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M&A Tax, International Tax & Tax Accounting Update

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HIGHLIGHTS

Congress Enacts Extenders Legislation Affecting 2015 and Beyond

Following the recent trend, Congress waited until the end of the year to extend, retroactively, a host of tax breaks benefiting individuals, business entities and tax-exempt organizations (the so-called "extenders"). This year, however, the legislation covered more than just the current year. On December 18, 2015, President Obama signed into law an omnibus spending package that included the House-passed Protecting Americans from Tax Hikes (PATH) Act of 2015. The PATH Act extends 52 provisions of the Code at least through December 31, 2016. The majority of extenders were made permanent. Even with a handful of revenue provisions in the legislation, the tax package was scored as costing $622 billion over ten years.

Research Credit

The most expensive of the extenders is the section 41 research credit, which was made permanent. Many had argued that the prior impermanence of the research credit made it difficult for companies to count on in planning and budgeting research projects and that most other western countries offered a permanent tax subsidy for R&D spending. The PATH Act also increased the tax benefits of the research credit for some small businesses by allowing the research credit to be used as an offset against AMT and, in more limited cases, against the employers' portion of payroll taxes.

International Extenders

The PATH Act also extended section 954(c)(6) through the end of 2019 and made permanent the active financing exception to subpart F. In general, section 954(c)(6) permits CFCs to treat dividends, interest, rents, and royalties received from related CFCs as not resulting in subpart F income to the extent the income of the related CFC is neither subpart F income nor income treated as effectively connected with the conduct of a trade or business in the U.S. The active financing exception permits eligible CFCs predominantly engaged in the active conduct of banking, financing, and similar businesses to exclude certain banking and financing income from subpart F income. While corporations have engaged in extensive planning using both of these subpart F exceptions for years, the length of these current extensions should alleviate doubt about whether such planning is worthwhile from a long-term perspective. Corporations should consider re-evaluating their offshore IP, supply chain, and other structures in light of this welcome development.

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Bonus Depreciation

Congress also extended the availability of bonus depreciation, but mitigated the cost of doing so by limiting extension to five years and phasing down the bonus depreciation percentage, from 50 percent for property placed in service in 2015, to 40 percent for 2016 and 2017 and to 30 percent for 2018 and 2019. The new statutory provision continues to allow taxpayers to elect to accelerate the use of AMT credits in lieu of taking bonus depreciation. The category of property eligible for bonus depreciation has been expanded to cover a broader class of improvements to the interior of nonresidential real property. For example, the taxpayer is no longer required to be a lessor of such property.

Other Extenders

Other extenders affecting business entities include:

- Permanent extension of 15-year straight-line cost recovery for qualified leasehold improvements, qualified restaurant buildings and improvements, and qualified retail improvements.
- Extension through 2016 of the eligibility of domestic gross receipts from Puerto Rico for the section 199 domestic production deduction.
- Extension through 2016 of the railroad track maintenance credit.
- Permanent extension of the provision reducing to five years (from ten years) the period for which an S corporation must hold its assets following conversion from a C corporation to avoid the built-in gains tax.

New REIT Rules

The PATH Act includes a number of provisions modifying the rules applicable to REITs. One such provision puts an end to "opco-propco" transactions in which a corporation spins off real estate into a newly formed REIT. Corporations that are either the distributing or controlled corporation in a spin-off are now prohibited from electing to become a REIT for ten years following the spin-off.

Proposed Regulations Implement Country-by-Country Reporting

As reported in our November update, the OECD released the final report for Action 13 ("Guidance on Transfer Pricing Documentation and Country-by-Country Reporting") under the BEPS project. On December 21, 2015, Treasury and IRS released proposed regulations that, once finalized, will implement country-by-country ("CbC") reporting for certain U.S. multinational groups ("U.S. MNE groups"). Comments to the proposed regulations must be received by March 22, 2016.

Prop. Treas. Reg. § 1.6038-4 incorporates the CbC reporting template proposed in the BEPS report and requires U.S. parent entities of U.S. MNE groups with at least $850 million in consolidated annual revenues to file a CbC report with the parent's U.S. income tax return. The CbC template includes information about the jurisdiction and main business activity of each group entity, as well as each entity's revenues (separately reporting related-party revenues), pretax profit, income taxes paid and accrued, accumulated earnings, number of employees, and the net book value of tangible assets other than cash or cash equivalents.

The preamble to the proposed regulations addresses confidentiality concerns, emphasizing that information contained in a CbC report is "return information," subject to section 6103 confidentiality rules. The preamble indicates that the competent authorities of the United States and other tax jurisdictions intend to further limit the permissible uses of CbC reports to "assessing high-level transfer pricing and other tax risks" and for "economic and statistical analysis." The preamble also proposes an exemption from CbC reporting on national security grounds.

The idea of CbC reporting has already created controversy. In letters to Treasury Secretary Lew, Senate Finance Committee Chair Hatch and House Speaker Ryan both questioned Treasury's authority to implement CbC reporting under existing statutes. Chairman Hatch has also asked the Government Accountability Office to undertake an in-depth analysis of recommendations made in the various BEPS reports, including CbC reporting.

As proposed, the new regulations will take effect in the first tax year beginning on or after the date the regulations are finalized. Thus for calendar year taxpayers, the earliest reporting period under the new regulations will be 2017. U.S. MNE groups should note, however, that foreign members of the group may need to comply with CbC reporting requirements in other jurisdictions that become effective before final U.S. regulations are published.

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Ivins Alumni in the News

Congratulations to former Ivins partner, and current Treasury Deputy Assistant Secretary (International Tax Affairs), Bob Stack on being named Tax Notes' Tax Person of the Year for 2015 for his role in representing U.S. interests as an OECD delegate and shaping the OECD's BEPS reports.