying to prevent this behavior, stopping it is like Sisyphus pushing his rock up the hill.

Grubert thought about how we might create an environment where there simply were no such incentives to do such a thing. The easiest way to do that, of course, would be to abolish the corporate income tax altogether and instead attempt to collect the

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revenue either via a sales or value-added tax, a concept Grubert explored in research with his Treasury Department colleague Jay Mackie.

Another idea is to integrate the personal and corporate income tax and essentially ascribe each dollar of corporate profits to a shareholder, thereby assessing the tax liability by treating it as ordinary income. Doing such a thing would be a complicated exercise: over three-fourths of all stock is owned by entities that do not have any tax obligations, like nonprofits, tax-preferred accounts like 401ks or IRAs, or by foreigners who have no U.S. tax liability.

Ultimately, Grubert concluded, neither scheme would fly politically. With Rutgers University economist Rosanne Altshuler, he conceptualized an alternative: an international tax system with rules devised to prevent companies from shifting profits across jurisdictions, a low corporate tax rate relative to where we are today, and a minimum tax on supernormal returns. It's a third-best scenario to be sure, but it may be the best we can achieve given that countries sometimes aid and abet profit shifting when it is in their own interests—and such scenarios are not uncommon. Grubert and Altshuler's idea has such merit that House Republicans incorporated a version of it in their recent tax reform plan.

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Harry was also a wary observer of the Organization for Economic Cooperation and Development's Base Erosion and Profit Shifting (BEPS) Framework. The organization developed BEPS over a period of years in order to slow the members' race to reduce corporate tax rates or offer other business tax breaks to attract business or investment to their countries. Grubert acknowledged the problem was real: a paper he wrote in the early 1990s observed that the sensitivity of corporate activity to tax rates may have actually doubled between 1984 and 1992.

However, he was not sure that the eventual BEPS recommendations were the right strategies. He observed that countries are, in fact, quite fine with profit shifting if those profits are being shifted into their own country. In another paper, Grubert observed that for most companies a little more investment in Ireland—which has the lowest corporate tax rate in the OECD, at just 12.5%—and other countries with low corporate tax rates can lead to a lot more inbound investment from multinational corporations.

He refused to jump on the formulary apportionment bandwagon—which is a tax regime that allocates profits across jurisdictions based on various measures of economic activity in each jurisdiction—when that idea became the rage among tax economists as a way to limit profit shifting across jurisdictions. The big problem is simply that such a scheme cannot work unless literally every country in existence agrees to participate—a nearly impossible level of cooperation for sovereign nations. He also documented how the "check the box" election—a business's ability to self-classify as a corporation or some other entity as part its tax filing—exacerbated profit shifting, and suggested that U.S. tax laws are too permissive when it comes to shifting royalties across jurisdictions.

Turn toward international economics / Grubert did not begin as a tax economist; his first job in D.C. was with the Department of Labor. He joined Treasury in 1978, and he only gradually waded into tax.

His hesitancy to embrace international tax issues was understandable. Edith Brashares, a colleague of his at Treasury, remarked that when Grubert was earning his doctorate at MIT, the issue was considered a backwater in the economics discipline, and there was a paucity of research on the subject at the time. But Grubert—born in Canada to Jewish émigrés from Poland—took quickly to the issue, and in the ensuing decades it became increasingly important as international trade ballooned, multinational corporations expanded, and strategies to avoid corporate income taxes became increasingly complex and common—as well as lucrative.

As the discipline grew in importance, so did Grubert's influence. His research has been cited over 1,500 times in *Tax Notes*, an important publication avidly read by tax professionals and policymakers in Washington, DC. He published 44 academic articles on tax policy, with nine different co-authors, along with dozens of Treasury working papers. A paper he did on the international taxation of financial services won the Musgrave Award for the best paper published in the *National Tax Journal*.

But the best tribute to Harry Grubert is that politicians in both parties came to rely on him and greatly valued his counsel. Shortly before he passed away after a brief illness, I encountered a friend who worked on tax reform in the Trump White House. When I asked him how their plan was coming along, he remarked that they were waiting to get Harry's input before they proceeded. When he learned of Grubert's passing a few weeks later, he lamented that they were not sure what to do without him.