



TAX STRATEGIST

CROSS-BORDER ISSUES

THIRD QUARTER CONSIDERATIONS

September 21, 2022

Agenda for Today



Introductions



Overview of Inflation Reduction Act



Global VAT Management and Value Creation



BEPS 2.0 Updates



Legal Entity Rationalization/Repatriation



Closing

With You Today



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Overview of Inflation Reduction Act



The Inflation Reduction Act and Beyond

THE INFLATION REDUCTION ACT (IRA)

- ▶ Introduced July 27, 2022
- ▶ Passed the Senate August 7, 2022, 51-50
- ▶ Passed the House August 12, 2022, 220-207-4
- ▶ Signed into law on August 16, 2022
- ▶ 15% minimum tax for certain large corporations
- ▶ 1% excise tax on corporate stock buybacks
- ▶ Two-year extension of IRC Sec. 461(l) loss limitation rules for noncorporate taxpayers
- ▶ Substantial funding for Internal Revenue Service
- ▶ Energy incentives



WHAT'S NOT IN THE LAW?

- ▶ Carried interest
- ▶ Increase in SALT deduction cap
- ▶ Other increases in tax rates



WHAT'S NEXT?

- ▶ Midterms
- ▶ Could we see additional tax legislative activity?
- ▶ IRS/Administrative/Regulations

U.S. Book Minimum Tax - Overview

- ▶ The Inflation Reduction Act, passed in Congress and signed by the President, introduced a corporate book minimum tax (“BMT”) that imposes a 15% minimum tax on adjusted financial statement income (“AFSI”) for corporations with average annual AFSI in excess of \$1 billion in the preceding three years.
- ▶ The BMT will increase the applicable corporation’s tax liability only to the extent it exceeds the corporation’s regular tax liability and BEAT liability.
- ▶ The Act defines a corporation’s AFSI for any tax year as the corporation’s net income or loss set out in their applicable financial statements, as adjusted in accordance with the provisions of the Act.
 - The specified adjustments pertain to related entities, certain items of foreign income, disregarded entities, defined benefit plans and depreciation, among other items. There is also a deduction for financial statement net operating losses.
- ▶ An applicable financial statement (“AFS”) generally includes:
 - Statements certified as prepared in accordance with generally accepted accounting principles (GAAP) and required to be filed with the U.S. Securities and Exchange Commission.
 - If no GAAP statements, statements prepared on the basis of international financial reporting standards (IFRS) and filed with the agency of a foreign government.
 - If no GAAP or IFRS statements, other statements filed by the taxpayer with a regulatory or governmental body as specified by the Treasury.
- ▶ The BMT applies to tax years beginning January 1, 2023.

U.S. Book Minimum Tax - International Items

- ▶ The BMT is not expected to be considered a Qualified Domestic Minimum Top-Up Tax under the Pillar Two rules.
 - Additional guidance is needed on how the BMT and Pillar Two rules would interact.
- ▶ AFSI includes a U.S. shareholder's pro rata share of the net income or loss on the CFC's AFS.
 - Any loss will not reduce AFSI but will be carried forward to the next taxable year to offset future net CFC income.
 - Subject to future guidance from the Treasury to prevent double counting of income from CFCs (deemed and actual income).
- ▶ The Act includes a new corporate AMT foreign tax credit ("FTC"), which is available to an applicable corporation that claims an FTC for the tax year.
 - For taxpayers that claim FTCs for regular tax purposes, the book minimum tax is reduced by the Corporate AMT FTC, defined as: (i) the taxpayer's creditable foreign income taxes that are stated on its AFS and paid or accrued by the taxpayer, and (ii) the taxpayer's pro rata share of the aggregate creditable foreign income taxes paid or accrued by its CFCs, stated on the CFCs' AFS for the taxable year.
 - The statute does not provide for a limitation on the utilization of "direct" taxes paid by the U.S. taxpayer, but it limits the aggregate amount of taxes paid by CFCs to 15 percent of the taxpayer's CFC net income. Any excess CFC taxes may be carried forward for five years.
- ▶ Notably by setting the minimum tax higher (15%) than the current GILTI effective tax rate (10.5%), the BMT could result in additional U.S. tax imposed on GILTI inclusions.

U.S. Book Minimum Tax - Application to Inbounds

- ▶ The book minimum tax applies to U.S.-related income of a foreign-parented multinational group when the AFSI of all members of the multinational group exceeds the \$1 billion three-year average annual net income threshold.
 - However, the tax will only apply when the net income in the U.S. equals or exceeds \$100 million on average over a three-year period.
- ▶ The legislation defines a foreign-parented multinational group with respect to any tax year as two or more entities that meet three specifications:
 - At least one entity is a domestic corporation and at least one is a foreign corporation.
 - The entities are included in the same applicable financial statement for the tax year.
 - The common parent of the entities is a foreign corporation, or, if there is no common parent, the entities are treated as having a common parent that is a foreign corporation under applicable rules.
- ▶ For these purposes, the legislation specifies that, in the case of a foreign corporation engaged in a trade or business in the U.S., the U.S. trade or business will be treated as a separate domestic corporation wholly owned by the foreign corporation.
- ▶ The Act directs the Treasury Department to issue regulations for determining when entities are treated as having a common parent that is a foreign corporation, the entities to be included in the foreign-parented group, and the common parent of the group.

Global VAT Management and Value Creation



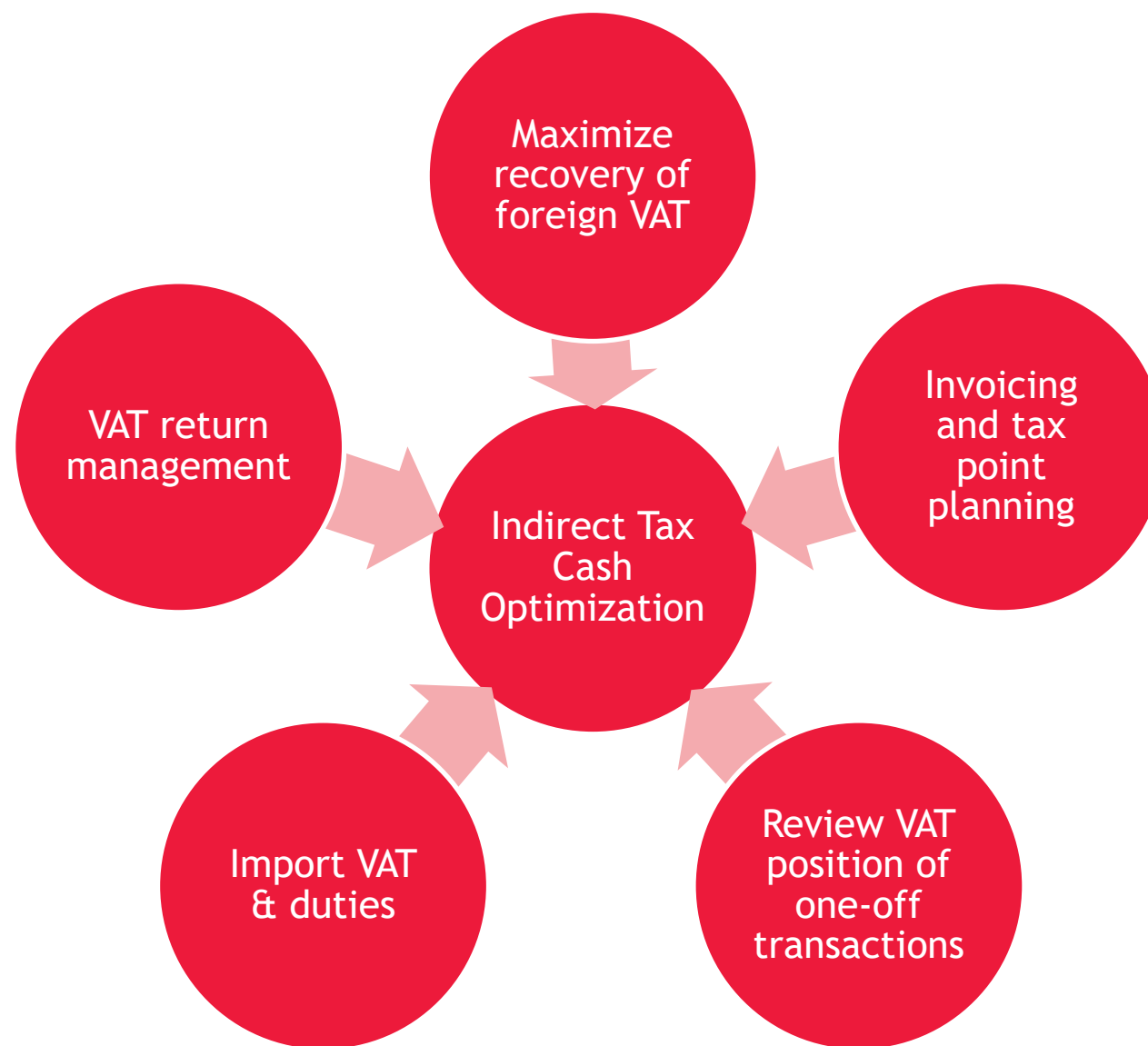


Global VAT Management and Value Creation

- ▶ Perception
 - Cost control
 - Risk mitigation

- ▶ Value creation
 - P&L savings
 - Working capital improvements
 - Risk mitigation
 - Quantification methodologies

Global VAT Management and Value Creation



OECD BEPS 2.0 UPDATE



Latest Developments - BEPS 2.0

PILLAR ONE

- ▶ OECD expecting to reach technical agreement on Pillar One by the G 20 November 2022, model rules expected to be drafted by end of year
- ▶ Practical implementation likely to be 2024

PILLAR TWO

- ▶ EU ECOFIN meeting in October to revisit status of Pillar Two - currently Hungary not in agreement. EU exploring other mechanisms to pass Directive within the EU
- ▶ France, Germany, Italy, Netherlands and Spain announced they will implement unilaterally if EU does not reach agreement
- ▶ UK, South Korea indicated implementation 2024 - South Korea introducing UTPR and IIR effective 2024
- ▶ Impact on delay in Pillar One implementation to Pillar Two implementation?



Latest Developments - BEPS 2.0

PILLAR TWO - US

- ▶ Implemented Book Minimum Tax effective 1.1.2023 - not a Pillar Two compliant tax
- ▶ Status of CbC GILTI?
- ▶ GILTI as a CFC tax vs IIR?

Latest Developments - BEPS 2.0

KEY ISSUES

- ▶ Computational
 - Tax credits
 - Deferred tax - losses, tax depreciation
 - Stock compensation
- ▶ Interaction of regimes
 - Uniformity in implementation
 - US CbC vs Pillar Two
 - Two computations?
- ▶ Compliance and safe harbors
- ▶ Timing

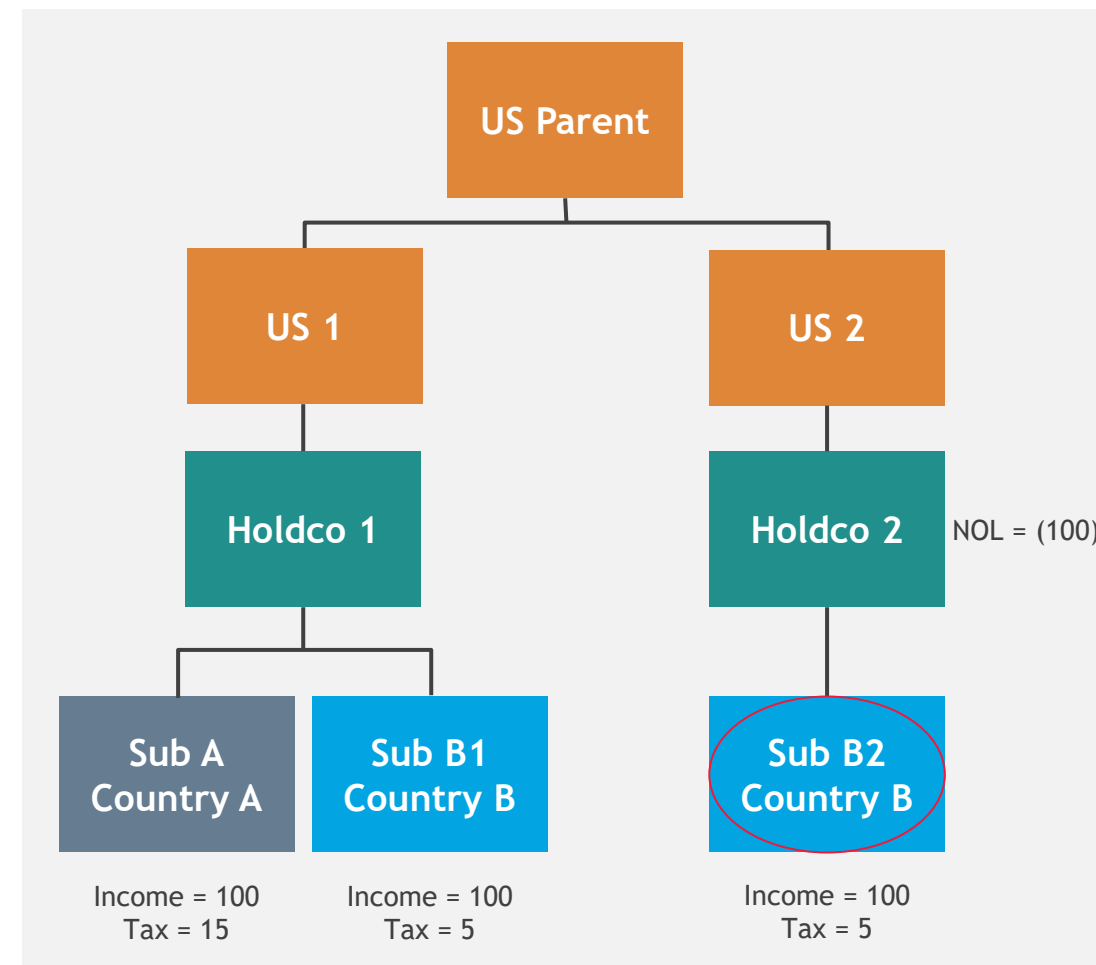


Pillar Two - US interaction

US GILTI - Qualifying CFC Tax

GILTI Calculation*			
	US1	US2	
GILTI Inclusion - NOL	200	-	
\$250 Deduction	(100)	-	
GILTI Taxable Income	100	-	
U.S. Tax on GILTI pre-FTC	21	-	
GILTI FTCs	(16)	-	
GILTI Liability	5	-	
Pillar Two Tax - Potential GILTI Tax Allocation - Based on % of Top-Up Tax			
	Country A	Country B	Total
GloBE Income	100	200	300
Minimum Tax (15%)	15	30	45
Local Covered Tax	15	10	25
Hypothetical GloBE Top-up Tax	-	20	20
% of Total Hypothetical Top-up Tax	0%	100%	100%
Allocation of GILTI Liability	-	5	5
Covered Taxes after GILTI Allocation	15	15	30
Actual GloBE Top-up Tax	-	15	-
Total Tax - \$20			

*Calculation simplified for presentation purposes

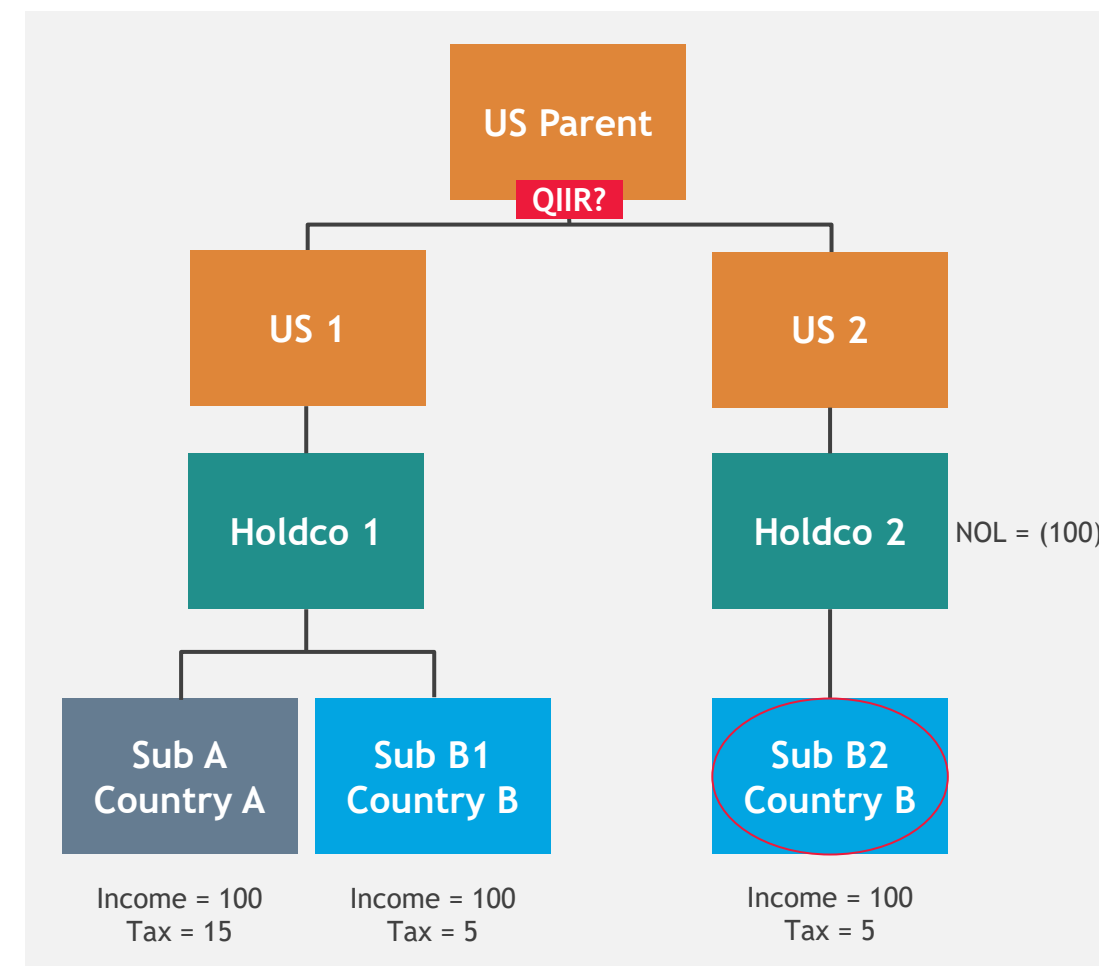


Pillar Two - US interaction

US CbC as a QIIR

CbC GILTI Calculation*			
	Holdco	Country A	Country B
GILTI Inclusion - NOL	-	100	100
\$250 Deduction	-	(27.5)	(27.5)
GILTI Taxable Income	-	72.5	72.5
U.S. Tax on GILTI pre-FTC @ 21%	-	15.23	15.23
GILTI FTCs - 95%	-	(14.25)	(4.75)
GILTI Liability	-	.98	10.48
No Pillar Two Top Up Tax as CbC GILTI respected as QIIR			

Total Tax - \$11.46

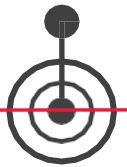


*Calculation simplified for presentation purposes

ACTION

APPROACH

Today



Identify
&
quantify

- In-scope Test
- Modelling & sensitivity analysis (ETR and cash tax)
- Assessment of systems / data

Prepare

- Risk / opportunity assessment
- Planning
- Design & implement systems / process changes
- Readiness Check

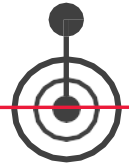
31 December 2023/4?



Report

- Gather data
- Prepare calculations
- Make elections
- Financial statement reporting
- Prepare return
- Make notifications
- File return

First Return



Legal Entity Rationalization and Repatriation Planning



Legal Entity Rationalization

Current landscape

- ▶ Number of Multinational Enterprises with large and complex legal and operating structures built up through acquisitions and organic growth
- ▶ Purpose of structure no longer relevant e.g. historic deferral or repatriation strategies may no longer be relevant given global tax reform

Challenges

Substance

- ▶ Increased local country requirements
- ▶ EU/OECD grey/black list
- ▶ Treaty abuse - increased scrutiny from tax authorities (PPT/LOB)
- ▶ ATAD 3 - Shell Company Directive

Cost

- ▶ Cost of maintaining legal entities increasing -
 - Internal cost - salaries, operational, administrative costs
 - External - audit, tax compliance etc.

Disclosure

- ▶ Country by Country Reporting
- ▶ Mandatory Disclosure Rules
- ▶ ATAD 3 - Shell Company Directive
- ▶ Pillar Two and potential US CbC GILTI

Legal Entity Rationalization

Rationalizing the corporate and operating structure

Legal and capital structure aligned with strategic priorities

Effectively evaluate performance of underlying assets

Align corporate structure with core business functions

Effective circulation of working capital

Considerations

Tax

- ▶ ETR planning
- ▶ Attribute preservation
- ▶ Repatriation strategy
- ▶ Treaty impact
- ▶ Rulings and incentives

Legal

- ▶ Contracts
- ▶ Asset protection
- ▶ Intellectual property
- ▶ Litigation
- ▶ Licenses

Accounting

- ▶ Statutory audits
- ▶ Changes to internal controls and processes
- ▶ Impact to Group consolidated reporting

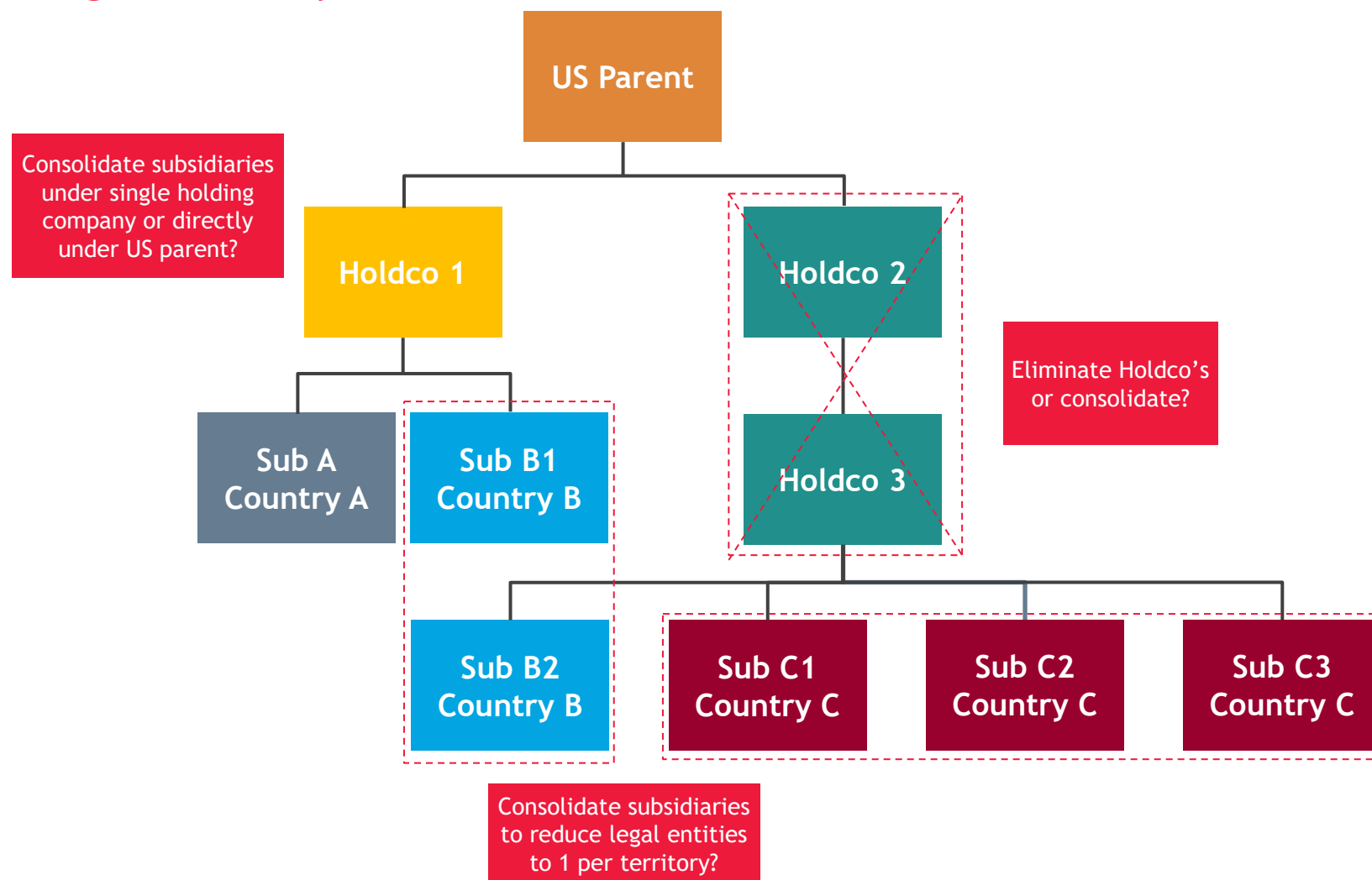
HR

- ▶ Works Council/union requirements and approval
- ▶ Changes to benefits and compensation
- ▶ Payroll

Treasury

- ▶ Impact on debt covenant, guarantees and credit rating
- ▶ Rationalize/unwind existing inter-company balances

Legal Entity Rationalization



Tax considerations

- ▶ Impact on tax attributes
- ▶ Future repatriation mechanisms and impact on dividend withholding tax
- ▶ Impact on US tax profile and US tax cost of restructuring

Non-tax considerations

- ▶ Future divestment or commercial/legal need to keep businesses separate
- ▶ Historic liabilities/claims e.g. pension liabilities
- ▶ HR - Works Council/union requirements and approval

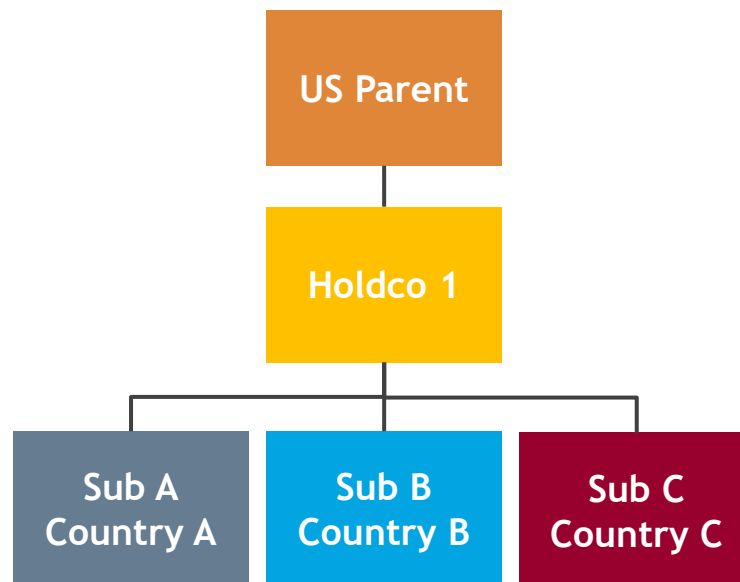
Legal Entity Rationalization - Future State

Legal and capital structure
aligned with strategic
priorities

Effectively evaluate
performance of underlying
assets

Align corporate structure with
core business functions

Effective circulation of
working capital



Outcome

- ▶ Significant reduction in cost - elimination of 5 legal entities
- ▶ Potentially easier working capital and repatriation

Repatriation and Working Capital Management

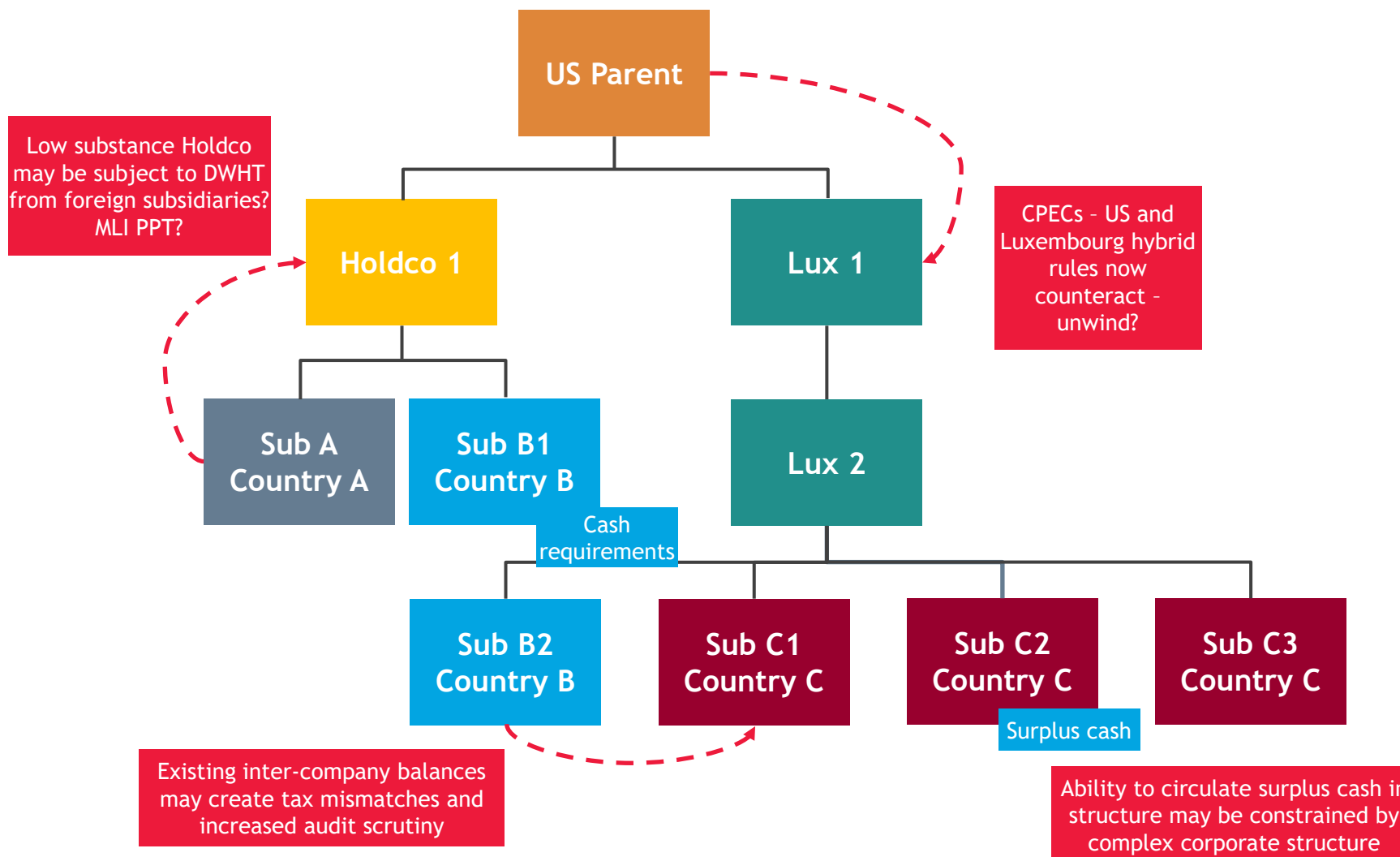
Current landscape - significant pressure on working capital

- ▶ Increased focus on liquidity and access to cash
- ▶ Cost of borrowing increasing
- ▶ Existing structures complex and burdensome for circulation of funds
- ▶ Increased pressure on substance - withholding tax
- ▶ Increased foreign exchange volatility
- ▶ Historic debt structures no longer fit for purpose in a post BEPS environment

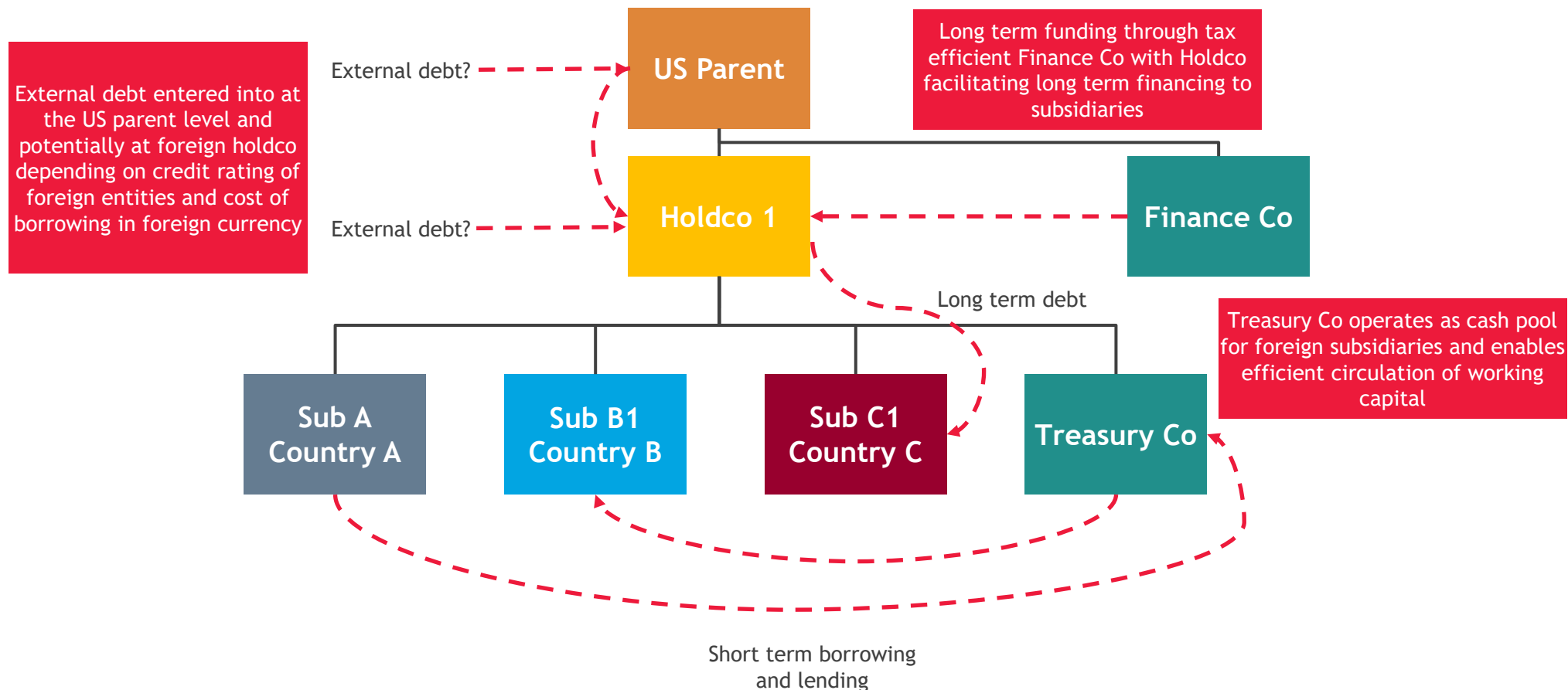
Tax considerations

- ▶ Interest limitations implemented in most jurisdictions - 30% EBITDA limitation
- ▶ Transfer pricing - increased scrutiny by tax authorities, number of tax cases in recent years
- ▶ Hybrid rules enacted in over 34 countries
- ▶ Increased scrutiny on withholding tax - focus on substance and purpose tests
- ▶ Benefit of low/no tax structures reducing - impact of Pillar 2?

Repatriation and Working Capital Management



Repatriation and Working Capital Management - Future State





Key Takeaways

- ▶ Evaluate corporate structure and working capital management to identify opportunities to simplify and reduce cash
- ▶ Engage with wider organization - legal, accounting, HR, IT to identify synergies and cost saving as well as potential pit falls
- ▶ Align corporate and working capital structure with strategic growth plans - future divestment of business lines?

Closing



Questions?



Join the Next Webinar

BDO Tax Strategist: Cross-Border Issues - Year-End Considerations

- ▶ December 14, 2022 - 12pm - 1pm ET
- ▶ Register at bdo.com/events

