KEY INTERNATIONAL TAX ASPECTS OF PENDING TAX REFORM

What you need to know

December 7, 2017

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With you today

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Pending US tax reform

Challenges presented to U.S. Multinationals in managing the complexity of U.S. Tax Reform in record timing

Paul Heiselmann

Pending US tax reform

Legislative Process Update

Todd Simmens

Federal Tax Legislative Process

WHO’S INVOLVED?

- “All Bills for raising Revenue shall originate in the House of Representatives; but the Senate may propose or concur with Amendments as on other Bills.” U.S. Const. Art. 1, Sec. 7.1. Formally, tax legislation must originate in the House of Representatives; it must take action before the Senate
- Individual members of the House or Senate may prepare a proposed law, or ‘bill’
- The House Committee on Ways and Means and Senate Committee on Finance are each responsible for considering tax legislation. Proposals are ‘marked up’ by a committee
- Staff from the (Congressional) Joint Committee on Taxation and U.S. Treasury Department generally assist in analysing policy changes. The Joint Committee on Taxation is the official scorekeeper.
- Legislation counsel from both the House and Senate assist with drafting bill language

Federal Tax Legislative Process

WHO'S INVOLVED?

- Ways and Means and Finance generally prepare 'committee reports' to describe marked up bills
- The Joint Committee on Taxation generally prepares a 'blue book' explanation of legislation after it is enacted
- ***Conference Committees are chosen to reconcile House and Senate bills when they are different. A conference report is generally prepared describing the agreed-to bill***
- The President/Treasury Department generally issues its suggested legislative changes ('revenue proposals') near the start of the calendar year. These can often become part of the legislative discussion.

The prospect of tax reform – other considerations

- Number of legislative days remaining as of December 7, 2017
  - House has 6 legislative days through December 14, 2017 (then recess)
  - Senate has 7 legislative days through December 15, 2017 (then recess)
- Climate
  - Distractions
  - Momentum
- Senate
  - Filibuster
  - Reconciliation
  - On-the-fence members
- Complexity of tax legislation
- Consequences of tax reform moving into 2018

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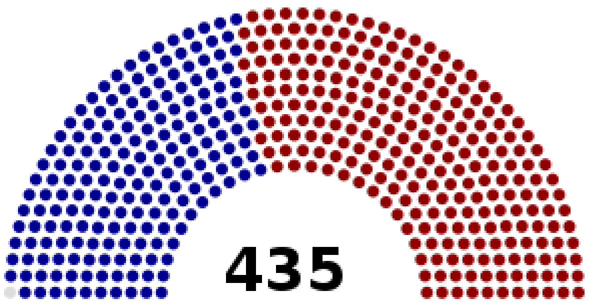
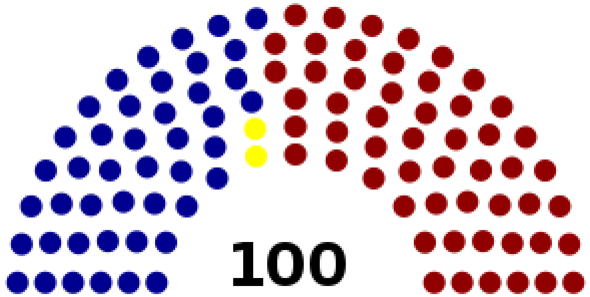
The prospect of tax reform – the numbers





HOUSE:

Republicans: 240

Democrats: 194

Independent: 1

Source House Press Gallery as of 11/13/17

Source: google

SENATE:

Republicans: 52

Democrats: 46

Independent: 2 (caucus with Democrats)

Source Senate as of 11/13/17

Source: google

The Conference Process

- House moved earlier this week to set up a conference committee to work out differences with the Senate
- Senate is expected to do the same this week
- Leadership from both chambers will appoint conferees
  - Leadership from both tax writing committees
  - Other members

- Joint Committee on Taxation
  - Non-partisan, Bicameral
  - Confer with Members and staff to analyze potential options
  - Prepares explanatory statement of managers portion of the conference report
  - Fields questions
  - Revenue estimates

Pending US Tax Reform

Foreign Earnings and Transition Tax

Joe Calianno & Monika Loving

Models of International Taxation

- **Worldwide Taxation /Deferral System:** A resident corporation is taxed on its worldwide income; the earnings of a foreign subsidiary are taxed when such earnings are actually or deemed to be distributed to the resident parent corporation
- **Exemption/Participation Exemption System:** Resident corporation is generally not subject to tax (or taxed at a significantly reduced rate) on earnings of foreign subsidiaries when distributed (some jurisdictions may have anti-deferral/CFC rules).

- U.S. imposes a worldwide taxation / deferral regime
  - U.S. corporations (and U.S. citizens and residents) are subject to U.S. tax on worldwide income
  - U.S. taxpayers may be able to mitigate double taxation (both U.S. and foreign tax on same items of income) via U.S. foreign tax credit regime.

Transition Tax under the senate bill

- As a part of the adoption of a participation exemption for foreign dividends, a 'transition tax' would apply for foreign earnings and profits (E&P) not previously subject to U.S. taxation.
  - Under the Senate bill, the transition tax rate is higher than under the House bill.
  - Rates applicable for domestic corporations for the transition tax generally is 14.5% of earnings comprising cash and cash equivalents, and 7.5% on non-cash earnings.
- Applies for tax years beginning BEFORE 2018 applied on the higher of the net E&P as of November 9, 2017, or December 31, 2017.
- Generally applies to U.S. shareholders owning at least 10% of certain foreign corporations.
  - U.S. individuals and Pass-through entities may be impacted
  - Deferral election for S Corporation shareholders
- Election to pay the tax liability over a period of up to 8 years in installments.
  - 1st payment due – April 2018.

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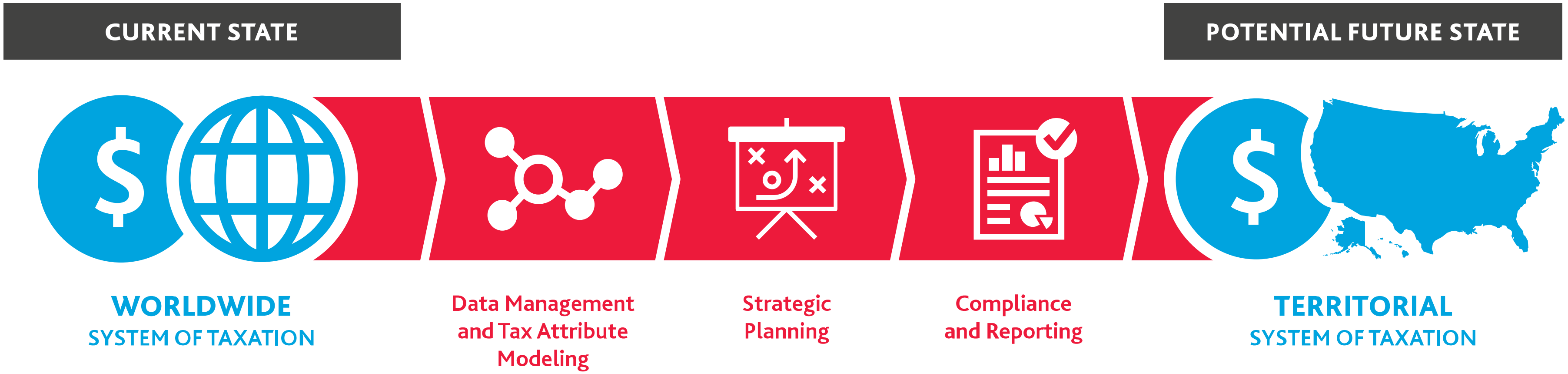
Transition Tax Side-by-side Summary

HOUSE VERSION	SENATE VERSION
▶ 10% U.S. shareholders of specified foreign corporations required to include post-1986 historical E&P as of 11/2/2017 or 12/31/2017 (whichever is greater) ▶ Subpart F ▶ 14% rate for E&P comprising of cash and cash equivalents ▶ 7% rate for E&P comprising of illiquid assets ▶ Deficits available to reduce inclusion ▶ Scaled back FTCs ▶ Election to pay over 8 equal installments ▶ Special deferral election for S-corporation shareholders	▶ Generally similar ▶ Testing as of 11/9/17 or 12/31/17 (whichever is greater) ▶ Rates higher under Senate version (e.g., rates for domestic corporation generally are 14.5% rate for E&P comprising of cash and cash equivalents and 7.5% rate for E&P comprising of illiquid assets) ▶ Election to pay over 8 installments with amounts increasing over time ▶ Limitations on assessment extended ▶ Special rules regarding REITs ▶ Election to preserve NOLs

Journey to a Territorial System of Taxation



Definition of E&P

- Earnings and profits ("E&P") is a tax accounting term
- E&P generally represents an increase or decrease in the amount of net assets of the corporation (subject to numerous special rules)
- E&P is intended to be an economic concept to measure the funds of a corporation available for distribution to its shareholders
- E&P is not defined in the Internal Revenue Code, and it is not equivalent to taxable income, book income, or retained earnings
- E&P is an annual computation

Calculation of Post-86 E&P

Starting with the entity's local country GAAP/Statutory reporting (financial statements) in functional currency

+/- Adjustments under U.S. GAAP principles

+/- U.S. tax adjustments

= Current Legacy E&P

+/- E&P received from lower tier CFCs or distributed

+/- E&P acquired in certain transactions

= <u>Current Year E&P Increase/Decrease</u>

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ASC 740 Tax Accounting Impact and Uncertainties

Mike Williams & Monika Loving

ASC 740 impact for transition tax

- Impact of change in tax law reflected in income tax expense/benefit from continuing operations
- Remeasurement of deferred tax asset/liability positions in period of enactment regardless of effective date
- Subsequent events
- Other possible impacts:
  - Effective tax rate and cash taxes.
  - Current taxes payable/Non-current taxes payable (FIN 48) – e.g., rate change.
  - Deferred tax assets/liabilities – possibly due to having to revalue and new items.
  - Valuation allowance positions.

Pending US tax reform

How can you position your organization for the challenges ahead?

Matt Becker

Questions?

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