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U.S. Tax Reform

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Key Considerations for Tax Reform

- 35% corporate tax rate was among world's highest
- Reduced global competitiveness
- Corporate inversions
- Transfer of intangible assets to low-tax foreign jurisdictions
- $2.6 million of profits parked in foreign subsidiaries
- High use of base erosion payments
- Stagnate wage growth

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Domestic Individual Provisions

- Top individual rate reduced - 39.6% to 37%
- Standard deduction doubled to $12,000/$24,000
- Mortgage interest deduction limited to $750,000
- Limit deduction for state & local tax, and property tax to $10,000
- Potential tax at maximum individual pre-tax reform rates on deemed repatriation of CFC earnings

Domestic Business Provisions

- 40% reduction in corporate rate
- Immediate and total expensing of capital expenditures
- NOLs limited to 80% of taxable income
- 20% deduction for qualified income of pass through businesses
- Limitation on interest deduction– 30% of EBITDA

Cross Border Business Provisions

- Quasi-territorial tax system
- Taxation of $2.6 trillion of foreign earnings
- Exemption for certain foreign income
- Effective rate of 10.5% on CFC intangible income (GILTI)
- Effective rate of 13.125% on domestic corporation's foreign derived intangible income (FDII)

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Cross Border Business Provisions

- CFC anti-deferral rules largely left intact
- New Base Erosion and Anti-Abuse (BEAT) tax
- Foreign person's sale of U.S. partnership with active trade or business taxed as ordinary income
- Change in CFC attribution rules expose certain foreign based companies to U.S. CFC reporting

Domestic Business Provisions

Most provisions effective as of January 1, 2018

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Corporate Rate Reduction

- Prior law - graduated rates, maximum of 35%
- New law - flat rate of 21%
  - Below the individual capital gains rate - 23.8%
  - Below the worldwide average corporate rate of 22.96%
- Reduced rate + full expensing of plant and equipment = more foreign investment

Full Expensing

Section 179 Expensing of Depreciable Business Assets

- Immediate expensing of plant and equipment up to $1 million
- Applies to both new and used property
- Reduced after property placed in service during year exceeds $2.5 million

Full Expensing

Bonus Depreciation under Section 168(k)

- Increased from 50% to 100% for property placed in service through 2023
- Useful for very large businesses that exceed Section 179 limit

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NOLs

- Limits NOL deduction to 80% of taxable income
- No carryback, unlimited carryforward
- No impact on pre-existing NOLs (including for 2017) 2-year carryback, 20-year carryforward, 100% offset

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20% Deduction on Pass Through Income

- Maximum effective rate of 29.6% for qualifying trade or business income of pass through entities
- Excludes foreign income and investment income

20% Deduction on Pass Through Income

- Threshold amounts for full deduction:
  - $157,500 single
  - $315,000 married
- Professional services phased out above threshold amounts
- Others subject to limitation based either on wages paid or wages paid plus a capital element

Limitation on Business Interest Expense

- Net interest expense deduction limited to the sum of (1) business interest income, plus 30% of EBITDA
- Exemption for corporations and pass throughs with gross income below $15 million
- In 2022, interest will be limited 30% of EBIT (i.e., after depreciation & amortization)
- Impacts businesses with significant debt levels
- Reduces the incentive to borrow

Cross Border Provisions

Most provisions effective as of January 1, 2018

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Quasi – Territorial System

- Available to U.S. corporations only
- Applies to income related to CFC depreciable business assets
- Not available for subpart F or deemed intangible income
- Applied via a 100% dividend received deduction
- Not applicable to hybrid dividends
- No foreign tax credit

Mandatory Repatriation

- Applies to $2.6 trillion held by foreign subs
- 15.5% for cash and 8% for non-cash earnings
- Regulations to be issued
- May elect to pay tax over 8 years
- Requires current verification of accuracy of foreign earnings and related tax pools
- Based upon the greater of E&P measured at November 2, 2017 or December 31, 2017

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Global Intangible Low-Taxed Income (GILTI)

- GILTI = residual income of a CFC in excess of a fixed 10% return on tangible assets
- Immediately includible in U.S. shareholder's gross income
- U.S. corporations - effective rate of 10.5% tax after applying a 50% deduction; may be offset by up to 80% of FTCs
- Individuals subject to maximum rate of 37% on GILTI
- Partial relief - 962 election to be taxed as a corporation
- Complicated formula - not based on actual CFC intangible assets

GILTI

GILTI Category	Category	CFC Income Description	U.S. Tax Rate	Foreign Tax Credit
Non Tested Income	Category 1	GILTI Exclusions: Subpart F, 956, ECI, foreign oil/gas, related dividends, certain subpart F amounts taxed in excess of 18.9%	21%	100% limited to current year taxes paid
Net CFC Tested Income	Category 2	Deemed Tangible Income: 10% return on tangible assets	Exempt	N/A
	Category 3	Deemed GILTI (residual amount in excess of bucket two amount)	10.5% until 2028, then 13.125%	80% in separate FTC basket with no carryback or carryover of excess taxes

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FDII

- Foreign-derived intangible income (FDII) is income that U.S. corporation derives in connection with:

1. selling, leasing or licensing property to non-U.S. persons for foreign use, or
2. services provided to any non-U.S. person

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FDII

- Formulaic calculations divide domestic company income in two tax categories:
  1. Deemed Tangible Income Return taxed at 21% and
  2. FDII taxed at 13.125%
- FDII tax rate is only available to corporations

FDII

- Policy intent - incentivize U.S. companies to exploit intangible assets from U.S. rather than transferring abroad
- Retaining productive intangibles in U.S. should generally permit a domestic company to generate a greater amount of residual income eligible for the reduced FDII rate
- U.S. exporters with low amounts of fixed assets should be able to generate higher amounts of FDII, regardless of balance sheet intangible assets

Foreign Tax Credits (FTC)

- Repeal of corporate indirect FTC on distributions from foreign subsidiaries
- Separate FTC limitation basket for foreign branch income
- Separate FTC basket for GILTI
- FTC available for taxable portion of the mandatory inclusion, but reduced to account for lower tax rates on such inclusions
- CFC intangible (GILTI) inclusions are eligible for FTC on 80% of foreign tax paid
- Allowable FTC based on current-year taxes attributable to subpart F income rather than prior “pooling” approach

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Base Erosion Anti-Abuse Tax (BEAT)

- Effectively applies a 10% minimum tax for taxable income adjusted for base erosion payments
- Targets large multinational corporations making large deductible payments to foreign related parties
- The tax only affects businesses where U.S. gross receipts are in excess of $500m (aggregated on a global group basis) and so has limited application for multinational groups without a significant U.S. presence
- Base erosion payments = deductible amounts paid or accrued by to a foreign related party or paid or in relation to acquisition of depreciable or property
- Includes royalties, interest, and also service fees made at arm's length; cost of goods sold is generally excluded

Sale of Partnership by Non-Resident

- Gain or loss on the sale, exchange or disposition of a partnership interest is treated as effectively connected with a U.S. trade or business to the extent a foreign partner would have had effectively connected gain or loss if the partnership sold all its assets at fair market value on the date of such transaction
- The transferee of the partnership interest must withhold 10% of the amount realized on the transaction (unless the transferor certifies it is not a foreign person)
- If the transferee fails to withhold, the partnership is required to withhold from distributions to the transferee partner

Change in CFC Attribution

Repeal of Section 958(b)(4)

- Foreign subsidiary that is more than 50% owned (by vote and value) by a foreign parent would be treated as a CFC if the foreign parent corporation also owns more than 50% of the value of the stock of a domestic subsidiary
- Per Section 318(a)(3)(C) constructive ownership rules, the domestic subsidiary of the foreign parent would be treated as constructively owning more than 50% of the foreign subsidiary (through attribution from the foreign parent)

Thank You!

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