

# U.S. – U.K. TAX PLANNING: COPING WITH UNCERTAINTY

---

IMPLEMENTING B.E.P.S. UNDER U.S. TAX LAWS  
AND OTHER PROVISIONS

**Stanley C. Ruchelman**  
**Fanny Karaman**

**Ruchelman P.L.L.C.**  
New York, NY

# Introduction

---

- B.E.P.S. is the O.E.C.D. project to deter tax base erosion and profit shifting from high tax jurisdictions to low tax jurisdictions
- In October 2015, the B.E.P.S. project culminated in 15 reports designed to achieve three broad objectives
  - Coherence in the application of tax law
    - The goal being the avoidance of double non-taxation
  - Substance in structures
    - The goal is to prevent name plate companies in low tax jurisdictions from being allocated most of the profits
  - Transparency
    - All cards are played face up on the table

# Introduction

---

- The U.S. has adopted several B.E.P.S. recommendations
  - Limit on Deduction of Interest Expenses and the Fight Against Base Erosion
  - G.I.L.T.I. and the Fight Against Innovation Box Regimes
  - Hybrid Payments and the Fight Against Double Nontaxation
  - CbC Reporting and Beneficial Ownership Transparency

# Limit on Deduction of Interest Expense

---

The Fight Against Base Erosion

# Limit on Deduction for Business Interest Expense

---

- Prior Law (Prior Code §163(j))
  - “Earnings Stripping” rule for interest paid to related parties or to lenders under loans guaranteed by related parties
  - Cap on related party net interest deduction imposed for “disqualified interest” payments
  - Payor Corporations Subject to cap if:
    - Payor’s debt-to-equity ratio > 1.5 : 1.0
    - Payor’s net interest expense > 50% of essentially E.B.I.T.D.A.
  - “Disqualified Interest” summarized:
    - Interest paid or accrued to related parties outside the U.S. that were not subject to full WHT
    - Interest paid or accrued to unrelated parties when the obligations was guaranteed or supported by a related party

# Limit on Deduction for Business Interest Expense

---

- T.J.C.A. (Amended Code §163(j))
  - Broader in scope than prior law
    - Not limited to related interest paid to related parties
    - Prevents deductions for interest expense deemed to be excessive
    - Moves away from debt : equity ratio
    - Relies on E.B.I.T.D.A. cap initially and then to an E.B.I.T. cap in 3 years
  - Exceptions:
    - Average annual gross receipts not in excess of \$25 Million over the last 3 years
    - Individuals in the trade or business of performing services as an employee
    - Real property trade or business electing out of the rule
    - A farming business electing out of rule
    - Certain public utilities that furnish or sell (i) electrical energy, water, or sewage disposal services, (ii) gas or steam through a local distribution system, or (iii) transportation of gas or steam by pipeline

# Limit on Deduction for Business Interest Expense

---

- T.J.C.A. (Amended Code §163(j))
- Limitation is the sum of:
  - Business interest income
  - 30% of adjusted taxable income
  - Floor plan financing interest on loans used to finance motor vehicle inventory for a dealer
- Unlimited carryforward with restrictions for partnerships

# Limit on Deduction for Business Interest Expense

---

- T.J.C.A. (Amended Code §163(j))
  - Business interest income:
    - Interest includible in taxpayer's gross income properly allocable to a trade or business
    - Interest paid or accrued on indebtedness allocable to property held for investment is not covered
  - Specific rules apply to partnerships to avoid double dipping by partners
    - Limitation is computed at partnership level
    - Adjusted taxable income of partner does not include distributive share of non-separately stated partnership income
    - Excess limitation at partnership level is allocated among partners



G.I.L.T.I.

---

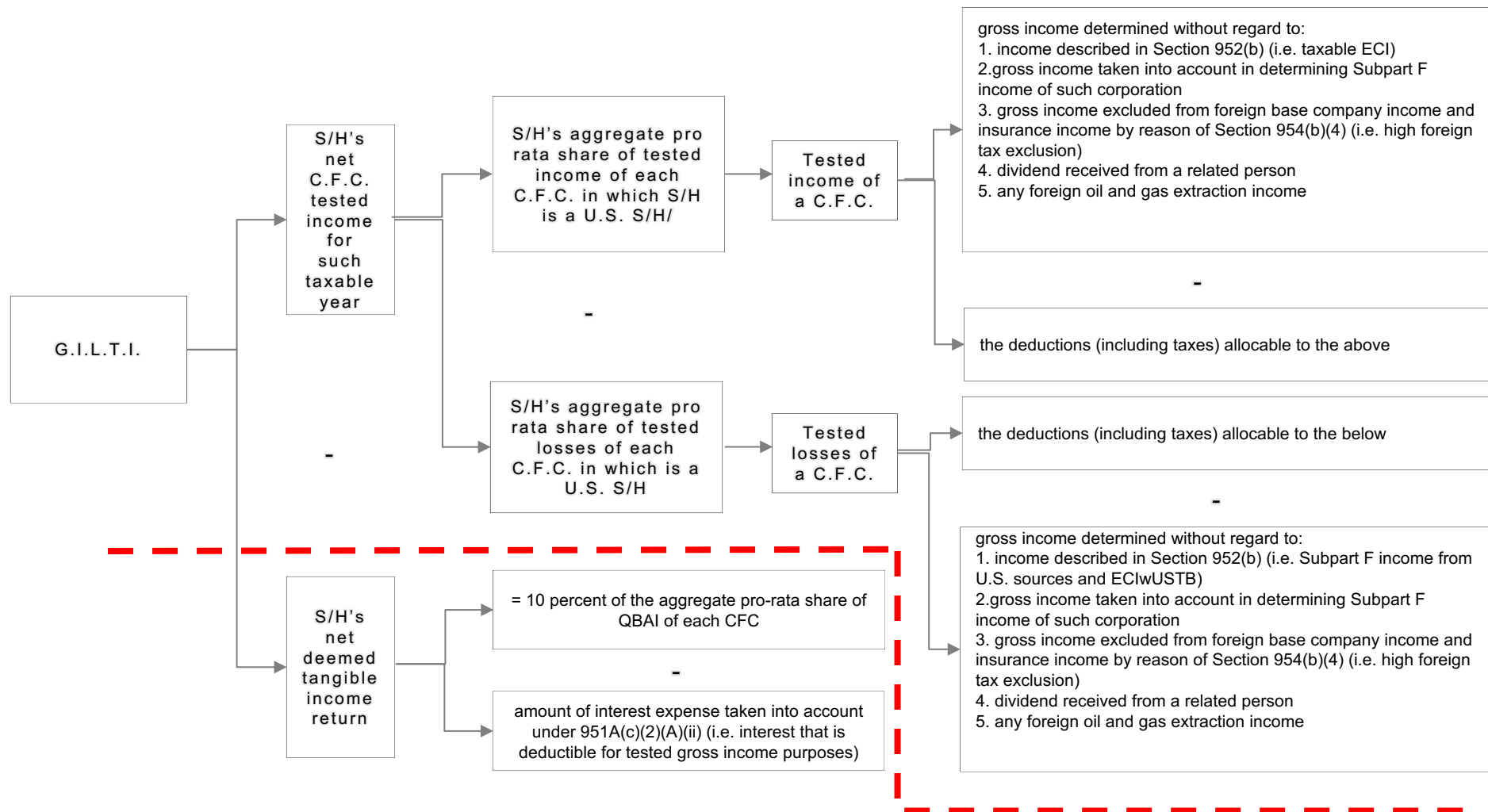
The Fight Against Innovation Box Regimes

# G.I.L.T.I.

---

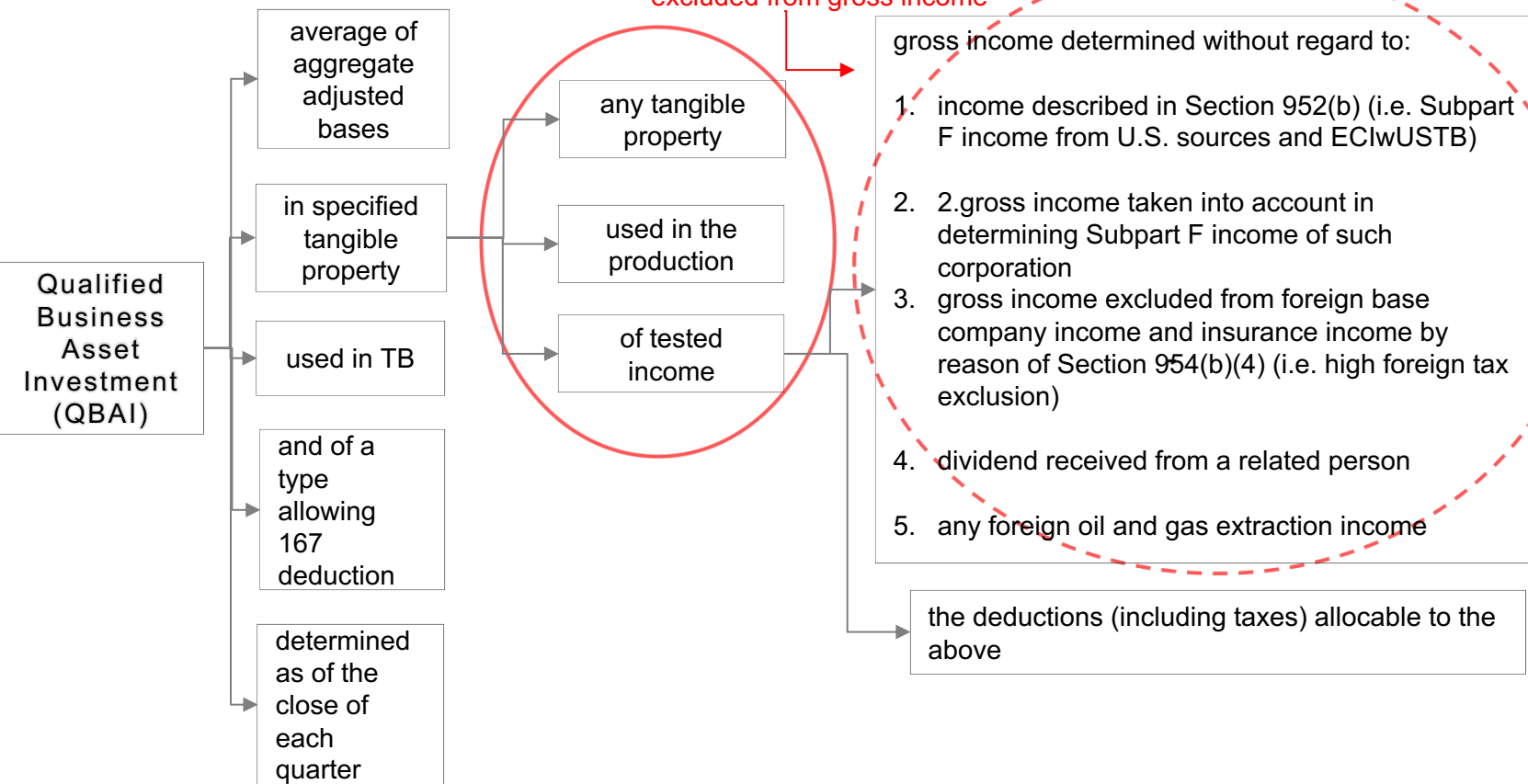
- Code §951A
- G.I.L.T.I. = Global Intangible Low-Taxed Income
- Affected Taxpayers :
  - U.S. shareholders of C.F.C.'s
  - “U.S. Shareholder” now determined by 10% of vote or value
- Consequence to U.S. Shareholders:
  - Individual and Corporate U.S. shareholders: G.I.L.T.I. inclusion in taxable income
  - In general, only corporate shareholders are entitled to a deduction (Code §250(a)(1))
  - Special treatment for individuals making a Code §962 election

## G.I.L.T.I.



## G.I.L.T.I.

Essentially, property, plant and equipment not giving rise these items excluded from gross income



# Hybrid Payments

---

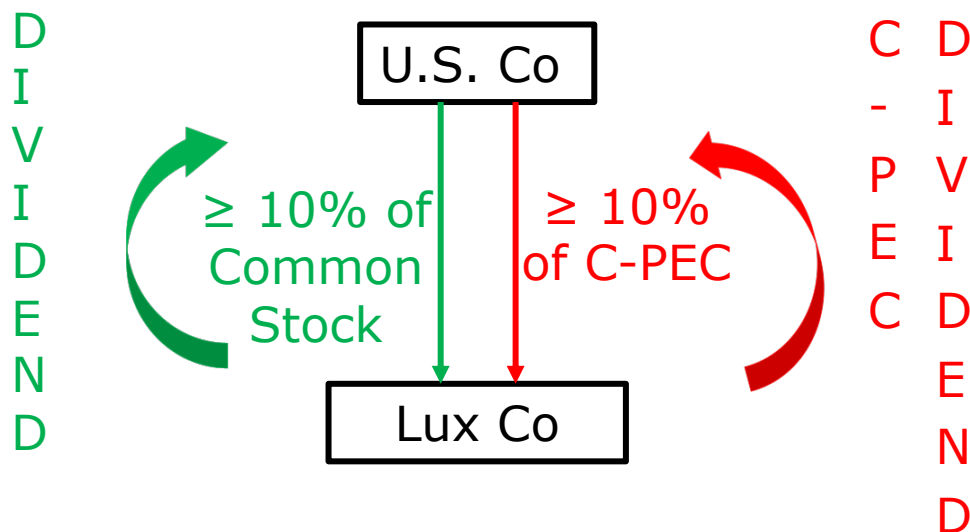
The Fight Against Double Nontaxation

# Hybrid Payments

---

- Code § 245A – D.R.D. allowed for dividend payments received by U.S. corporation from a  $\geq 10\%$  owned foreign corporation
  - A dividend from a foreign corporation benefits from D.R.D. when:
    - Received from a  $\geq 10$ -percent owned foreign corporation
    - By a domestic corporation
    - That is a “United States shareholder” in the foreign corporation
    - But only for the foreign-source portion of such dividend
    - And only if the payor does not deduct the dividend paid
    - And only if the payor is not a P.F.I.C.
  - Deemed paid credit eliminated
  - Post 1986 pool of E&P is eliminated by the Code §965 inclusion
  - No foreign tax credit allowed for withholding tax

# Hybrid Payments



- Receipt of dividend on common stock
  - Not Deductible for payor in Luxembourg
  - Dividend is deductible under Code §245A

- Receipt of C-PEC distribution
  - Deductible for payor in Luxembourg
  - Not deductible under Code §245A(e)

# Hybrid Payments

---

- Code §267A – deduction disallowed for certain hybrid payments made from U.S.
  - Disallows deduction for Disqualified Related Party Amount
    - Paid or Accrued pursuant to a hybrid transaction, or
    - Paid or accrued by, or to, a hybrid entity
  - “Disqualified Related Party Amount”:
    - Interest or royalty paid or accrued to a related party if
      - Not included in income of related party, or
      - Related party can deduct amount
    - Exception: subpart F inclusion in the hands of a U.S. shareholder under Code §951(a)



# Hybrid Payments

---

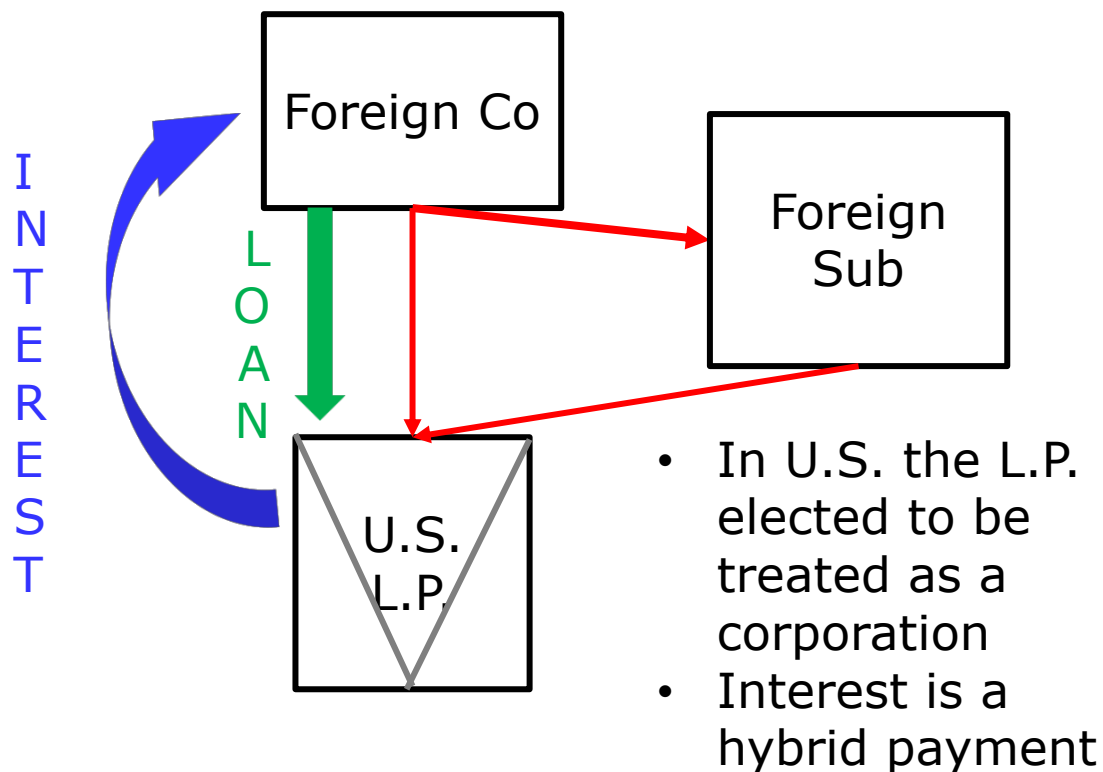
- Code §267A
  - “Related Party”:
    - An individual, corporation, trust, or estate which controls, or is controlled by, the payor or
    - A corporation, partnership, trust, or estate which is controlled by the same person/persons which control the payor
  - “Control”:
    - Corporation: Direct or indirect ownership of more than 50% (vote or value)
    - Partnership, trust, estate: Direct or indirect ownership of more than 50% by value of beneficial interest therein
  - Code §958 attribution rules apply

# Hybrid Payments

---

- Code §267A
  - Hybrid Transaction:
    - Payment of interest or royalty from a U.S. person, but the receipt of payment is not taxable in foreign country or the recipient is entitled to a deduction
  - Hybrid entity:
    - Treated as fiscally transparent in the U.S. but not for purposes of foreign country, or
    - Treated as fiscally transparent in foreign country but not in the U.S.
    - Proposed Regs to be issued by year end with final Regs. by June 2019

## Hybrid Payments



- Foreign Co and Foreign Sub formed in Country C
- In Country A, U.S.L.P. is treated as a partnership
- Under Country C tax law, partners cannot do business with themselves
- Transactions between partners and partnership are eliminated
- In U.S. the L.P. elected to be treated as a corporation
- Interest is a hybrid payment

# CbC Reporting

---

Beneficial Ownership Transparency

# CbC Reporting

---

- O.E.C.D.'s BEPS Action 13 Report (Transfer Pricing Documentation and Country-by-Country Reporting)
- Treas. Reg. §1.6038-4
- Applies to ultimate U.S. parent entity of a multinational enterprise group that has annual revenue in preceding accounting period of  $\geq$ \$850 Million
- Must file Form 8975 (Country-by-Country Report)









# CbC Reporting

---

- Two tables of data to report
  1. Report by jurisdiction
    - Revenue
    - Profit, accumulated earnings
    - Tax paid and accrued
    - Stated capital, tangible assets (other than cash)
    - Employee count
  2. Report by entity by jurisdiction
    - Jurisdiction of organization, tax jurisdiction of residence
    - Main business activities (12 categories plus 'Other')

# CbC Reporting

---

- The goals
  - Promote consistency of reporting obligations across tax jurisdictions
  - Reduce the risk that other countries will depart from the agreed standard
  - Achieve a balance of benefits to tax administrations and the compliance costs and burdens for MNE groups
  - The reported information may be used only for assessing high-level transfer pricing and other tax risks and, where appropriate, for economic and statistical analysis

# CbC Reporting

---

- Exchange of information
  - Reports may be exchanged with tax authorities in other countries pursuant to bilateral agreement
  - The parent company of the MNE group prepares the CbC report and files it with the tax authority of its home jurisdiction
  - CbC reports prepared by non-U.S. based MNE groups will be furnished to the I.R.S.
  - I.R.S. expects that the reports will enable it to perform high-level transfer pricing risk identification and assessment of issues
  - This is consistent with recently announced audit plan guidelines applicable to the examination of an MNE

# CbC Reporting

---

- Countries approved for CbC exchanges of information\*

Australia	Belgium	Bermuda	Brazil	Canada
Colombia	Croatia	Czech Rep.	Denmark	Estonia
Finland	France	Germany	Greece	Guernsey
Hungary	Iceland	India	Ireland	Isle of Man
Israel	Italy	Jamaica	Jersey	Latvia
Liechtenstein	Lithuania	Luxembourg	Malta	Mauritius
Mexico	Netherlands	New Zealand	Norway	Poland
Portugal	Rep. of Korea	Slovakia	Slovenia	South Africa
Spain	Sweden	U.K.		

\* As of February 7, 2018.

# Important Notice

This presentation is not intended to be legal advice. Reading these materials does not create an attorney-client relationship. The outcome of each case stands on its own merits.