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Tax

Tax News & Views

Capitol Hill briefing.

February 26, 2016

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Boustany eyes March release of international tax reform legislation

House Ways and Means Committee Republicans hope to release a legislative proposal to overhaul the US international tax rules by the end of March, Tax Policy Subcommittee Chairman Charles Boustany, R-La., said February 24.

Boustany, who has been tasked with taking the lead on developing international reform legislation for the House taxwriting panel, made his comments to reporters immediately after a Ways and Means Committee hearing to consider the global tax environment in 2016 and its implications for international tax reform.

Last summer, Boustany and Ways and Means Committee Democrat Richard Neal of Massachusetts released a draft proposal for an “innovation box” that would provide a lower tax rate on certain C corporation profits related to intellectual property, and it is expected that this year’s bill will include a modified version of that proposal. Other likely elements include a shift from the current worldwide system to a territorial system for taxing foreign-source income of US multinationals, a “deemed repatriation” provision that would tax – at a lower rate than the statutory corporate rate – profits that US multinationals currently hold overseas, and base-erosion safeguards.

Boustany acknowledged earlier in the week that “international tax reform separate from a large comprehensive package” is “unlikely” to become law this year; but Ways and Means Chairman Kevin Brady, R-Texas, has indicated that he views the committee’s work on international reform as “a down payment that clears the way to focus on the work [of] lowering rates and simplifying the tax code for all businesses and individuals, so that we are ready to enact comprehensive tax reform in 2017.”

Congressional Republicans have long advocated comprehensive tax reform but have determined that goal is not feasible while President Obama remains in office. They say

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international reform would be an important first step and is especially urgent in light of the OECD's Base Erosion and Profit Shifting (BEPS) project.

Ways and Means hearing highlights partisan divide

The February 24 Ways and Means Committee hearing on the global tax environment showcased the strong interest of most committee members in the issue of reforming the tax laws for companies operating internationally and stemming the tide of corporate inversions, but it also highlighted the political divide on the appropriate steps Congress should take.

Witnesses at the hearing included Itai Grinberg, an associate professor at the Georgetown University Law Center; Michelle Hanlon, a professor of accounting at the MIT Sloan School of Management; Ed Kleinbard, a professor at the University of Southern California's Gould School of Law and former chief of staff to the congressional Joint Committee on Taxation; and Raymond Wiacek, a partner at Jones Day.

GOP backs corporate rate cut: Republicans – led by Chairman Brady – focused largely on the need for a lower statutory tax rate to make US companies competitive internationally. Brady noted in his opening statement that Congress needs to "permanently lower America's tax gate so that the estimated $2 trillion in stranded US profits can flow back into America to be invested in new jobs, research, and growth."

Democrats propose a different approach: But many Democratic taxwriters argued there is too much incentive in the current code for businesses to relocate or simply keep their overseas profits outside the US, and that Congress should focus on making inversions less attractive.

"More and more of the horses are galloping out of the barn, using a huge loophole," Ways and Means ranking Democrat Sander Levin of Michigan said in his opening statement. "Failure to close the barn door is bad for the American economy and unfair to the typical American taxpayer who can't lower their taxes by simply changing their address to another country with a lower tax rate."

Levin, along with House Budget Committee ranking member Chris Van Hollen, D-Md., introduced legislation on February 23 aimed at curbing corporate inversion transactions by tightening the current earnings stripping rules of section 163(j) for any US company that inverted on or after May 8, 2014, as part of a transaction that resulted in historical shareholders of the former US firm owning between 50 percent and 80 percent of the new foreign parent.

Specifically, the Stop Corporate Inversions Act of 2016 (H.R. 4581) would eliminate the 1.5:1 debt-equity ratio safe harbor, reduce the interest deduction limit from 50 percent to 25 percent of adjusted taxable income, and lower to five years the carryforward period for any disallowed deductions. (Section 163(j) otherwise permits an indefinite carryforward period for disallowed deductions). Companies subject to the law also would be barred from carrying forward excess limitation amounts.

Levin also introduced legislation (H.R. 415) last year that would tighten the anti-inversion rules in section 7874 for transactions completed after May 8, 2014, by denying foreign status to

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inverted firms that continue to be majority-owned by the historical shareholders of the former US firm or that, regardless of ownership, continue to be managed and controlled from within the US.

Neither bill is expected to be taken up by the Republican-controlled House.

Concerns about piecemeal reform: Levin and several other Democrats at the hearing also cited recent comments by Doug Oberhelman, the new chairman of the Business Roundtable (BRT), who told reporters earlier this month that the BRT does not support moving international tax reform legislation on its own.

Oberhelman argued that for tax reform to be successful, "[y]ou've got to have revenue on the table. You've got to have lower tax rates on the table, simplification. And you play with all of this at the same time to get something that's going to be a compromise for all."

Although Ways and Means Democratic members did not endorse the BRT's call for a significant corporate rate cut, they did echo Oberhelman's opposition to "piecemeal" legislation.

Hatch: Corporate integration offers potential interim fix

On the other side of the Capitol, Senate Finance Committee Chairman Orrin Hatch, R-Utah, continued to focus on the development of a corporate integration proposal that would end the double taxation of corporate dividends – a change he says would "significantly reduce effective corporate tax rates without all the difficult and highly politicized tradeoffs that will accompany a reduction in the statutory corporate tax rate" and deter inversions and foreign takeovers of US firms.

In remarks delivered at a Bloomberg BNA tax policy event on February 24, Hatch explained that his proposal – the details of which he "is still working out" – could complement the efforts currently underway at Ways and Means.

"One of the best features of a potential integration proposal is that, while it would have significant positive effects on its own, it does not prejudice or limit our ability to enact other reforms," Hatch said. "We could pass a stand-alone integration bill to quickly address immediate problems. Or, as Chairman Brady recently said, it could be enacted to complement a broader international tax reform package. It could also eventually be included as part of a comprehensive tax reform bill, once we get to that point."

Hatch indicated that he will "have much more to say about" his approach to corporate integration "in the near future."

Wyden planning anti-inversion legislation: For his part, Finance Committee ranking Democrat Ron Wyden of Oregon told the audience at a Brookings Institution event on February 25 that he is working on his own proposal "to crack down on inversions and tax games to preserve our tax base for broader reform."

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Wyden did not say when his proposal would be introduced, but noted that action to address inversion transactions cannot wait until Congress undertakes fundamental tax reform in 2017.

"It's vital that Congress triage the inversion virus and the rampant tax gaming to defend against base erosion," Wyden said.

Wyden had vowed to move anti-inversion legislation when he chaired the Senate Finance Committee in 2014, but did not introduce a proposal or hold a committee mark-up.

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Permanent Internet tax moratorium, increased failure-to-file penalty become law

President Obama on February 24 signed into law a Customs overhaul and trade enforcement bill that includes provisions to permanently extend the moratorium on state and local taxes on Internet access service and increase the penalty for failure to file a tax return more than 60 days after its due date. The Trade Facilitation and Enforcement Act of 2015 (H.R. 644) was approved in the Senate on February 11 and cleared the House late last year.

Internet tax moratorium

The Internet tax moratorium – known officially as the Internet Tax Freedom Act (ITFA) – was originally enacted as a temporary measure in 1998 and received multiple short- and long-term extensions in the intervening years. The original moratorium included a grandfather clause to give states that were then taxing Internet access some time to transition to other sources of revenue. To date, most of the originally grandfathered states have discontinued taxing Internet access. H.R. 644, as enacted, requires any remaining state-imposed Internet access taxes to be phased out by June 30, 2020.

Remote sales provisions not included: The new law does not include provisions from the Marketplace Fairness Act (MFA) which are intended to make it easier for states to capture sales and use tax revenue from transactions involving on-line and other "remote" vendors that do not have an in-state physical presence. Disagreements over linking a permanent Internet tax moratorium with provisions to tax remote sales had in the past stymied efforts to move a permanent extension of the ITFA through the Senate. MFA supporters blocked Senate floor consideration of H.R. 644 last December by threatening to raise a point of order to strike the ITFA language from the underlying Customs legislation. They eventually dropped their objections, clearing the way for Senate passage of H.R. 644, after Majority Leader Mitch McConnell, R-Ky., promised that he would hold a floor vote on the Marketplace Fairness Act later this year.

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Increased failure-to-file penalty

H.R. 644 also includes a revenue provision that increases the penalty for failure to file a tax return more than 60 days after its due date to the lesser of $205 or 100 percent of the amount required to be shown as tax on the return (from $135 or 100 percent of the amount required to be shown as tax on the return under current law). The provision is effective for returns required to be filed in calendar years after 2015.

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