Accounting for Income Taxes
Quarterly Hot Topics

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US Federal

Treasury and the IRS recently issued proposed Treasury Regulations and Notices related to the Tax Cuts and Jobs Act (the “Tax Act”)
The recently issued proposed Treasury Regulations and Notices may impact the financial statement income tax accounting calculations pursuant to ASC 740 of companies for the period of enactment or subsequent quarters in the measurement period under SAB 118.

Please refer to Deloitte Financial Reporting Alert 18-1—Frequently Asked Questions About Tax Reform (Updated August 30, 2018), FAQ 12.4 for considerations regarding when to reflect the financial statement impact of guidance received during the measurement period.

Transition tax proposed Treasury Regulations released

On August 1, 2018, the US Department of the Treasury (“Treasury”) and the Internal Revenue Service (“IRS”) released proposed regulations under IRC section 965 (the “transition tax” provision of the Tax Act). The proposed Treasury Regulations under IRC section 965 restate the guidance provided in the prior guidance, with some modifications, and provide additional guidance related to IRC section 965.

Please see United States Tax Alert dated August 10, 2018 for additional details.

100% bonus depreciation proposed Treasury Regulations released

On August 3, 2018, the Treasury and the IRS issued proposed Treasury Regulations under IRC section 168 (the “Proposed Regulations”) providing long-awaited guidance regarding the 100% bonus depreciation provisions of the Tax Act, which include the following provisions:

- Property acquired or self-constructed under a written binding contract entered into on or before September 27, 2017, is not eligible for 100% bonus depreciation. The date a written binding contract is entered into (and not, for example, the closing date) is the date that is used in evaluating whether property is eligible for 100% bonus depreciation.
- In determining eligibility for 100% bonus depreciation, a taxpayer is considered to have used property only if the taxpayer previously had a depreciable interest in the property (whether or not the taxpayer claimed depreciation).
- Assets acquired in a transaction to which IRC section 336(e) or IRC section 338 applies generally are eligible for 100% bonus depreciation.
- IRC section 743(b) adjustments generally are eligible for 100% bonus depreciation, but IRC section 734(b) adjustments and distributed partnership property with a basis determined under IRC section 732 are not eligible for bonus depreciation.

Executive compensation deduction limitation Notice released

IRC section 162(m) generally imposes a $1 million limit on the deduction allowed to be taken by a “publicly held corporation” for remuneration paid to covered employees. The Tax Act made significant amendments to IRC section 162(m), including amending the definition of applicable employer remuneration to eliminate exceptions for qualified performance-based compensation and commissions, expanding the definitions of covered employee and publicly held corporation, and adding a transition rule to allow for grandfathering certain payments. These rules impact any corporation which is an issuer of securities that is required to be registered under section 12 or that is required to file reports under section 15(d) of the Securities Exchange Act of 1934 paying certain executives remuneration that exceeds $1 million for tax years beginning after December 31, 2017.
On August 21, 2018, the IRS issued Notice 2018-68 ("the Notice") to provide initial guidance on certain aspects of the amendments made by the Tax Act. In particular, the Notice addresses the amended rules for identifying covered employees and the operation of the grandfather rule, including when a material modification to a written binding contract has occurred rendering the contract ineligible for grandfathering.

IRS clarifies application of proposed Treasury Regulations on treatment of certain payments made in exchange for state and local tax credits to business taxpayers

On September 5, 2018, the IRS clarified the application of the proposed Treasury Regulations with respect to businesses who make business-related payments to charities or government entities for which the taxpayers receive state or local credits. In the clarification, the IRS stated that such taxpayers can generally deduct the payments as business-related expenses.

Responding to taxpayer inquiries, the IRS clarified that this general deductibility rule is unaffected by the recent notice of proposed rulemaking concerning the availability of a charitable contribution deduction for contributions pursuant to such programs. The business expense deduction is available to any business taxpayer, regardless of whether it is doing business as a sole proprietor, partnership or corporation, as long as the payment qualifies as an ordinary and necessary business expense. Therefore, businesses generally can still deduct business-related payments in full as a business expense on their federal income tax return.

Global Intangible Low Taxed Income proposed Treasury Regulations Released

The Treasury and the IRS released on September 13, 2018 proposed Treasury Regulations addressing the new global intangible low-taxed income (GILTI) provision of the Tax Act.

Treasury Secretary Steven Mnuchin said in a September 13 news release that the proposed regulations offer “clarity for US shareholders on computing global intangible low-taxed income.” He noted, though, that “these proposed regulations do not include foreign tax credit computational rules, which will be addressed in future regulatory packages.”

Please refer to the September 14, 2018 issues of Tax News & Views for additional detail as well as a high-level Deloitte summary of the proposed regulations.

US Federal Tax Accounting Methods and Periods

CCA memorandum decision on success-based fee deduction and safe harbor election

In a recent chief counsel advice (CCA) memorandum, CCA 201830011 (the “CCA”), the IRS concluded that an investment banker’s allocation letter and slide presentation did not satisfy the documentation requirements for a success-based fee deduction. The IRS also noted that because the Taxpayer did not make the safe harbor election under Revenue Procedure 2011-29, it must satisfy the documentation requirements under Treasury Regulation section 1.263(a)-5(f), or the amount deductible is zero.

In general, a taxpayer (whether it is the acquirer or target) must capitalize an amount paid to facilitate certain capital transactions described in Treas. Reg. section 1.263(a)-5(a)(1)-(10). An amount is paid to facilitate such transaction if the amount is paid in the process of investigating or otherwise pursuing the transaction.
An amount paid that is contingent on the successful closing of a covered transaction (a "success-based fee") is presumed to facilitate the transaction, and is required to be capitalized unless a taxpayer maintains sufficient documentation to establish that a portion of the fee is allocable to activities that do not facilitate the transaction. In lieu of satisfying the supporting documentation requirement, Rev. Proc. 2011-29 allows taxpayers to make a safe harbor election for success-based fees paid or incurred in taxable years ending on or after April 8, 2011. Such election allows a taxpayer to treat 70 percent of success-based fees paid in connection with a covered transaction as an amount that does not facilitate the transaction for purposes of capitalization under IRC section 263(a). The remaining 30 percent of the fee must be capitalized as an amount that facilitates the transaction.

Taxpayers who paid or incurred success-based fees in a covered transaction and are considering not electing, or have not elected Rev. Proc. 2011-29 should be aware of the IRS’s advice in the CCA and consult with their tax advisor.

**US Multistate**

**Recent US Supreme Court decision—Wayfair**

On June 21, 2018, the US Supreme Court issued its opinion in *South Dakota v. Wayfair, Inc.* et al. overturning the decades-old physical presence nexus standard required in order for a state or locality to impose a sales or use tax collection responsibility upon a remote seller. While the *Wayfair* decision can be expected to have a significant impact on sales and use tax collection obligations of remote sellers, the *Wayfair* decision potentially also impacts state-level nexus determinations relative to income tax. This potential income tax consequence is reinforced by the fact that a number of states (e.g., California and New York) have enacted nexus standards for income taxes based on the existence of sales or customer transactions exceeding a certain threshold annually.

For additional details, please see the [Multistate Tax Alert](#) dated June 28, 2018.

**New state judicial updates**

**Maryland Court affirms that companies have nexus based on “enterprise dependency” with in-state affiliates**

A Maryland Court of Special Appeals recently affirmed that "enterprise dependency" existed between two out-of-state companies and their in-state affiliates such that the out-of-state companies were not considered separate business entities but instead part of a unitary business enterprise for Maryland corporate income tax purposes.

For additional details, please refer to the August 17, 2018 issue of [State Tax Matters](#).

**Massachusetts Appellate Tax Board holds that taxpayer is a “manufacturer” required to compute its corporate excise tax liability using single sales factor apportionment**

On June 21, 2018, the Massachusetts Appellate Tax Board (the "Board") issued a case ruling addressing the scope of the "manufacturing corporation" definition for Massachusetts corporate excise tax purposes as it applied to a taxpayer that did not physically manufacture any of the products that it sold. Instead, the taxpayer contracted with a third-party manufacturer to produce the shoes according to a detailed design sketch and a description of materials developed by the taxpayer. The Board determined that the taxpayer was properly treated as a manufacturing corporation and therefore required to use a single-sales factor apportionment formula.

For additional details, please refer to the July 24, 2018 [Multistate Tax Alert](#).
New Jersey Superior Court appellate division affirms Tax Court decision in MCI

On June 15, 2018, the appellate division of the New Jersey Superior Court affirmed the earlier decision of the New Jersey Tax Court ("Tax Court") in MCI Communication Services "substantially for the reasons expressed" by the Tax Court. The Tax Court of New Jersey had previously held that the taxpayer could not adjust its New Jersey entire net income Corporation Business Tax (CBT) base to reverse the impact of reductions in tax attributes required under the IRC and related consolidated return Treasury Regulations, notwithstanding New Jersey taxation of corporations on a separate entity basis.

For additional details, please see the Multistate Tax Alert dated June 22, 2018.

Oregon Supreme Court affirms that affiliates lacking in-state physical presence had nexus for corporate income tax purposes

The Oregon Supreme Court (Court) has affirmed that two out-of-state finance companies had nexus with Oregon for the tax years at issue for Oregon corporate income tax purposes even though they lacked an in-state physical presence, because they generated income derived from sources in Oregon. In doing so, the Court explained that Oregon’s corporate income tax statutes (which are separate and distinct from Oregon’s corporate excise tax provisions) merely reference and provide that taxable income be derived from “sources within this state” and that “nothing about the statutory text or context suggests that the taxpayer must also have some physical presence here.” Please note that Oregon’s corporate excise tax generally is imposed on C corporations doing business in Oregon, while Oregon’s corporate income tax generally is imposed on C corporations that are not doing business in Oregon but have income from Oregon sources.

For additional details, please refer to the August 17, 2018 issue of State Tax Matters.

Texas Comptroller decision—taxpayer did not qualify for reduced Texas franchise tax rate

The Texas Comptroller of Public Accounts (Comptroller) recently released a decision addressing whether a prescription eyeglass distributor (taxpayer) was eligible for the reduced tax rate reserved for taxable entities primarily engaged in retail or wholesale trade for purposes of the Texas franchise tax (commonly referred to as the Texas margin tax) under Texas Tax Code (TTC) section 171.002(b).

The Comptroller ultimately determined taxpayer’s processing activities related to lenses it sold to customers constituted producing or manufacturing a product under TTC section 171.002(c)(2), which disqualified the taxpayer from using the reduced rate.

For additional details, please see the Multistate Tax Alert dated July 30, 2018.

Texas Comptroller ruling—taxpayer may not include costs of purchasing franchise agreement in cost of goods sold deduction

The Comptroller recently released a ruling addressing whether an automotive retailer (taxpayer) was entitled to include the purchase price of franchise rights obtained as part of a recent acquisition within its costs of goods sold (COGS) for purposes of the Texas franchise tax (commonly referred to as the Texas margin tax) under TTC sections 171.001 and 171.1012. The Comptroller ultimately determined the amount paid by the taxpayer for the car manufacturer’s franchise rights did not qualify as deductible direct COGS under TTC section 171.1012(d)(10), but instead were indirect COGS and affirmed the refund denial.

For additional details regarding this development, please refer to the Multistate Tax Alert dated September 5, 2018.
Texas trial court holds in taxpayer’s favor by sourcing subscription revenues based on fair value of services performed in-state, rather than market-based approach

In a case involving the sourcing of a satellite radio company’s subscription revenues for Texas franchise tax (commonly referred to as the Texas margin tax) purposes, a Texas trial court recently held in the taxpayer’s favor that such receipts must be sourced to Texas based on the fair value of services performed in Texas, rather than the Comptroller’s “market” method based on the location of where the taxpayer’s services were received by subscribers. More specifically, the Comptroller had unsuccessfully argued that the taxpayer’s subscription receipts should be sourced to Texas based on the locations where the satellite transmissions were received by subscribers, and thus had adjusted the taxpayer’s Texas apportionment factor accordingly.

Under the facts, the taxpayer’s headquarters, transmission equipment, and production studios were mostly located outside of Texas; the taxpayer generally produced and transmitted its audio radio content from outside of Texas. Thus, the taxpayer’s receipts were properly sourced based on the location of the taxpayer’s production activities (i.e., outside of Texas) according to the district court. The Comptroller has since filed an appeal with the Texas Third Court of Appeals.

For additional details, please refer to the September 7, 2018 issue of State Tax Matters.

Wisconsin DOR issues proposed rule changes that attempt to clarify nexus-creating activities

The Wisconsin Department of Revenue has issued proposed rule amendments that attempt to clarify the level of activity and/or types of activities that, when performed by out-of-state businesses, establish nexus in Wisconsin for Wisconsin corporate income and franchise tax purposes. Currently, this administrative rule provides a listing of activities that constitute nexus for an unlicensed foreign corporation thereby requiring the filing of Wisconsin corporate income or franchise tax returns. This current list of activities employs the terms “usual or frequent” and “regularly” to describe certain activities that create nexus—such as defining “regularly” to mean fifteen or more days of activity.

For additional details, please refer to the August 17, 2018 issue of State Tax Matters.

New legislative updates

Alaska

Effective January 1, 2019, new law requires a corporate taxpayer that qualifies as a “public utility” to allocate and apportion its state corporate income in accordance with Alaska statutes adopting the Multistate Tax Compact apportionment method (i.e., using the same three-factor apportionment formula of property, payroll, and sales that generally is used by all other non-oil and gas corporate income taxpayers in Alaska). Under current state law, public utilities are not “required” to file their state corporate income tax returns using this three-factor formula; however, there is also no other apportionment method specified for such taxpayers.

For additional details, please refer to the July 27, 2018 issue of State Tax Matters.
Florida
The Florida Department of Revenue has issued a technical assistance advisement regarding a corporate taxpayer's gross receipts from intercompany product sales with its foreign affiliates, specifically concluding that, under the given facts in this case, such transactions constitute includable "sales" for purposes of computing the taxpayer’s sales factor for state corporate income tax apportionment purposes.

For additional details, please refer to the July 27, 2018 issue of State Tax Matters.

Missouri
On July 5, 2018, Governor Parson signed a new law which provides that intercompany transactions between corporations that file as part of a Missouri consolidated income tax return generally are not included in the definition of "sales" for apportionment purposes or Missouri taxable income calculations. Additionally, the new law provides that in each year in which there is a reduction in the Missouri tax rate applicable to corporations, there shall be a corresponding and proportional reduction in the Missouri tax rate applicable to banks, credit institutions, and credit unions and savings and loan associations. This new law also clarifies that an entity not subject to Missouri corporate income tax generally is not required to complete or file any document or return related to Missouri corporate income taxes.

For additional details, please refer to the July 13, 2018 issue of State Tax Matters.

New Jersey
On July 1, 2018, Governor Murphy signed Assembly Bill 4202 (A4202), which includes, among other changes, the following modifications to New Jersey corporate business tax:

- Effective retroactive to January 1, 2017, add limitations to the dividend received deduction.
- Effective January 1, 2018, adds a 2.5 percent surtax (increasing tax rate from 9 percent to 11.5 percent) on entire net income in excess of $1 million for privilege periods beginning on or after January 1, 2018, through December 31, 2019. For privilege periods beginning on or after January 1, 2020, to December 31, 2021, the surtax is 1.5 percent.
- Effective January 1, 2018, adds limitations on the treaty exemption affecting interest expense and intangible related add-backs.
- Effective January 1, 2019, amends provisions affecting the corporate business tax base including:
  - Adoption of mandatory unitary combined reporting.
  - A new deduction for publicly traded companies related to the impacts upon deferred tax assets and liabilities resulting from the adoption of mandatory unitary combined reporting.
  - Amendment to the computation and utilization of net operating losses.
  - Adoption of market-based sourcing of services.

For additional details, please refer to the Multistate Tax Alert dated July 18, 2018.
**North Carolina**

On June 12, 2018, the North Carolina General Assembly overrode Governor Roy Cooper’s veto of Senate Bill 99 (S.B. 99)—thereby enacting S.B. 99 into law which impacts state income, franchise, and sales and uses taxes. S.B. 99 includes the following significant modifications to North Carolina income tax law which are effective immediately unless specified otherwise.

- Modifies and clarifies certain provisions related to the sales factor, notably receipts from intangibles.

For additional details regarding this development, please refer to the [Multistate Tax Alert](#) dated July 17, 2018.

**Multistate tax considerations of the Tax Act**

Typically, states address conformity to the IRC through legislation, although certain states may seek to address essential details through administrative guidance as well. Legislative responses are expected throughout 2018, depending upon when each state is in session.

The following states have recently enacted new tax legislation and/or administrative guidance in connection with the Tax Act:

**Alabama**

The Alabama Department of Revenue (“Department”) has issued another notice applicable to Alabama corporate taxpayers that paid or accrued transition tax, including those filing as part of a federal consolidated group. In this notice, the Department generally explains that such taxpayers, including those filing as part of a federal consolidated group, that paid or accrued transition tax must remove the transition tax from the standard calculation of Alabama’s federal income tax deduction.

Additionally, the Department recently announced that it has issued preliminary guidance on the state impact of certain provisions of the Tax Act, specifically addressing whether and how the provisions of the federal legislation are tied to Alabama’s taxing regime, as they relate to individuals (including sole proprietors), corporations, and financial institutions.

For additional details, please refer to the June 29, 2018 issue of [State Tax Matters](#) and the August 3, 2018 issue of [State Tax Matters](#).

**Connecticut**

The Connecticut Department of Revenue Services has issued administrative guidance with respect to how some provisions under the Tax Act may impact Connecticut corporate business taxpayers—specifically regarding Connecticut’s treatment of GILTI for tax years beginning after 2017, including related application for purposes of computing Connecticut’s gross income, dividends received deduction and apportionment factors.

For additional details, please refer to the July 27, 2018 issue of [State Tax Matters](#).
Georgia

The Georgia Department of Revenue has issued a policy bulletin discussing taxpayer eligibility for Georgia’s exclusion for dividends from sources outside the United States, applicable for tax years beginning before January 1, 2018. The guidance addresses:

- which entities are eligible for this exclusion and
- whether Georgia has deferral payment options similar to IRC sections 965(h) or 965(i)

For additional details, please refer to the July 13, 2018 issue of State Tax Matters.

Hawaii

On September 4, 2018, the Hawaii Department of Taxation has issued a summary of legislation enacted in 2018, including recently enacted legislation that updates statutory references to the IRC, providing that for taxable years beginning after December 31, 2017, references to the IRC in Hawaii corporate income tax laws generally refer to the federal law in effect as amended as of February 9, 2018. The guidance also generally explains that this legislation makes numerous amendments to the way in which Hawaii conforms to the IRC in response to the Tax Act.

For additional details, please refer to the September 14, 2018 issue of State Tax Matters.

Idaho

The Idaho State Tax Commission has issued a temporary administrative rule and simultaneously proposed a similar permanent new administrative rule regarding certain provisions of the Tax Act, specifically addressing how to report the deemed repatriation income under IRC section 965 on an Idaho tax return. Reflecting Idaho legislation enacted over the last several months addressing state conformity to various federal tax provisions both the temporary and proposed permanent new rule provide that Idaho taxpayers must include the IRC section 965 increase in their subpart F income when computing their Idaho taxable income regardless of how such income is reported to the IRS on the federal income tax form.

For additional details, please refer to the August 10, 2018 issue of State Tax Matters.

Indiana

The Indiana Department of Revenue has issued two bulletins on how to report repatriated income under IRC section 965, in light of Indiana’s recently enacted legislation that updates state conformity to certain provisions of the IRC. The bulletins generally explains that Indiana law partially aligns with the Internal Revenue Service on how such income is reported, and that impacted C corporation taxpayers must include the gross amount of the repatriated dividend in their Indiana adjusted gross income.

Additionally, the bulletins address the recently enacted legislation that relates to (i) foreign source dividend treatment, including underlying apportionment implications; (ii) the requirements for inclusion of GILTI, such as the necessary adjustments and apportionment treatment for Indiana state income tax purposes; and (iii) required modifications related to deductions for business interest under IRC section 163(j). The bulletin also discusses net operating losses and includes guidelines for interest and penalty waivers.

For additional details, please refer to the July 13, 2018 issue of State Tax Matters, the July 20, 2018 State Tax Matters and the September 7, 2018 issue of State Tax Matters.
Kentucky

The Kentucky Department of Revenue ("Department") has issued guidance on certain provisions of the Tax Act and how the provisions impact state income taxation in Kentucky, specifically Kentucky’s income tax treatment of GILTI. The Department references recently enacted legislation which includes updating Kentucky’s IRC conformity date to apply to the IRC as in effect on December 31, 2017 (thereby conforming to several provisions contained in the Tax Act).

For additional details, please refer to the August 24, 2018 issue of State Tax Matters.

Maine

Effective immediately and applicable to tax year beginning on or after January 1, 2017, and “to any prior tax years as the United States Internal Revenue Code of 1986 and amendments to that Code as of March 23, 2018,” new law enacted September 12, 2018 generally conforms state corporate income tax references to the IRC as the IRC in effect as of March 23, 2018. The legislation includes a number of new state coupling and decoupling provisions to the IRC, some of which are in response to the Tax Act, as well as various other state tax law changes such as revised corporate income tax brackets beginning in 2018, and elimination of Maine’s corporate alternative minimum tax for tax years beginning after 2017.

Regarding the federal mandatory repatriation of deferred foreign income, taxation of dividends, subpart F income and GILTI, the legislation includes a number of specified addition and subtraction modifications for state corporate income tax purposes, as well as modifies Maine’s deduction for dividends received from certain foreign affiliates. Another law change of note includes permitting a state deduction to offset some of the effects of the new federal net operating loss limitations.

For additional details, please refer to the September 14, 2018 issue of State Tax Matters.

Massachusetts

On September 11, 2018, the Massachusetts Department of Revenue ("Department") issued draft administrative guidance ("Draft TIR") for under the Tax Act may impact Massachusetts corporate taxpayers, specifically Massachusetts’ treatment of the federal repatriation transition tax under IRC section 965. The Draft TIR attempts to provide guidance on the Massachusetts tax treatment of the deemed repatriated income for business corporations and financial institutions including related apportionment calculations, as well as how to report such income for state purposes, noting that for many affected taxpayers, the deemed repatriated income is recognized in the 2017 taxable year.

For additional details, please refer to the September 14, 2018 issue of State Tax Matters.

Additionally on September 11, 2018, the Department issued an emergency amended version of an administrative regulation that addresses the requirements and procedures for obtaining classification as a “manufacturing corporation” for various tax purposes under Massachusetts law, including how some changes under the Tax Act should not impact such classification—particularly with regard to calculating the “gross receipts fraction” used to determine whether a taxpayer qualifies as a manufacturing corporation. More specifically, the amended version provides that in calculating the gross receipts fraction denominator for eligibility the term ‘dividend’ shall not include amounts included in federal gross income pursuant to IRC sections 951 and 951A, as amended and in effect for the taxable year.

For additional details, please refer to the September 14, 2018 issue of State Tax Matters.
Michigan

The Michigan Department of Treasury ("Department") has issued a notice explaining the impact of various provisions of the Tax Act on Michigan’s corporate income tax (CIT), specifically the impact of the new foreign income repatriation provisions under IRC section 965, base erosion and anti-abuse tax (BEAT) provisions, and GILTI provisions. The guidance generally explains that the IRC section 965 repatriated income reported for federal income tax purposes must be included in the federal taxable income used as the starting point for computing Michigan’s CIT base income; however, the CIT provides a deduction for foreign dividends, including but not limited to Subpart F income, to the extent included in federal taxable income. Regardless, the Department concludes that taxpayers must properly report IRC section 965 income on their Michigan return even though it may have no tax effect. Accordingly, taxpayers that have filed their 2017 Michigan CIT returns and have not included the IRC section 965 income “must file an amended 2017 Michigan CIT return to properly report that income and any associated deduction.”

For additional details, please refer to the June 8, 2018 issue of State Tax Matters and the July 13, 2018 issue of State Tax Matters.

Minnesota

Adding to some of its earlier guidance on how certain provisions of the Tax Act may impact Minnesota business tax returns the Minnesota Department of Revenue has issued an information sheet outlining how the recent federal changes involving deferred foreign income and the new transition tax affect some Minnesota tax returns for the 2017 tax year. The guidance generally explains that under IRC section 965, deferred foreign income is part of federal taxable income and added to a US shareholder’s subpart F income. However, the guidance notes that even though federal taxable income generally is the starting point for determining income subject to Minnesota income and franchise taxes, deferred foreign income is not included in Minnesota net income because state tax law does not currently conform to the changes made by the Tax Act.

For additional details, please refer to the August 17, 2018 issue of State Tax Matters.

New Jersey

As mentioned above, on July 1, 2018, Governor Murphy signed A4202, which includes, among other changes, the following modifications to New Jersey corporate business tax related to the Tax Act:

- Effective January 1, 2018, decouples from certain provisions of the Tax Act, including a pro-rata application of limitations under IRC section 163(j).

For additional details, please refer to the July 6, 2018 issue of State Tax Matters and the Multistate Tax Alert dated July 18, 2018.
New York

The New York Department of Taxation and Finance has issued two notices on the Tax Act, specifically the state income tax impact for C corporations and flow-through entities, respectively, for tax year 2017 regarding the mandatory deemed repatriation income under IRC section 965. The first notice discusses and provides instructions for reporting these IRC section 965 amounts on the 2017 New York State corporation tax returns and attachments, while the second notice includes instructions for reporting these IRC section 965 amounts on the 2017 New York S corporation, partnership (including a limited liability company treated as a partnership for federal income tax purposes), and fiduciary (trusts and estates) New York State tax returns and attachments.

For additional details, please refer to the August 10, 2018 issue of State Tax Matters.

North Carolina

As mentioned above, on June 12, 2018, the North Carolina General Assembly overrode Governor Roy Cooper's veto of S.B. 99—thereby enacting S.B. 99 into law which impacts state income, franchise, and sales and uses taxes. S.B. 99 includes the following significant modifications to North Carolina income tax law which are effective immediately unless specified otherwise.

- Updates the North Carolina income tax code to conform to the IRC as of February 9, 2018 for both corporate and individual income tax purposes.
- Modifies certain additions and subtractions from federal taxable income to arrive at North Carolina net income in response to the Tax Act.
- Clarifies the filing requirements as a result of federal income tax return changes and adjustments.

For additional details regarding this development, please refer to the Multistate Tax Alert dated July 17, 2018.

North Dakota

Commenting on how certain provisions of the Tax Act make “significant changes to the taxation of foreign-sourced income earned by US corporations and their foreign subsidiaries,” the North Dakota State Tax Commissioner has issued a notice describing how some of these provisions impact North Dakota business tax returns. The notice addresses the treatment for North Dakota tax purposes of IRC section 965 regarding the deemed repatriation of foreign dividends, GILTI, foreign-derived intangible income (FDII), and the BEAT provisions. The guidance generally applies to the 2017 and subsequent tax years.

For additional details, please refer to the August 24, 2018 issue of State Tax Matters.

Oregon

Pursuant to recently enacted Oregon legislation that addresses certain provisions of Tax Act, specifically the mandatory deemed repatriation of income under IRC section 965, as well as the repeal of Oregon’s “tax haven” statute, the Oregon Department of Revenue has issued an administrative rule that prescribes a method for computing the new state repatriation tax credit based upon the lesser of:

- Oregon tax attributable to IRC section 965, or
- The amount of Oregon tax attributable to and imposed on the taxpayer pursuant to Oregon’s tax haven law for tax years beginning on or after January 1, 2014 and before January 1, 2017.

For additional details, please refer to the July 13, 2018 issue of State Tax Matters.
Pennsylvania

Effective immediately and applicable to tax years beginning on or after January 1, 2017, new law essentially allows for Modified Accelerated Cost Recovery System ("MACRS") depreciation deductions on qualified property for which a 100% bonus deduction is claimed for federal tax purposes, thereby reversing the Pennsylvania Department of Revenue policy as previously announced in Corporation Tax Bulletin 2017-02 which had stated that any deductions for depreciation of qualified property under IRC section 168(k) placed in service after September 27, 2017 must be added back to Pennsylvania taxable income with absolutely no recovery allowed until the taxpayer disposes of the asset.

While the addback of bonus depreciation will still be required, this new law amends the Pennsylvania corporate net income tax statute to allow an additional deduction equal to the regular MACRS depreciation that would have applied to the qualified property pursuant to IRC sections 167 and 168 absent the application of IRC section 168(k).

For additional details, please refer to the July 6, 2018 issue of State Tax Matters.

City of Philadelphia

The City of Philadelphia (City) Department of Revenue has issued a policy update on how it treats federal bonus depreciation for City “Business Income and Receipts Tax” and “Net Profits Tax” purposes. The guidance explains that the City is required to follow the Commonwealth of Pennsylvania rules on federal bonus depreciation, and that the Commonwealth of Pennsylvania (and thus also Philadelphia) has decoupled from the federal 100% bonus depreciation deduction allowed for qualified properties acquired and placed into service after September 27, 2017 and before January 1, 2023 under the Tax Act.

As such, the Department explains that both the Commonwealth of Pennsylvania and the City require taxpayers to add back to their federal taxable income any 100% bonus depreciation taken on their federal return—noting that both Pennsylvania and the City do allow taxpayers to take “normal depreciation” (as permitted in IRC section 167) pursuant to recently enacted Pennsylvania legislation.

For additional details, please refer to the August 10, 2018 issue of State Tax Matters.

Rhode Island

On the Rhode Island Division of Taxation's 2018 third quarter newsletter, comments were made related to some state tax impacts of the Tax Act, in which the Division of Taxation generally explained that because the provisions of IRC section 179 recently were expanded, “Rhode Island follows suit” under state law conformity provisions. However, even though the Tax Act changed the rules for bonus depreciation pursuant to IRC section 168(k), “Rhode Island does NOT follow suit” pursuant to state law generally permitting depreciation for Rhode Island tax purposes to the extent it would have been computed prior to the enactment of the federal Job Creation and Worker Assistance Act of 2002.

Additionally, the Rhode Island Department of Revenue’s Division of Taxation has released the latest in a series of documents involving the state income tax treatment of IRC section 965 income for C corporations, including guidance on how to report deferred foreign income for Rhode Island tax purposes for the 2017 tax year in light of the Tax Act, and an accompanying new administrative regulation addressing the same.

For additional details, please refer to the July 27, 2018 issue of State Tax Matters and the August 10, 2018 issue of State Tax Matters.
Utah

Effective immediately and with "retrospective operation for the last taxable year of a taxpayer beginning on or before December 31, 2017,” new law clarifies the application of legislation enacted earlier this year in Utah which permits corporations to elect to pay Utah corporate income tax due on deferred foreign income under IRC section 965 in installments under certain circumstances. Consistent with how Utah has treated the repatriation of foreign dividends in the past, the new law specifies that corporations can receive a related 50% deduction on such income. This legislation also adds deferred foreign income to the definition of “unadjusted income” for Utah corporate income tax purposes, and modifies the payment schedule for a corporate taxpayer to pay the associated income tax on deferred foreign income.

Additionally, the Utah State Tax Commission (Commission) had issued state tax guidance pursuant to certain provisions of the Tax Act and recently enacted state legislation which clarifies that deferred foreign income under IRC section 965 generally is subject to Utah corporate income tax. Accordingly, the Commission explains that corporate taxpayers having a federal tax liability under IRC section 965(a) are also subject to tax on that income by Utah.

For additional details, please refer to the July 27, 2018 issue of State Tax Matters and the August 24, 2018 issue of State Tax Matters.

Vermont

Enacted July 2, 2018, effective retroactively to January 1, 2018, and applicable to taxable years beginning on and after January 1, 2017, new law generally updates statutory references to the IRC for state personal and corporate income tax purposes, referring to the federal income tax law as in effect on December 31, 2017, but “without regard to the federal income tax rates” under IRC section 11. The new law decouples from and/or responds to certain provisions of the Tax Act.

Additionally, the Vermont Department of Taxation (“Department”) has issued guidance on certain provisions of the Tax Act, specifically Vermont’s treatment of the federal repatriation transition tax under IRC section 965. The Department explains that with the enactment of the Tax Act, Vermont net income and taxable income changed for state personal and corporate income tax purposes because the federal definition was altered. Regarding the federal one-time inclusion in tax year 2017 of certain untaxed foreign earnings and profits (i.e., IRC section 965 income) in a taxpayer’s subpart F income, the Department generally explains that this accumulated post-1986 deferred foreign income is part of the Vermont tax base for the 2017 tax year as well.

Additionally, the Department issued guidance on Vermont’s treatment of GILTI. The Department explains that GILTI is now included in federal taxable income; therefore, as a result, GILTI is automatically included in Vermont taxable income and Vermont net income. Further, the Department explains that the federal GILTI deduction now allowed under IRC section 250 is also available to domestic corporations for Vermont corporate income tax purposes.

For additional details, please refer to the August 3, 2018 issue of State Tax Matters, the July 6, 2018 issue of State Tax Matters, and the August 17, 2018 issue of State Tax Matters.
Amnesty/Voluntary Disclosure

Indiana DOR offers voluntary disclosure initiative for online sellers that runs through December 31, 2018

The Indiana Department of Revenue (Department) is offering certain qualifying retailers that do not "already have a clearly defined sales tax and income tax filing obligation" in Indiana the opportunity to participate in a one-time voluntary disclosure initiative (VDI). According to the Department, this special VDI is tailored to meet the unique needs of retailers that have inventory located in third-party Indiana warehouses and sell to Indiana customers—explaining that many of these retailers selling goods to Indiana customers through service providers have both income and sales/use tax obligations in Indiana.

For additional details, please refer to the July 6, 2018 issue of State Tax Matters.

New Jersey

As mentioned above, on July 1, 2018, Governor Murphy signed A4202, which includes, among other changes, the following changes to the New Jersey corporate business tax amnesty program:

- Establishes an amnesty period not to exceed 90 days.
- Creates a non-abatable five percent penalty for eligible taxpayers who fail to pay during the amnesty period.

On July 17, 2018, the New Jersey Division of Taxation posted a notice, indicating that the amnesty will not begin until after November 1, 2018, and will end by January 15, 2019.

For additional details, please refer to the Multistate Tax Alert dated July 25, 2018.

International

Classification of Argentina as a highly inflationary economy under US GAAP

Argentina has continued to experience negative economic trends, as evidenced by (1) multiple periods of increasing inflation rates, (2) devaluation of the peso, and (3) increasing borrowing rates, requiring the Argentinian government to take mitigating actions. Due to the lack of reliable CPI data (among other factors), for US GAAP financial reporting purposes Argentina would be considered a highly inflationary economy after the calendar year second quarter of 2018. Thus, under ASC 830 (as described in Financial Reporting Alert 18-8), the rules governing the treatment of highly inflationary economies with respect to the Argentine currency would start no later than July 1, 2018.

For taxpayers that follow the US GAAP methodology in determining whether a currency is hyperinflationary for tax purposes, the Argentine Peso (ARS) may be a hyperinflationary currency for tax purposes as of taxable year beginning in 2019, and such taxpayers’ controlled foreign corporations and IRC section 987 qualified business units with ARS as their functional currency may be required to adopt the United States Dollar Approximate Separate Transactions Method (DASTM) at the beginning of such taxable year.

Please see United States Tax Alert dated August 13, 2018 for additional details.
Did You Know?

Accounting for highly inflationary currency

When the country in which a foreign entity operates becomes highly inflationary, the entity must change its functional currency from the local currency to its parent’s reporting currency (e.g., the US dollar). In addition, regardless of whether the economy is highly inflationary, an entity may switch its functional currency from the local currency to the reporting currency when significant changes in facts and circumstances occur (such that the determination of the functional currency under ASC 830 is affected). When the reporting currency is the functional currency, ASC 830-10-45-18 requires that historical exchange rates be used to remeasure non-monetary assets and liabilities from the local currency into the reporting currency and therefore the exception in ASC 740-10-25-3(f) applies.

ASC 830-10-45-10 states that “[i]f the functional currency changes from a foreign currency to the reporting currency, translation adjustments for prior periods shall not be removed from equity and the translated amounts for non-monetary assets at the end of the prior period become the accounting basis for those assets in the period of the change and subsequent periods.”

In this case, because the pre-tax carrying amounts of the subsidiary’s assets and liabilities do not change when the functional currency changes, temporary differences also do not change. Therefore, the subsidiary’s deferred tax assets (“DTA”) and deferred tax liabilities (“DTL”) should not be adjusted on the date the functional currency changes.

However, the guidance in ASC 740-10-25-3(f) would be applied prospectively from the date of the change. Therefore, after the functional currency is changed to the reporting currency, the exception applies and the local-currency-equivalent amount of the financial reporting carrying value (for use in determining the temporary difference) is measured by using the historical exchange rates as of the date of the change in the functional currency (even though the resulting local-currency amount differs from the amount that an entity needs to recover the reporting-currency carrying value of the asset or liability).

In addition, an entity would continue to recognize deferred taxes for (1) differences related to the effects of exchange rate changes associated with reporting-currency-denominated monetary assets and liabilities and (2) other differences (excluding the effects of indexing, which are discussed below) between the local-currency financial reporting carrying value and local-currency tax basis of non-monetary assets (e.g., differences arising when a non-monetary asset is depreciated over different periods for book and tax purposes).

Further, certain countries (especially those that are considered highly inflationary) permit the tax basis of assets to be indexed. ASC 830-10-45-16 states:

> Deferred tax benefits attributable to any such indexing that occurs after the change in functional currency to the reporting currency shall be recognized when realized on the tax return and not before. Deferred tax benefits that were recognized for indexing before the change in functional currency to the reporting currency are eliminated when the related indexed amounts shall be realized as deductions for tax purposes.

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1 See ASC 830-10-45-11 through 45-13 for guidance on determining whether an economy is considered highly inflationary.
Therefore, deferred tax effects (either a reduced DTL or a DTA) that were recognized as a result of indexing before the change in functional currency to the reporting currency are not derecognized. Rather, such effects reverse over time as those benefits are realized on the tax return (i.e., previously recognized DTAs should not be reversed when the functional currency is changed to the reporting currency). Going forward, no new DTAs should be recognized for the effects of indexing that occur after the change in the functional currency.\(^2\)

Because the effects of indexing are ignored for deferred tax accounting purposes when the reporting currency is the functional currency, the current-year tax depreciation of indexation not recognized under ASC 740 (i.e., any indexation after the reporting currency became the functional currency) will result in a favorable permanent difference. Therefore, the excess tax depreciation (due to unrecognized indexing) will result in a lower effective tax rate in the year in which it is realized on the entity’s tax return. The prohibition in ASC 740-10-25-3(f) causes the timing of recognizing the tax benefit related to indexing to shift from the period in which the indexing occurs to the period in which the additional tax basis is depreciated or amortized (even when the resulting deduction increases an NOL carryforward).

Please see A Roadmap to Accounting for Income Taxes 2017, Section 12.04 Deferred Income Tax Effects When the Functional Currency Changes from the Local Currency to the Reporting Currency for additional details.

Multistate tax considerations associated with IRC section 163(j) and Notice 2018-28

The provisions of the Tax Act replaced current IRC section 163(j) with a new rule that potentially limits the deduction for business interest expense. On April 2, 2018, the Internal Revenue Service issued Notice 2018-28 with respect to the new business interest expense limitations. The new IRC section 163(j) creates additional complexity for taxpayers in determining their state income tax liabilities. As set forth in Section 5 of the Notice, it is anticipated that to-be-issued temporary regulations will, consistent with the legislative history, clarify that the limitation under the new IRC section 163(j) applies at the consolidated group level, and that the regulations will not include a general rule treating an affiliated group that does not file a consolidated return as a single taxpayer for purposes of new IRC section 163(j).

Implications will vary based on filing methodology applicable in the state. The clarifications in the Notice will likely have a direct impact in determining the new IRC section 163(j) limit in state tax jurisdictions which require entities to file separate income tax returns.

For additional details, please see the Multistate Tax Alert dated June 26, 2018.

Accounting Developments

FASB releases targeted improvements to ASC 842

On July 30, 2018, the FASB issued ASU 2018-11 to provide entities with relief from the costs of implementing certain aspects of the new leasing standard, ASU 2016-02 (codified as ASC 842, Leases). The ASU addresses two issues—transition relief related to presentation of comparative periods post adoption (“Issue 1”) and lessor relief related to separation of lease and non-lease components (“Issue 2”).

\(^2\) Since the exception only applies to deferred tax accounting, the current tax benefit related to the depreciation or amortization of the tax basis from indexation should be recognized.
Effective date and transition

The transition relief amendments (Issue 1) in the ASU apply to entities that have not yet adopted ASC 842. Entities that have early adopted ASC 842 cannot elect the transition relief amendments in this ASU.

For entities that have not yet adopted ASU 2016-02, the effective date of the lessor relief practical expedient (Issue 2) is aligned with the new leasing standard’s effective date and transition requirements. Entities that early adopted ASU 2016-02 before the issuance of ASU 2018-11 may apply the lessor practical expedient to all new and existing leases either retrospectively or prospectively.

In addition, ASU 2018-10 (issued on July 19, 2018) makes narrow-scope amendments (i.e., minor changes and clarifications) to certain aspects of the new leasing standard.

Entities that expect impacts to income tax accounting as a result of adoption of ASC 842 should determine if ASUs 2018-10 and 2018-11 will affect the entity’s adoption method and timeline, and plan for changes to the entity’s income tax accounting and reporting, accordingly.

For more information on ASU 2018-10 and ASU 2018-11, please refer to Deloitte’s Heads Up dated August 7, 2018.

Accounting Standards Update Number 2018-09—Codification Improvements

ASU 2018-09 was issued on July 16, 2018 and provides changes to clarify the Codification, correct unintended application of guidance, or make minor improvements to the Codification. Interested parties should review the entire document to assess any effects that the amendments in this Update may have on entities that are within the Update’s scope. However, a summary of some of the improvements that should be considered for purposes of applying ASC 740 is provided below:

- **Amendments to Subtopic 718-740, Compensation—Stock Compensation—Income Taxes**
  The amendments in Accounting Standards Update No. 2016-09, Compensation—Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting, require that all excess tax benefits and tax deficiencies be recognized as income tax expense or benefit in the income statement. In addition, the amendments require that an entity recognize an excess tax benefit even if the entity cannot use the deduction to reduce taxes payable in the current period (for example, when an entity has a net operating loss).

  Some stakeholders noted that the guidance in paragraph 718-740-35-2 is not clear about whether an entity should recognize excess tax benefits (or tax deficiencies) in its income statement in the period when the amount of the tax deduction is determined or in the period when the tax deduction is taken on the entity’s tax return. The amendments clarify that an entity should recognize excess tax benefits (or tax deficiencies) in the period when the amount of the tax deduction is determined, which typically is when an award is exercised, in the case of share options, or vests, in the case of non-vested stock awards.

- **Amendments to Subtopic 805-740, Business Combinations—Income Taxes**
  This amendment removes the guidance in Subtopic 805-740 that provides three methods for allocating the consolidated tax provision to an acquired entity after acquisition. The guidance originated in EITF Issue No. 86-9, IRC Section 338 and Push-Down Accounting, which was issued in March 1986 and described a narrow fact pattern in which an entity was acquired and pushdown accounting was not elected.
After Issue 86-9 was issued, the accounting for the tax effect from a change in tax basis from all transactions with or among shareholders was addressed in EITF Issue No. 94-10, *Accounting by a Company for the Income Tax Effects of Transactions among or with Its Shareholders under FASB Statement No. 109*. Issue 94-10, now codified in Topic 740, specifically included the scenario described in Issue 86-9, namely, that an investor purchasing 100 percent of the outstanding stock of a company in a transaction treated as a purchase of assets for tax purposes chooses not to “push down” the purchase price for financial reporting purposes. The decision in Issue 94-10 was not consistent with the decision in Issue 86-9. Specifically, Issue 94-10 stated that the consequences of all temporary tax differences should be recognized through net income or adjustments to equity, not as permanent differences.

Furthermore, the guidance in Topic 740 requires an entity to adopt a tax allocation approach that is systematic, rational, and consistent with the broad principles established by the Topic when allocating the consolidated tax expense to separate financial statements of members of a consolidated entity. The guidance in paragraph 805-740-25-13 does not support those general principles and is no longer relevant given the overall principles in Topic 740. Removing the allocation methods in paragraph 805-740-25-13 simplifies the Codification and helps to ensure that the principles in Topic 740 are applied consistently.

- **Amendments to Subtopic 740-10, Income Taxes—Overall**
  Paragraph 740-10-25-3(e) was amended in Accounting Standards Update No. 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory*, to limit the scope of the paragraph to only the intra-entity transfers of inventory. As a result, intra-entity transfers of assets such as property, plant, and equipment and intellectual property no longer are subject to the prohibition on the recognition of income tax consequences. Stakeholders informed the FASB that the tax laws that created the need for the guidance in paragraph 740-10-25-55 were, and continue to be, applicable only to certain fixed and intangible assets.

  Therefore, the guidance in paragraph 740-10-25-55 and its related pending content, which now only references intra-entity transfers of inventory, describes a null set of transactions and is no longer relevant. The amendment to remove the reference to an intra-entity transfer of inventory from the example about transactions between a taxpayer and a government also is being made for the same reason.

**Learn More**

**REMINDER: Tax Act signed into law**
Deloitte has issued Financial Reporting Alert 18-1—Frequently Asked Questions About Tax Reform (Updated August 30, 2018), which contains responses to frequently asked questions (FAQs) about how an entity should account for the tax effects of the Tax Act in accordance with ASC 740. While the answers to the FAQs reflect both our views and the views expressed by the FASB at various, meetings, these views are subject to change on the basis of additional input received or further developments in practice. We also plan to frequently update this document to reflect developments as they occur and as additional questions surface.

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A Roadmap to Accounting for Income Taxes

The 2017 edition of A Roadmap to Accounting for Income Taxes was released on December 18, 2017. This Roadmap provides Deloitte’s insights into and interpretations of the income tax accounting guidance in ASC 740 and IFRS. Throughout the Roadmap, new guidance has been added, examples related to some of the guidance included in the previous edition have been added or substantively revised, and minor edits have been made to existing guidance to improve its clarity. This edition does not include updates related to tax legislation that had not been enacted before this edition was published. Updated guidance addressing the impact of the tax legislation’s provisions on the accounting for income taxes under ASC 740 will be included in a subsequent edition.

We hope that you find our Roadmap useful and informative.

Additional resources you may find helpful

- Accounting for Income Taxes—Quarterly Hot Topics Archive
- Tax Reform Insights
- Deloitte Tax Accounting & Provision Services Home Page
- Deloitte Tax Accounting & Provisions Dbriefs Webcasts Series
- Deloitte Heads Up Newsletter Archive
- Global Tax Developments Quarterly—Accounting for Income Taxes

As always, we are interested in your comments on our publications. Please take a moment to tell us what you think by sending us an e-mail.

Talk to us

If you have any questions or comments about the ASC 740 implications described above or other content of Accounting for Income Taxes Quarterly Hot Topics, contact the Deloitte Washington National Tax Accounting for Income Taxes Group at: USNationalWNTActIncomeTaxesGrp@deloitte.com