

Enacted Indiana legislation provides for IRC conformity update, decouples from new IRC Section 163(j) and expands DRD

Overview

On May 14, 2018, Indiana Governor Eric Holcomb signed House Bill 1316(ss),¹ which amended Indiana's tax laws in response to the 2017 Tax Reform Act² (the Act). H.B. 1316(ss) includes the following notable amendments:

- Effective retroactive to January 1, 2018, updates the Internal Revenue Code (IRC) conformity date to February 11, 2018 for both individual and corporate income tax purposes.
- For tax years beginning after 12/25/2016, requires deemed repatriation income under IRC Section 965(a) to be added back for corporate income tax purposes and requires the deduction under IRC Section 965(c) to be added back for individual income tax purposes.
- Expands the foreign source dividend deduction for corporate income tax purposes to include income associated with IRC Section 965 and IRC Section 951A for taxable years after December 25, 2016.
- Prescribes rules for the treatment of receipts in apportionment for IRC Section 965 and IRC Section 951A for taxable years beginning after December 25, 2016.
- Effective retroactive to January 1, 2018, decouples from IRC Section 163(j) interest limitations rules.
- Effective retroactive to January 1, 2018, updates the Indiana Net Operating Loss (NOL) carryforward period from being tied to IRC Section 172(b) to being limited to a 20 year carryforward period.

This tax alert summarizes the more significant provision of the tax amendments provided by H.B. 1316(ss) and provides some taxpayer considerations.

IRC conformity update and decoupling from certain provisions of the Federal Tax Reform Act

Effective retroactive to January 1, 2018, H.B. 1316(ss) updates the IRC conformity date to February 11, 2018 for both corporate and individual income tax purposes.³

Corporate income tax conformity amendments

IRC Section 965 (deemed repatriation) addback required for taxable years beginning after December 25, 2016.

While Indiana conforms to the IRC as of February 11, 2018, retroactive to January 1, 2018, there are provisions in the statute that require the IRC Section 965(a) deemed repatriation income to be added back to Indiana adjusted gross income for corporations for taxable years beginning after December 25, 2016. A corporation, other than a real estate investment trusts (REITs), must add back an amount equal to the amount reported for the IRC Section 965(a) per the Transition Tax Statement, Line 1.⁴ Special rules are applicable to REITs, which must add back the amount of the deduction allowed under IRC Section 965(c), but only to the extent that the taxpayer included income from IRC Section 965 in its taxable income or is required to add back dividends paid (for a captive REIT).⁵

GILTI deduction addback

By updating Indiana's IRC conformity date to February 11, 2018, retroactive to January 1, 2018, Indiana conforms to the IRC Section 951A global intangible low-taxed income (GILTI) inclusion in the starting point of taxable income. However,

¹ A copy of H.B. 1316(ss) is available [here](#).

² Pub. L. 115-97, 131 Stat. 2054 (Dec. 22, 2017).

³ IC 6-3-1-11; H.B. 1316(ss), Section 3.

⁴ H.B. 1316(ss), Section 2(b)(13).

⁵ IC 6-3-1-3.5(b)(13); H.B. 1316(ss), Section 2(b)(13).

Indiana requires an addback for the deduction that was claimed by the taxpayer under IRC Section 250(a)(1)(B) for GILTI.⁶ (Note that the deduction allowed by Section 250(a)(1)(A) (FDII) would be allowed in the calculation of Indiana taxable income.) Also, as described below, the definition of “foreign source dividend” qualifying for the dividend received deduction (DRD) was expanded to include GILTI.⁷

Nonconformity to interest expense limitation under IRC Section 163(j)

The new federal interest deductibility limitations provided by IRC Section 163(j), as amended by the Act, are specifically excluded from the calculation of Indiana taxable income under H.B. 1316(ss).⁸ The federal amendments to IRC Section 163(j) generally limit the deductibility of interest to no more than net interest income plus 30% of adjusted taxable income and certain floorplan interest, and allow a carryforward of limited business interest.⁹ As such, H.B. 1316(ss) retains conformity to the pre-Act version of IRC Section 163(j) for Indiana purposes.

Directly related interest expenses (intercompany interest addback) in conjunction with IRC Section 163(j) decoupling

H.B. 1316(ss) also provides that any directly related interest expense (intercompany interest addback) required to be added back under IC 6-3-2-20 must still be added back to the Indiana adjusted gross income. Since Indiana does not conform to the federal interest expense limitation, the amount of the interest addback may need to be modified to consider the adjustments that were necessary under 6-3-1-3.5(15).¹⁰

IRC Section 118 contributions to capital

H.B. 1316(ss) decouples from the Act’s amendments to the contribution to corporate capital rules under IRC Section 118. Historically, IRC Section 118 excluded contributions to the capital of a corporation from the corporation’s gross income.¹¹ The amendments to IRC Section 118, however, provide that certain contributions by customers and potential customers and certain contributions by government entities or civic groups to a corporate are not considered contribution[s] to the capital of the taxpayer, and thus would be includable in the corporation’s gross income.¹² Similar to the state’s treatment of IRC Section 163(j), H.B. 1316(ss) retains conformity to IRC Section 118 for Indiana purposes as it existed *prior* to the enactment of the Act.¹³

Foreign sourced dividends deduction expanded

Indiana has traditionally allowed a deduction for Subpart F income and will continue to allow that deduction under H.B. 1316(ss) for IRC Section 965(a) foreign income that qualifies as Subpart F income under the IRC.¹⁴ H.B. 1316(ss) expanded the definition of “foreign source dividend” qualifying for the DRD to include both IRC Section 951 (effective for years beginning after December 25, 2016) and Section 951A (effective retroactive to January 1, 2018), thereby allowing a dividends received deduction for the GILTI inclusion. A 2014 decision of the Indiana Supreme Court held that a taxpayer may not deduct a foreign source dividend when calculating its Indiana net operating loss. A DRD may not cause a NOL or increase an NOL. Therefore, a DRD is only available to reduce adjusted gross income to the maximum of the DRD or reduce AGI to zero.

Apportionment amendments

H.B. 1316(ss) addresses how both the Section 965(a) deemed repatriation income (effective for years beginning after December 25, 2016) and GILTI (effective retroactive to January 1, 2018) will be reflected in the receipts factor for apportionment.¹⁵

Net dividends included in taxable income under IRC Section 965(a) and IRC Section 951A GILTI, after reduction for applicable DRDs, are considered dividends from investments for apportionment purposes.¹⁶ For entities that are eligible to claim a DRD, then the amounts shall be included in the receipts factor in the year reported in gross income after the

⁶ H.B. 1316(ss), Section 2(b)(14).

⁷ H.B. 1316(ss), Section 8.

⁸ IC 6-3-1-3.5(b)(15); H.B. 1316(ss), Section 2(b)(15).

⁹ IRC §163(j)(2).

¹⁰ IC 6-3-1-3.5((b)(8); H.B. 1316(ss), Section 2(b)(15).

¹¹ IRC §118(a).

¹² IRC §118(b).

¹³ IC 6-3-1-3.5(b)(16) H.B. 1316(ss), Section 2(b)(16).

¹⁴ IC 6-3-2-12(1); H.B. 1313(ss), Section 8.

¹⁵ IC 6-3-2-2.

¹⁶ IC 6-2-2-2(t), H.B. 1316(ss), Section 4.

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reduction for applicable DRDs.¹⁷ Generally, dividends from investments are sourced to the taxpayer's commercial domicile.¹⁸

For entities that are not eligible to claim a DRD, the deemed repatriation and GILTI inclusions shall not be considered receipts.

Net Operating Loss Carryforward clarification

H.B. 1316(ss) decouples Indiana's NOL carryforward rules from the amendments in the Act. For Indiana purposes, net operating losses are to be carried forward no longer than twenty years after the year of the taxable loss.¹⁹ There are also no limitations as to the amount of NOL that can be used in a given year, unlike the new federal rules that limit NOL usage to 80% of taxable income.

Individual income tax conformity amendments

As previously noted, effective retroactive to January 1, 2018, H.B. 1316(ss) updates the IRC conformity date to February 11, 2018 for individual income tax purposes as well.²⁰ However, for taxable years beginning after December 25, 2016, H.B. 1316(ss) requires individual taxpayers to addback "an amount equal to the deduction for deferred foreign income that was claimed by the taxpayer for the taxable year under Section 965(c) of the [IRC]."²¹ It should also be noted that Indiana does not provide an exclusion for foreign dividends for individual income tax purposes.²²

Similar to the corporate income tax amendments, H.B. 1316(ss) retains conformity to the pre-Act version of IRC Section 163(j) for Indiana individual income tax purposes.²³

Penalty & interest relief

H.B. 1316(ss) gives authority to the Indiana Department of Revenue to waive penalties and interest when the general assembly enacts a change in a listed tax for a tax period that increases a taxpayer's liability for that tax after the due date for the tax and tax period.²⁴ These waivers apply only to the extent of the increase in tax liability and only for a period not exceeding sixty days after the change is enacted (i.e., through July 13, 2018).

Considerations

H.B. 1316(ss) results in significant changes to Indiana's corporate adjusted gross income tax, most notably updating the IRC conformity to February 11, 2018, decoupling from the interest deductibility limitations under IRC Section 163(j), addbacks for deemed repatriation and GILTI income and amending the apportionment factor. Individual taxpayers are potentially impacted as well by the changes provided by H.B. 1316(ss). Taxpayers potentially impacted by the enactment of these laws should consult with their Indiana tax advisors for further assistance.

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¹⁷ H.B. 1316(ss), Section 4(t). Further consideration should be given to the receipts included when the DRD is limited to the amount of taxable income or when no DRD is allowed due to a net operating loss in the current year.

¹⁸ IC 6-3-2-2(j).

¹⁹ IC 6-3-2-2.6(f); H.B. 1316(ss) Section 5.

²⁰ IC 6-3-1-11; H.B. 1316(ss), Section 3.

²¹ IC 6-3-1-3.5(a)(23), H.B. 1316(ss), Section 2. Uncertainty exists regarding the implications of this new addition modification, though further analysis is beyond the scope of this alert.

²² IC 6-3-2-12.

²³ IC 6-3-1-3.5(a)(24), H.B. 1316(ss), Section 2.

²⁴ IC 6-8.1-3-17(d)(3)(3), H.B. 1316(ss) Section 13.

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