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Corporate tax alert
International tax

Potential U.S. tax legislative developments and President Trump tax proposals

With the start of the new year, U.S. tax reform is a top priority for both the Legislative and Executive branches in 2017. While it has been a constant discussion topic the past 10 years, this year the Republicans control both the Executive and Legislative branches starting in May 2017, which makes reform much more likely.

There are two proposals that provide insight on potential changes, the Trump proposal and the House GOP Blueprint. While the Trump proposal and the House GOP Blueprint have some key differences and lack a number of technical details, there appears to be quite a bit of agreement around some key policy objectives.

Many policy debates remain and practical challenges could arise if and when tax reform is enacted. The proposals and key changes are outlined below.

In addition to the two proposals, on January 20 President Donald Trump signed an executive order instituting a moratorium on all federal rulemaking until the new administration can review all regulations in process. This executive order will require that recently released tax rules, including final regulations for master limited partnership qualifying income, dividend equivalent payments and a proposal on a partnership audit regime, to be sent back to the Internal Revenue Service until further notice.

Outline of House GOP Blueprint and Trump Tax Proposal

I. International Tax Regime, Base Erosion, and Repatriation

Trump tax proposal provides a significant reduction of the highest income tax rate from 35% to 15%, while simultaneously broadening the taxable base by eliminating or limiting most business tax expenditures. The Republican proposal ("House GOP Blueprint") also proposes to lower the tax rate to 20%, but would implement a territorial tax regime.

Trump's proposal provides for retaining a current law system of worldwide taxation and a foreign tax credit regime, but would repeal deferral. On the other hand, the House GOP Blueprint provides for a territorial tax regime, with a 100% participation exemption. The House GOP Blue print also provides for the elimination of most Subpart F rules, except with respect to passive income.

Both proposals, provide for a one-time deemed repatriation of accumulated deferred foreign income, with Trump's proposal providing a 10% tax and the House GOP Blueprint providing for a 8.75% tax on cash and 3.5% tax on non-cash assets. The Trump proposal is silent on the number of years to pay the tax, but the House GOP Blueprint provides paying the repatriation tax over 8 years at the taxpayer's election.

One major difference between the two proposals, is the House GOP Blueprint provides for border adjustments using a destination based cash-flow approach, which has elements similar to a consumption-based tax. The cash-flow based approach that will replace the current income-based approach for taxing both corporate and non-corporate businesses will be applied on a destination basis. The proposal provides that "products, services and intangibles that are exported outside the United States will not be subject to U.S. tax regardless of where they are produced, and products, services and intangibles that are imported into the United States will be subject to U.S. tax regardless of where they are produced." It is anticipated that this will result in a broader tax base by increasing the tax cost of imports.

II. Research Credit

R&D credit remains allowable in both proposals. The House GOP Blueprint will analyse options to make it more effective.

III. Section 199 deduction

The 9% deduction for domestic production activities is likely to be repealed in both proposals.

IV. Depreciation

Under Trump's proposal, US manufacturing activities will be able to elect full deduction of the cost of their capital investments in the first year for tangible property including equipment and buildings, and related capital costs of acquisition of intangible property. There would also be an option to revoke the election within 36 months. Under the House GOP Blueprint taxpayers would be able to fully expense cost of tangible and intangible assets in year one, except for land.

The U.S. Corporate Tax team is available to discuss any questions with respect to these potential changes and the impacts that they could have on companies' U.S. business.

Contacts

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