Recent Corporate Tax Developments
Tax Reform and Troubled Corporations
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NOL Changes
New NOL Rules

• Net operating losses (NOLs) arising in tax years *ending after* 12/31/2017
  – Indefinite carryforward and no carrybacks
  – No more CERT rules or Specified Liability losses for the new NOLs
  – Old rules apply to NOLs from before 12/31/2017

• NOLs *beginning after* 12/31/2017
  – Deduction is limited to 80% of taxable income for which the NOL is carried to
  – Exceptions

• Legislative history

• No changes to capital loss carryforward and carryback rules
  – Carryback 2 years and carryforward 5 years
  – Only capital gains can offset capital losses
NOL Ordering

• 172(a) – NOL deduction for the taxable year an amount equal to the lesser of:
  – the aggregate of the net operating loss carryovers to such year, plus the net operating loss carrybacks to such year, or
  – 80 percent of taxable income computed without regard to the deduction allowable under this section

• Example
  – Calendar year LossCo has $90 million in NOLs generated through December 31, 2017 and incurs a $50 million NOL in the tax year ending Dec. 31, 2018
  – LossCo generates $100 million in taxable income in 2019
  – Result?
    ▪ The entire $90M of 2017 and prior NOL would be available to offset 2019 taxable income.
    ▪ Can LossCo offset the remaining $10M with the 2018 NOL? If so, how much?
Select Section 382 Issues
Rules for the Carryforward of Disallowed RBILs

- Section 382(h)(4) says that disallowed RBILs are carried forward to subsequent taxable years under rules similar to the carryforward of NOLs and are subject to limitation in the same manner as a pre-change loss.

**Question:** For disallowed RBILs that are recognized after the effective date of TCJA, but which relate to ownership changes which occurred before the effective date of the TCJA, are those RBILs carried forward for 20 years or indefinitely?

Are the RBILs limited to offsetting 80% of taxable income?
RBIG and the Transition Tax

• The “Transition Tax” rule (Section 965) provides for a mandatory subpart F income inclusion of the accumulated post-1986 earnings of the specified foreign corporation.
  – Rate is 15.5% on cash and cash-equivalent assets and 8% on non-cash assets.
  – Rate is achieved by allowing a deduction to offset the inclusion so that inclusions are at the rates indicated above.

Questions:

• Is the subpart F inclusion RBIG?
• Does the deduction impact the amount of RBIG?
RBIG and Amended Section 168(k)

• Section 168(k) was amended to temporarily allow 100% expensing on Qualified Property.
  – No original use requirement.
  – Does not apply to intangibles.

Questions:

• How will this temporary expensing rule be taken into account for purposes of calculating RBIG?

• Example: Lossco has a single asset with a basis of $100 and a value of $200. Assume the asset has 10 years of depreciation left at $10 per year. If Lossco adopts the section 338 approach permitted by Notice 2003-65, how much RBIG does Lossco have in the first year of the recognition period?
Amended Section 163(j)
Amended Section 163(j)

• Repealed prior section 163(j) limitations on the deductibility of a corporation’s interest expense paid to a related person that is not subject to tax (e.g., a foreign person).

• Section 163(j) was amended to generally provide that the deduction for net business interest (business interest expense reduced by business interest income) would not exceed 30% of adjusted taxable income. Amount in excess of this limit carries forward indefinitely.

• Section 163(j) carryforward treated as a section 381 attribute and treated as a pre-change loss for section 382 purposes.
Amended Section 163(j) Continued

**Questions:**

- What happens to historic 163(j) carryforwards? Are they treated as a pre-change loss?
- Are 163(j) carryforwards subject to attribute reduction under section 108?
- Timing of E&P reduction for interest in excess of the allowed amount?
  - Consider significance of proposed regs. related to historic section 163(j).
Corporate AMT Repeal
Corporate AMT Repeal


Creates an AMT Refundable Credit Amount (RCA) equal to 50% (in years 2018 - 2020) and 100% in 2021 of the excess of the MTC over the MTC allowed in such year (before the application of this section).
Corporate AMT Repeal


X has an ownership change on January 1, 2018 and an annual section 383 limitation on its credits of $10.

X has regular tax liability in 2018 of $45 (before taking use of credits into account).
Corporate AMT Credit

Step 1 - Determine MTC for year (Section 53(b))

MTC Prior Years 100
MTC Used in Prior Years 0

100
Corporate AMT Credit

Step 2 - Determine RCA (Section 53(e))

MTC | 100
MTC Allowed in current year* | -10
Sum | 90

X 50% (2018, 2019, 2020) or 100% (2021) x 50%

RCA | 45

Does MTC Allowed take into account only limitation in Steps 3 or all limitations (such as section 383)?
Corporate AMT Repeal

Step 3 - Compute MTC Limitation - (Section 53(c))

Regular Tax Liability (without use of MTC) 45
- [Old less Tentative Minimum Tax] 0
+ RCA 45

Section 53(c)) (as adjusted by section 53(e)(1)) 90

However use of credit still subject to section 383 limitation of $10/year.
Corporate Tax Repeal

Step 4 - Compute MTC Refund (Section 6401)

RCA 45
- Tax Imposed 35
MTC Refund 10

- Section 53(e)
  - Treated as credit allowed under subpart C
  - IRCSection 6401 Applies
- Subject to sequestration - 6.6.%?
- Does X carryforward $80 of AMT credits?
- What if tax imposed was zero?
AMT Repeal

• If AMT credit are subject to limitation under section 383, is the RCA subject to section 383 limitation?

• CCA201126029 - refundable credits arising due to increase in AMT credit and general business credit treated as not subject to 383 limitation.
New International Provisions and NOLs

Interaction between Sections 245A and 1059

• Under Tax Reform, the U.S. shifts (1) from an international tax system where foreign earnings generally were subject to U.S. tax on receipt of a dividend (permitting deferral of foreign earnings) (2) to a system where most foreign earnings will be subject to U.S. tax currently.

• A “transition tax” (Section 965) enables the transition to the new system.

• Under the new system, there are new income categories for U.S. multi-national corporations (MNCs), including:
  – GILTI – Global intangible low-taxed income (Section 951A)
  – FDII – Foreign-derived intangible income (Section 250)
  – BEAT – Base erosion and anti-abuse tax (Section 59A)

• The transition tax and new income categories implicate NOLs and other tax attributes of U.S. MNCs.
  – NOLs affect the consequences of the provisions (i.e., reduce income).
  – The provisions affect how a U.S. MNC uses its NOLs.
    ▪ Foreign tax credit planning
    ▪ New income categories absorb NOLs, with absorption dependent on a number of factors.
Transition Tax (Section 965)

• In general, a 10% U.S. shareholder of a “specified foreign corporation” has a mandatory subpart F income inclusion of the accumulated post-1986 earnings of the specified foreign corporation.
  – A specified foreign corporation is a controlled foreign corporation (CFC) or a foreign corporation with respect to which 1 or more domestic corporations is a U.S. shareholder.

• Corporate transition tax rates:
  – 15.5% on cash and cash-equivalent assets
  – 8% on non-cash assets

• Transition tax may be reduced by foreign tax credits.

• NOL Election – Section 965(n)
  – A U.S. shareholder can elect to exclude:
    ▪ The amount to be included in income under Section 965 in determining the current year net operating loss; or
    ▪ The amount of NOL carryover or carryback to be used.
  – U.S. Parent (in the diagram) might elect out of using NOLs to offset the mandatory income inclusion to (1) avoid reducing its foreign source income from the mandatory inclusion to preserve the use of foreign tax credits for that year and (2) preserve NOLs for future use.
GILTI (Section 951A)

• GILTI is a new category of income that generally would have been subject to tax deferral under prior law.

• A 10% U.S. corporate shareholder of a CFC is required to include its GILTI in gross income, in a manner similar to subpart F income.

• Very generally, GILTI is the excess of a CFC’s net income over a routine or ordinary return on depreciable tangible assets.
  – The computation involves the excess of a CFC’s “net tested income” over an amount equal to 10% of the adjusted basis of the CFC’s depreciable tangible assets, reduced by certain interest expense taken into account in determining the CFC’s net tested income.

• A 10% U.S. corporate shareholder of a CFC is allowed a deduction of 50% of the GILTI amount from 2018 through 2025, and 37.5% beginning in 2026.
  – The deduction is limited to taxable income.
GILTI (Section 951A)

• A 10% U.S. corporate shareholder’s effective tax rate on GILTI (with a 21% corporate income tax rate):
  – 10.5% for 2018 through 2025
  – 13.125% beginning in 2026

• A 10% U.S. corporate shareholder can offset the GILTI amount with foreign tax credits equal to 80% of the foreign taxes attributable to the tested income of its CFC. The foreign tax credits are in a separate basket with no carry back or carry forward.

• GILTI and NOL carry forwards:
  – GILTI represents a new income category for NOL purposes.
  – NOL utilization and the GILTI deduction amount depend on a number of factors, including:
    ▪ Whether an NOL is (1) a pre-Tax Reform NOL that may be carried forward to offset 100% of taxable income or (2) a post-Tax Reform NOL that offsets 80% of taxable income.
    ▪ The relationship between taxable income and the GILTI deduction:
      * If the GILTI deduction exceeds taxable income, an NOL carryover (or a portion thereof) may be absorbed with the GILTI deduction subject to elimination or reduction. But see CCA 201226021.
      * If taxable income exceeds the GILTI deduction, an NOL carryover (or a portion thereof) may be absorbed and there is no reduction to the GILTI deduction.
FDII (Section 250)

• In general, a U.S. corporation’s FDII is its “deemed intangible income” attributable to:
  – A sale of property to a foreign person for use outside the U.S.
  – A license of intellectual property to a foreign person for a foreign use.
  – Services provided to a person located outside the U.S.
  – Special rules apply to related-party transactions.

• The actual computation is complicated.

• The U.S. corporation is required to include FDII in gross income but then is allowed a deduction.
  – The deduction is 37.5% from 2018 through 2025, and 21.875% beginning in 2026.
FDII (Section 250)

• Effective tax rate on FDII (with a 21% corporate income tax rate)
  – 13.125% for 2018 through 2025
  – 16.406% beginning in 2026

• NOL considerations are similar to those for GILTI.
BEAT (Section 59A)

- BEAT is a minimum tax on certain related-party deductible payments (base erosion payments).
- In general, BEAT applies to a U.S. corporation that has annual gross receipts of $500 million or more and related-party deductible payments totaling more than 3% of overall deductions.
- The tax is 5% (2018 rate) of the U.S. corporation’s modified taxable income (MTI), reduced by its regular tax liability. MTI is taxable income increased by any deductible payment made to a related foreign person.
- The U.S. corporation is required to pay the greater of its regular tax liability or its BEAT tax liability.
- A base erosion payment is subject to BEAT when it gives rise to a “base erosion tax benefit,” meaning the tax year in which a deduction for the payment is allowed.
- If a base erosion payment forms a part of an NOL, the base erosion tax benefit is taken into account as part of the Section 172 deduction in the year to which it is carried.
BEAT (Section 59A)

- BEAT effective date ambiguity concerning NOLs:
  - BEAT concerns base erosion payments that are paid or accrued in tax years beginning after December 31, 2017.
  - It is logical that no part of a pre-effective date NOL could arise from an amount paid or accrued after the effective date.
  - This means that the base erosion percentage of any pre-effective date NOL should be zero when absorbed in post-effective date years.
  - However, due to language in the definitions of “base erosion percentage” and “modified taxable income,” pre-effective date NOL deductions could be subject to the BEAT provisions when absorbed in later years. That is, it is not clear whether the base erosion percentage of an NOL carryover deduction is determined in the year the NOL arises, or when absorbed.
Interaction between Sections 245A and 1059

• **Section 1248(a)** generally provides that, if a U.S. person sells the stock of a CFC, the gain recognized on the sale is included in the U.S. person’s gross income as a dividend, to the extent of the earnings and profits of the CFC attributable to the stock.

• **Section 1248(j)** provides that an amount treated as a dividend under Section 1248(a) is treated as a dividend for purposes of applying Section 245A.

• **Section 245A** allows a U.S. corporation that is a 10% shareholder of a foreign corporation (other than a PFIC) a 100% dividends-received-deduction (DRD) for the foreign source portion of the dividends received from the foreign corporation.
Interaction between Sections 245A and 1059

• **Section 1059(a) and (b)** generally provide that, if a corporation receives an “extraordinary dividend,” with respect to a share of stock, (1) the basis of the corporation in the stock is reduced (but not below zero) by the “nontaxed portion” of the dividend and (2) if the nontaxed portion of the dividend exceeds the stock basis, the excess is treated as gain from the sale or exchange of the stock.
  
  – For this purpose, the nontaxed portion of the dividend is the excess of (1) the amount of the dividend over (2) the “taxable portion” of the dividend.
  
  – The taxable portion of the dividend is (1) the portion of the dividend includible in gross income reduced by (2) the amount of any deduction allowable with respect to the dividend under Section 243, 245 or 245A.

• **Section 1059(d)** provides that the reduction in stock basis under Section 1059(a) is treated as occurring on the date the stock becomes ex-dividend.
Example – Foreign Sub Distributes Dividend

- Foreign Sub distributes a dividend to U.S. Parent. Assume Foreign Sub’s e&p exceeds the dividend, and U.S. Parent’s basis in its Foreign Sub stock is less than the dividend.

- U.S. Parent has a 100% DRD with respect to the dividend. Section 245A.

- U.S. Parent reduces its basis in the Foreign Sub stock (but not below zero) by the untaxed portion of the dividend (i.e., the entire amount of the dividend); U.S. Parent recognizes gain to the extent the dividend exceeds stock basis, with the excess treated as gain from the sale or exchange of Foreign Sub stock. Section 1059(a), (b).

- Does Section 1248 apply to the gain, such that it is treated as a dividend? If so, Sections 245A and 1059 presumably are implicated, beginning an endless loop of this analysis (until Foreign Sub’s e&p is depleted).
Example – U.S. Parent Sells Stock of Foreign Sub

- U.S. Parent sells the stock of Foreign Sub to Buyer (unrelated) for cash and recognizes gain on the sale. Assume Foreign Sub’s e&p exceeds the gain recognized.
- U.S. Parent’s gain is treated as a dividend from Foreign Sub, including for purposes of Section 245A. Section 1248(a), (j).
- U.S. Parent has a 100% DRD with respect to the dividend. Section 245A.
- U.S. Parent reduces its basis in the Foreign Sub stock by the untaxed portion of the dividend (i.e., the entire amount of the dividend). Section 1059(a), (b). The basis reduction is treated to occur before the stock sale.
- Is it necessary to recalculate the gain on the stock sale, taking into account the new stock basis?