Podcast Transcript

The Tax Implications of The One Big Beautiful Bill on Global Pharma Supply Chains

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Kattman: In our last two episodes, we discussed the impact of U.S. policy shifts on global FDA-regulated products supply chain and shared industry perspectives on global supply chain disruptions. On today’s episode, we unpack the sweeping tax reforms introduced by the One Big Beautiful Bill Act signed into law on July 4th, 2025. With major changes to R&D expensing, international tax regimes, and incentives for domestic manufacturing, the bill is poised to reshape the global pharmaceutical supply chain. We explore how these provisions affect multinational pharma companies’ supply chain strategies. I’m Amy Kattman, and you’re listening to BakerHosts.

On today's episode, Winston Kirton, co-leader of BakerHostetler's FDA Practice and co-leader of the Life Sciences Industry team, will be speaking with BakerHostetler Partner Brian Davis. Let's listen in.

Kirton: Hello, friends. This is Winston Kirton. And today, it is my absolute pleasure to welcome my friend and partner, Brian Davis, to the podcast. Brian is resident with me in our Washington, D.C. office, and he heads up the firm's International Tax Group. His practice is built on decades of experience in law and accounting firm environments, as well as years of experience as international tax counsel for a publicly-traded global media conglomerate. He works with inbound and outbound clients on a diverse array of U.S. and non-U.S. tax matters, and with an emphasis on cross-border M&A and restructuring transactions, cross-border financing arrangements, international intangibles planning, and effective supply chain realignments.

Hello, Brian. We're delighted to have you join the podcast today. How are you doing?

Davis: Hey, Winston. It is great to be here. Thank you for inviting me to talk about a subject that is near and dear to my heart.

Kirton: Wonderful. So over the last two episodes, I have to tell you, our FDA-regulated product supply chain podcast, we've been discussing disruptions caused by U.S. policy shifts. And we also shared some, what I thought was, sage advice on regulated product industry perspectives regarding mitigating and managing supply chains disruptions. Today, though, which is in your wheelhouse, I'd like to chat with you a bit about the impact of the One Big Beautiful Bill Act on multinational pharma companies and their supply chain strategies. So, if you're good, let's get started with the basics.

The One Big Beautiful Bill Act was signed into law to address longstanding concerns about import practices, trade imbalances, and supply chain vulnerabilities. But Brian, what exactly does it do?

Davis: Yeah. So Winston, I think to appreciate what the Big Beautiful Bill Act does, requires that you step back for a minute and understand a few principle or some basic concepts from a tax planning perspective, and then also understand the U.S. tax landscape over the last 40 years. And if you'll indulge me for a second, I'll just set the table so that it is easier to understand what the Big Beautiful Bill is trying to do.

So from a tax planning principle perspective, I think it is important to understand that when we're talking about planning for multinational organizations in the life sciences or pharma space, there is a significant difference between a U.S.-based multinational and a non-U.S.-based multinational. And today, we're going to focus principally on U.S. multinationals, but understand that there are different and sometimes competitive economic differences between the two. I think a second tax planning principle to understand is that there are three key principle profit drivers within an enterprise, and that is an IP return, a manufacturing return, and a distribution or sales-based return. Those returns trigger profits, and where those profits are placed are significantly important in terms of determining the overall effective tax rate of an enterprise. And then, finally, aligned with supply chain is this concept of a tax operating model. And that is really, how do you structure your internal affairs to optimize for tax? And here, we'll see trade pop up, because things like trade policy and indirect taxes like VAT also influence this operating model. It is not just income taxes.

I think then to bring us closer to the Big Beautiful Bill, it is important to understand the U.S. tax landscape over the last 40 years. And there, there are three main eras that I would direct your attention to. And when you think of these in conjunction with those tax planning principles that I just mentioned, I think you'll start to see what the Big Beautiful Bill really is trying to do.

So the first era is really the era, I would say, between 1986 and 2017, and I'll call that the pre-TCJA era. That is really the era before our tax reform in 2017. And the TCJA really is the Tax Cuts and Jobs Act of 2017 that was a significant reset of tax policy here in the United States. But if you look at that pre-TCJA era, that era between 1986 and 2017, our U.S. tax system, corporate tax system, was a worldwide system that had a very high corporate tax rate, a 35% tax rate, which was an outlier amongst OECD countries. And there were also some very light anti-abuse rules that were used for policing active offshore businesses of U.S. multinationals. Those rules are known as Subpart F. And essentially, if you were very good at navigating Subpart F, it meant that you never had to pay that 35% tax that you would have had to pay on those offshore earnings if they had been earned in the United States. Instead, you would just pay the local tax. And it was easy to follow incentives in other countries to get that local tax down very low.

And what did that mean? What does that mean from a tax planning perspective? It meant that during that era, it was almost a knee-jerk reaction to put everything offshore, including your IP, because you could park more of your profits offshore by doing so. And the E.U. was somewhat complicit in this because they wanted jobs. If you look at a country like Ireland, Ireland created a very low tax regime, in part because they wanted lab coats to show up in their jurisdiction. They wanted their people to be employed. But what this pre-TCJ era really was known for, also from a U.S. multinational perspective, was it created what is known as a lockout effect. Because as long as those offshore earnings were maintained offshore, you could pay just the local tax rate. And so, if you could get that local tax rate down to 2%, that delta between the U.S. tax rate at 35% and 2% was a significant savings. And the lockout effect essentially meant that if you brought those offshore low-tax earnings back home to the United States, you had to pay the residual tax liability, that additional 33% in my example. So what that encouraged was keeping those offshore profits offshore and reinvesting in the offshore operations, which, for many U.S. multinationals, was where the growth was anyway. So it was a no-brainer.

If we shift now to 2017 in what I'll call the TCJ area again, the period between 2017 and July of 2025, we see tax reform set in the United States. And what that did was it reduced our corporate tax rate from 35% to 21%. And it also included other provisions that effectively neutralized this knee-jerk reaction that everything should just be put offshore, and instead created a carrot-and-stick approach that somewhat leveled the playing field between placing assets in the United States or abroad. And it also incentivized exports from the United States and somewhat eliminated the kind of free ride that occurred if you had been earning offshore operations because a new provision was enacted, we call it GILTI. It's got a new name now under the Big Beautiful Bill Act, but it effectively ensured that even if you were very good, as we all were, at navigating the Subpart F rules of the prior eras, there still would be some tax to pay on those offshore earnings if you were a U.S. multinational. And then it eliminated lockout effect, which had the incentive of allowing offshore earnings to come back to the United States without a residual U.S. tax owed. Which, think about it from a policy perspective, allows those earnings to come back in the United States and be reinvested in U.S. jobs and U.S. manufacturing. And then I guess the last piece of that TCJA era was there was 100% expensing that was allowed that, really, what that meant was, is if you put equipment into the service in the United States and if you did R&D in the United States, you effectively were able to deduct those expenses in the near term.

So those created, relative to the prior era, a significant incentive to reshore operations. Now, it wasn't 100% perfect, and a lot of companies didn't change their operating models that had been developed over years. But we did see with the tech companies that the TCJA did incentivize some tech companies to bring back their IP to the United States and take advantage of the FDII, or Foreign Derived Intangible Income, provision that was adopted as part of the TCJA. And that provision effectively allowed export income of a U.S. company to be taxed at a 13% rate as opposed to a 21% rate. So we saw some tech companies do that. We didn't see as many of the life sciences or pharma companies do that. And in part, that has to do with the substance that companies in the life sciences and pharma space have built up over years. There is actually real manufacturing and operations overseas, whereas a lot of the tech companies can operate digitally and have a lighter physical footprint overseas than, say, a company that is involved in chemicals or life sciences manufacturing.

Another part that I think discouraged, or at least did not incentivize, life sciences and pharma companies in terms of bringing back manufacturing to the United States was really the structure of the market itself. And if you look at something like the tech companies, they're able to reach their consumers digitally, and the consumer pricing outside of maybe VAT and indirect tax issues is not really that different globally. But if you look at the life sciences and pharma industries, you'll see that the profits for distribution into the U.S. market are a multiple of the profits that you get for, say, distributing into the E.U. And so I think that also the structure of the tax policies aligned with the market dynamics, and the historical buildup of manufacturing by life sciences companies overseas, really encouraged that maintenance of offshore manufacturing.

Now, if we turn now to 2025 and the Big Beautiful Bill era, I think what we see there is the Big Beautiful Bill builds off of the Tax Cuts and Jobs Act and the tax policy principles that were adopted as part of that act. But what it does is it makes those things permanent. Under the TCJA, the 2017 tax reform, many of the provisions that were enacted had a shelf life of five or maybe 10 years, and then they went back to the old law. And the Big Beautiful Bill made those changes that were enacted as part of the TCJA permanent. And it also corrected some mistakes by basically putting the thumb on the scale in favor of onshoring, and we can get into that in a little bit. But I think it is important for those who are in the life sciences industry or the pharma industry to understand that this Big Beautiful Bill, at least from a tax policy perspective, really is just one leg of what I think of as a three-legged stool that the Trump administration is using to encourage domestic production. The other legs are tariffs, as everybody is aware, and the executive order on pharma pricing that recently came out.

Kirton: That is an incredible frame, and I think it really sets the baseline for what is going on with the Big Beautiful Bill altogether. And you and I were talking, we said, listen, this, the Big Beautiful Bill Act really applies to all levels of manufacturing, all various enterprises. However, even within the FDA-regulated space, it is across the board. But we wanted to focus on pharma because of much of what you mentioned before, the offshoring, the incentives, and whatnot.

So I want to ask you about, more specifically, the impact or the significance of the Big Beautiful Bill, the significance of those international tax changes on pharma. But also, you mentioned foreign-derived intangible income, and that's now become foreign-derived, deduction-eligible income. That is why I have an expert like you on, because you obviously have a deep appreciation for these acronyms. And then you also mentioned GILTI in your frame, Global Intangible Low-Taxed Income, which my understanding is now called net CFC tested income. So, two-part question. Is the significance of the international tax changes in the Big Beautiful Bill for pharma, right, taking into consideration some of the things you mentioned? And then, how does foreign-derived, deduction-eligible income and net CFC tested income reshape tax planning for global pharma operations? Two parts.

Davis: Sure. Alright. Let me, I will say this. I think that the changes to GILTI and FDII, which I'll continue to refer to them as GILTI and FDII, despite the new name changes, because that is how most of us in the industry still refer to these provisions. Those are probably the most impactful in terms of changing the dynamics, those are probably the most impactful international rules in terms of changing the dynamics regarding where supply or functions may be placed, the U.S. or ex-U.S. And so, let me focus on those in just a second.

I will say, there are some other provisions of the Big Beautiful Bill Act that I think really are important for life sciences and pharma companies. Permanence, we already mentioned, is one of them. So making everything permanent helps everybody plan from a tax perspective. The 100% expensing is a really significant benefit, and the Big Beautiful Bill Act extended that to facilities. So now, if you're building a manufacturing facility in the United States and you're operating it, you can expense the entire cost. And normally, a portion of that facility would have had to have been capitalized and recovered over something like, say, 39 years. And so that is a big incentive. You get a big jolt by just starting your production and building your facility in the United States.

R&D deductions, the changes that were made to the ability to, again, deduct immediately your R&D expense for expenditures made in the United States, as opposed to capitalizing them and recovering them over a five- or other year period, is significant. Because it is driving that R&D, again, back to the United States, and that is big for life sciences and pharma. There have been changes to interest deductibility. The Big Beautiful Bill moves back to a still restrictive, but less restrictive than in recent years, limitation on interest deductions. And that helps those who are financing facilities. And then there are a smattering of other benefits that encourage investment by other actors, by private actors, to get into or invest their capital into U.S. production facilities.

But let's turn to the second part of your question and really talk about how that changes the dynamic for life sciences and pharma companies, and that is the GILTI and FDII changes. So the changes, so again, FDII was a provision that was enacted in the TCJA in 2017 that was designed to encourage export sales, so distribution out of the United States. And the changes that were made by the Big Beautiful Bill are essentially encouraging onshoring and are driving the scale farther in the direction of placing not only your production, but your distribution profits in the United States.

And how did they do that? How did Congress do that? They eliminated something known as the Qualified Business Asset Investment return, or QBAI return. And that return essentially was a hurdle that people had to overcome before they got into this preferential rate. So if you were selling product out of the United States and you were normally subject to 21%, it used to be that you had to overcome this investment in physical assets that you had made in the United States before you could actually get into the 13% rate on your income. That's been eliminated, so you don't have this hurdle that you have to overcome before you go from income tax at 21% to income tax at 13%. And it also changed some expense allocation rules, which I'm not going to get into, but essentially, the changes were designed on the FDII's side to make it so that you got into that preferential rate more quickly than you would have before the Big Beautiful Bill. So that encourages U.S. onshoring of IP, and it encourages distribution out of the United States.

The changes that were made to GILTI, or now known as net CFC tested income, are really changes that were designed to reduce any lingering incentives that might have been there after 2017 to place operations offshore. Our tax laws recognize that if you need your operations to be offshore, you need to have manufacturing close to a customer, then it makes sense to do that. But what the Big Beautiful Bill did was it, in addition to making the rates for GILTI permanent, it also eliminated that QBAI return. Which, unlike the FDII QBAI problem under the GILTI regime, the QBAI return under GILTI was a benefit because it meant that you didn't pay tax on earnings until they cleared that hurdle, that QBAI hurdle, which was geared to your investment in tangible property abroad. So if you think about it, the historic GILTI rules would give you, from a U.S. tax perspective, a free pass, almost tax-free income on earnings, to the extent that you had built overseas production facilities. And it was only once you crossed over that QBAI hurdle that you started having that offshore income taxed in the United States.

And so those two changes, again, I think shift the dynamic where it incentivizes, or at least it disincentivizes just automatically establishing new production abroad. If you need to do it for commercial reasons, obviously, you do it. But if you are just doing it because there is a QBAI benefit and/or you have this historic manufacturing operation offshore, the changes to GILTI reduce that benefit that you previously had and the changes to BIDI stop creating disadvantages for building productive facilities in the United States.

Kirton: Wow. Okay. So I'm hearing, Brian, from what you're explaining, that this Big Beautiful Bill obviously has implications for multinational tax planning as well as IP management. You made that clear. It obviously will have impact on API imports and perhaps other imports for multinational pharma. Obviously, I've heard tariffs and tariff signals, which would essentially force sourcing diversification. And then, lastly, what I've heard, which is music to my ears and we see many of our clients starting to respond, in regards to reshoring or unshoring and domestic manufacturing and the incentives that are being created by the Big Beautiful Bill, including upstream with R&D expensing.

So in the last couple minutes that we have here, and I'm mindful of your time, we always like to give some takeaways for our audience, right? And I'm hopeful that our audience is going to be made up of pharma CFOs and tax directors and tax stakeholders. And, of course, our audience will also be made up of legal teams and pharma. So what advice, besides calling BakerHostetler and connecting with you and I, what advice would you give to these pharma CFOs and tax directors on what they should be preparing and how they should strategize? Perhaps just a couple, top-of-mind. And then legal teams, how should legal teams be responding to the impact of the One Big Beautiful Bill Act on pharma company supply chain strategies?

Davis: Yeah, thanks. I would say this, we already mentioned that the Big Beautiful Bill is part of a three-legged stool; we've got sectorial tariffs and the EO on drug pricing. I think just understand that modeling supply chain realignments and considering onshoring as an alternative is something that you should be engaged in. And I say that because, although we have the policies that are coming out of the Big Beautiful Bill Act, remember that there are other things out there that are not maybe enacted in law yet, but are lurking in the wings.

I'm talking about things like the tax on round-tripping. That is really the structures that I've been talking about, where U.S. multinational continues to have its production offshore and it sells that production into the United States. Why? Because it can park significant profits offshore at a very low rate. There are bills that have been circulating, and the Democrats have certainly been promoting, anti-round-tripping bills. Which would effectively ensure, if enacted, that the income earned by CFCs for sales into the U.S. market are taxed at regular rates. So there is a possibility, and I wouldn't put it past the populist Republicans also to align with the Democrats on this and really focus on this round-tripping problem or something that they consider to be a problem. And then things that you and I have talked about in the past, Winston. Things like the BIOSECURE Act enjoy bipartisan support and are designed to root out Chinese influence in our life sciences and pharma supply chains, but is also designed to encourage reshoring or onshoring.

So just be aware that this modeling exercise is something you should take seriously because there are other shoes that may drop later. And when you do that, you need to take into account things like, what does my FDII benefit look like if I were to shift distribution to the U.S.? I'm not saying that people will do that necessarily, but it is something to take into consideration. And then, and it is a big if, but if people were to move their IP back in the U.S., you've got to focus on what that cost will be to do that. Because, although the U.S. may be encouraging through its tax policies, it is unlikely that the location where that IP resides today would not try to tax it on exit. So those are things to think about.

I think transfer pricing is something that is significantly important in supply chain planning. And I think tariffs and these shifts, I think it is important to understand what tariffs one mean for your transfer pricing. You might think about whether U.S. should be a limited risk distributor, that is a distributor within the group that earns a very small profit, or whether it should be earning a larger profit with an ability to repatriate the funds if you're a foreign multinational back home, or maybe put some of that profit into a company that is going to benefit from FDII. And then prepare for audits in this regard. Because anytime you're shifting your transfer pricing or you're doing restructurings, there will be tax authorities out there looking to audit you. Those are the high-level thoughts here. We've got the U.S. really trying to encourage onshoring and domestic manufacturing, but there are going to be consequences in other jurisdictions that need to be taken account, and you need to model this.

I think from a legal perspective, and this is probably equally applicable to finance departments as well, I think you want to think about, what are those local incentives? Winston, you and I have talked about incentives at the local level, not at the federal level, but here in the United States, the local level for production. And we're seeing a lot of interest in exploration with local authorities as to what is possible. And then, again, I think thinking about the operating models and your intercompany contracts are going to be very important for the legal department. Because, rightly or wrongly, when a tax authority comes to audit a company, they start with the transfer pricing and the transfer pricing intercompany agreements. Just making sure that those are durable, and fit for purpose, and are aligned with any model changes that are made, are going to be incredibly important. Because, as we've seen in some of the jurisprudence that have come out of the U.S. tax court, as models shift and intercompanies no longer reflect the operating model, it creates an opportunity for judges to rule against companies.

Kirton: Wow, what a roadmap. What spot on recommendations, just an incredible share of depth and information around this. I thought Brian, having partnered with you, and we've been discussing these matters for several months and then culminate with the Big Beautiful Bill, that I learned a lot. But I still learned even more on this podcast. And I know we can continue forever and ever on here because you're so very passionate about this, but this is that, we've come to our time. And I just want to thank you for being such a gracious guest with your time and so informative.

I believe that our listeners have really got a gem today. And we like to tell our listeners and our clients, look, you don't have to go it alone. You don't have to be fearful of what is coming out in terms of policies and new tax, perhaps, implications. Embrace them. Come talk to us, and we'll help you put a plan that makes sense for you in place and is actionable.

So Brian, thank you, again, for your time. You're an incredible partner. And I look forward to us coming back at some point and expanding on the impacts of the Big Beautiful Bill on pharma supply chains globally, and maybe even jumping into some other sectors. Would you be up for that?

Davis: I would, Winston. Thank you so much for inviting me to be a part of your podcast. I've really enjoyed it, and I'm so happy that we're partners and we get to approach these issues together.

Kirton: Wonderful, take care. And to our listeners, be well, and reach out. You don't have to go it alone.

Kattman: Thank you, Winston and Brian. If you have any questions for Winston or Brian, their contact information is in the show notes. As always, thanks for listening to BakerHosts.