



International Provisions to the Tax Cuts and Jobs Act: Issues and Update

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Agenda

- Tax systems
- Participation exemption
- 965 repatriation tax
- GILTI
- BEAT
- Other provisions
- Questions



Tax Systems



Tax Systems

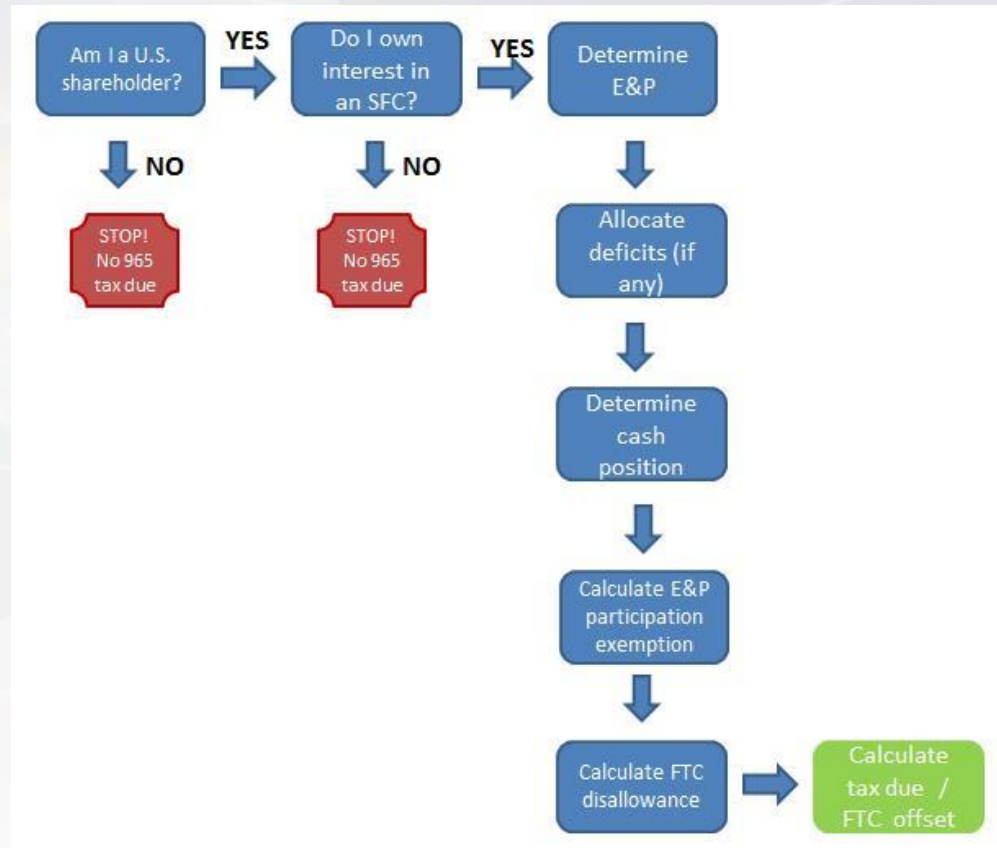
- World-wide taxation system
- Territorial taxation system
- Quasi or hybrid territorial taxation system

965 Repatriation Tax

965 Repatriation Tax

- Transition rule to effect participation exemption accomplished via section **965 mandatory repatriation tax**
- Subpart F income of a SFC for its last taxable year pre 1/1/2018 is increased by > of its accumulated E&P as determined as of 11/2/2017 or 12/31/2017 (“deferred foreign income”)
- U.S. s/h includes their pro rata share of this amount in gross income
- The transition rule includes a participation exemption which is designed to arrive at E&P taxed at reduced rates of 15.5% to extent attributable to cash and 8% non-cash (i.e., 55.7% cash; 77.1% non-cash)
- An SFC is generally a CFC or FC that is at least owned 10% by a U.S. s/h
- Deficits may offset deferred foreign income
- FTCs subject to the participation exemption may also offset amount due
- NOLS may offset amount due or taxpayers may elect out of use of NOL to preserve for future use
- Mazars has templates to compute this amount
- A flow chart detailing the steps by which to compute this amount is also provided in Mazars tax alert
- Notices 2018-7 and 2018-13 have been issued to provide clarifying guidance on computation
- Applicable taxpayers include ALL U.S. s/h and special rules exist for S-corps and REITs.
- Purpose of this rule is to bring back \$\$\$ back on onshore for what hopefully will be US investment

965 Repatriation Tax (Cont'd)



965 Repatriation Tax (Cont'd)

- What are we seeing in practice?
 - State and local tax impact
 - E&P studies
 - Cash vs non-cash analysis
 - Definition of receivables
 - Multiple inclusion years
 - Consolidated groups
 - Use of tax attributes (NOLs)
 - Use of elections
 - Timing of repatriation
 - Cash needs
 - Ordering rule of general subpart F vs. section 965 PTI
 - Section 965 vs. section 956
 - Anti-abuse rules

Participation Exemption

Participation Exemption

- New code section **245A** which allows a domestic corporation that is a U.S. s/h of a specified 10% FC a 100% DRD for the foreign source portion of dividends received from the FC
- Only available to domestic C-corporations that are not REITS or RICS
- Dividends from PFICs do not qualify for the DRD
- Hybrid dividends are also not eligible for the DRD
- Subpart F and GILTI is not eligible for the DRD
- No FTC permitted w/r/t DRD
- Holding period for U.S. s/h w/r/t to the FC (1 year)
- Applies to distributions made post 12/31/2017
- Expected to reduce revenues by approximately \$223.6B over 10 year period



Global Intangible Low Taxed Income (GILTI)

GILTI

- New section **951A** adds new category of subpart F income for global intangible low taxed income or GILTI
- GILTI is a U.S. s/h's excess of all CFC's net tested income over a deemed return on tangible assets (i.e., 10% of its CFC's qualified business asset investment) reduced by certain interest expense
- QBAI is defined as the average adjusted bases in specified tangible property that used in the production of tested income (i.e., tangible assets subject to depreciation)
- Corporate s/hs are allowed a deduction equal to 50% of their GILTI amount (reduced to 37.5% commencing 2026). This results in an ETR on GILTI amounts of 10.5% tax prior to 2026
- Non-corporate s/hs are subject to GILTI at full tax but can make section 962 election to be taxed like c-corporations
- Limited deemed paid credit of 80% of the foreign taxes attributable to tested income is permitted
- Increase revenues by \$112.4B over 10 years

GILTI (Cont'd)

- What are we seeing in practice?
 - CFC status
 - Tested income
 - Expense allocation
 - High tax exception
 - Section 962 election



Base Erosion and Anti-Abuse Tax (BEAT)

BEAT

- Section 59A creates a new base erosion minimum tax
- BEAT equals the excess of 10% of the applicable taxpayer's MTI for the year over taxpayer's regular tax liability reduced by certain credits (low income housing credit, renewable energy production credits, other energy credits and section 38 credits)
- Applicable taxpayer definition is a corporation (not S-corporations, RICs or REITs), w/ \$500M gross receipts over 3 year period average, 3% base erosion percentage
- MTI definition
- Base eroding payment definition (rtd pty rents, royalties, interest, service fees subject to exceptions)
- Related party definition quite broad
- Mazars tax alert published

BEAT (Cont'd)

- What are we seeing in practice?
 - Do you meet the gross receipts test?
 - Do you satisfy the threshold base erosion percentage?
 - Impact of section 163j interest limitation
 - Depreciation / amortization adjustments
 - COGS exception
 - Service cost method exception
 - Add back for subpart F / GILTI amounts
 - Double counting
 - Netting of inbound and outbound payments (e.g., reinsurance premiums netted against ceding commissions or claims)?
 - What constitutes a base eroding payment where US insurco establishes and deducts reserve in Year 1 but pays underlying claim in Year 2?
 - When is BEAT tax due if reinsurance contract is written in Year 1 but premiums are transferred in Year 2?
 - Consideration should be given to the applicability of BEAT to tax sharing agreements
 - Domestic alternatives

Beat Calculation Example 1 – Profitable Year

| | <u>Regular Tax</u> | <u>BEAT Tax</u> |
|------------------------------------|--------------------|-----------------|
| Gross Income | 1,100 | |
| Deductions: | | |
| Non-BEAT | <950> | |
| BEAT (regular tax regime) | <u><50></u> | |
| Taxable Income / <Loss> before NOL | 100 | |
| Net Operating Loss Carry Forward | <u>-</u> | |
| Taxable Income / <Loss> | 100 | 100 |
| BEAT Deductions (BEAT tax regime) | | 50 |
| NOL x Base Erosion Percentage | | <u>-</u> |
| Modified Taxable Income | | 150 |
| Tax Rate | <u>21%</u> | <u>10%</u> |
| Tax | 21 | 15 |

Note: In profitable years, BEAT tax is a function of how BEAT deductions compare to regular taxable income (and amount of credits offsetting regular tax). In this example, BEAT deductions were not large enough in relation to regular taxable income to generate a BEAT tax.

Beat Calculation Example 1 – Loss Year

| | <u>Regular Tax</u> | <u>BEAT Tax</u> |
|-----------------------------------|--------------------|-----------------|
| Gross Income | 975 | |
| Deductions: | | |
| Non-BEAT | <950> | |
| BEAT (regular tax regime) | <u><50></u> | |
| Taxable Income/ <Loss> before NOL | <25> | |
| Net Operating Loss Carry Forward | <u>-</u> | |
| Taxable Income/ <Loss> | <25> | <25> |
| BEAT Deductions (BEAT tax regime) | | 50 |
| NOL x Base Erosion Percentage | | - |
| Modified Taxable Income | | 25 |
| Tax Rate | <u>21%</u> | <u>10%</u> |
| Tax | - | 2.5 |

Note: In loss years, BEAT tax is a function of how BEAT deductions compare to current year regular taxable loss. In this example, BEAT deductions exceed current year regular taxable loss so BEAT is generated.

Other Provisions

Other Provisions

- Repeal section **954(g)** which means no longer U.S. tax on foreign oil-related income of a foreign subsidiary
- Repeal section **955** which means no longer U.S. tax on previously excluded foreign shipping income of a foreign subsidiary if there was a net decrease in qualified shipping investments
- Elimination of constructive ownership rule under section **958(b)(4)** which prevented downward attribution of stock owned by a foreign person to a U.S. person. So, now, stock owned by a FC would be treated as constructively owned by its wholly owned domestic subsidiary for purpose of determining the U.S. s/h status of the subsidiary and the CFC status of the FC
- Revision of definition of U.S. s/h under section **951(b)** to include 10% vote and **value**
- Elimination of requirement of CFC status for 30 day period under section **951(a)** for purposes of a U.S. s/h's subpart F inclusion

Other Provisions (Cont'd)

- Amendment to definition of intangible property for purposes of section **936(h)(3)(B)** to include of WIP, GW, GCV and any other item the value of which is not attributable to tangible property or services of an individual
- Denial of deductions for interest and royalty payments to related parties under **hybrid arrangements** that give rise to stateless income
- Modification of the insurance exception to the PFIC rules. Active t or b exception now only applies to a FC whose applicable insurance liabilities constitute > 25% of its total assets as reported on the financial statements
- Special rules for **inverted entities**
- Repeal of section 902 credit



Questions?



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