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Paycheck Protection Program enhancement bill clears Senate, heads to White House

The Senate on June 3 approved by unanimous consent a bipartisan proposal that would expand the loan forgiveness rules and make other enhancements to the Paycheck Protection Program, which was enacted in March as part of the Coronavirus Aid, Relief, and Economic Security (CARES) Act (P.L. 116-136).

The Paycheck Protection Program Flexibility Act of 2020 (H.R. 7010), which cleared the House of Representatives on May 28 by a vote of 417-1, now heads to the White House, where President Trump is expected to sign it into law.
URL: https://docs.house.gov/billsthisweek/20200525/BILLS-116hr7010-SUS.pdf

Paycheck Protection Flexibility Act: Key provisions

As enacted in the CARES Act, the Paycheck Protection Program (PPP) makes loans available to most businesses with fewer than 500 employees and to hospitality industry businesses with fewer than 500 employees per location. The loans are intended to be used largely for payroll, as well as for nonpayroll business expenses such as rent, utilities, and certain other expenses. The PPP is scheduled to expire on June 30, unless there is congressional action to extend or expand the program. Unofficial estimates suggest that roughly $130 billion in PPP funds have not yet been allocated.

H.R. 7010 generally would make the PPP more flexible for borrowers by extending current-law deadlines and loan terms, adjusting limitations imposed by the Small Business Administration (SBA) on the percentage of loan proceeds that borrowers can use to cover nonpayroll expenses, and rescinding restrictions that prevented borrowers under the program from also taking advantage of certain other CARES Act tax incentives, such as payroll tax deferral.

The provisions in the bill would take effect retroactively, as if they had originally been enacted in the CARES Act, which was signed into law on March 27.

Covered loan period: The CARES Act provides that the "covered period" under the PPP's loan forgiveness rules applies to expenses incurred within eight weeks after the loan origination date, a limitation that some businesses, as well as lawmakers in both parties, came to regard as impractical once the program was up and running.

H.R. 7010 would extend the covered period to include expenses incurred through the earlier of December 31, 2020, or 24 weeks after the loan origination date. Borrowers that received a PPP loan before the legislation's enactment date would be permitted, at their election, to continue using the 8-week covered loan period originally included in the CARES Act.

Limitations on payroll v. nonpayroll expenses: The bill would modify restrictions imposed in regulations issued by the Treasury Department and SBA implementing the Paycheck Protection Program which provide that a loan is forgivable if an employer spends no more than 25 percent of PPP loan proceeds on nonpayroll business expenses.

Lawmakers in both parties – along with a number of business groups – have cited that limitation as a source of concern, and a bipartisan group of Senate members – including several taxwriters – recently urged Treasury and the SBA to modify the cap, calling it "problematic for several business sectors, especially those whose mortgage, rent, or utility payments constitute a large portion of fixed monthly expenses." (For prior coverage, see *Tax News & Views*, Vol. 21, No. 25, May 8, 2020.)
URL: https://www.menendez.senate.gov/imo/media/doc/PPP%20forgiveness%20letter_final_.pdf
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200508_1.html

Under H.R. 7010 as approved, borrowers would be able to spend up to 40 percent of their loan proceeds on nonpayroll business costs and remain eligible for loan forgiveness.

Interaction with payroll tax deferral: The measure provides that employers participating in the PPP would also be permitted take advantage of the CARES Act's payroll tax deferral provisions.

Under the CARES Act, employers (and self-employed individuals) are allowed to defer payment of the 6.2 percent employer-side Social Security payroll tax for wages paid between the date of that bill's enactment and December 31, 2020 (with remittance due in equal installments by December 31, 2021 and December 31, 2022). Though recipients of forgiven PPP loans were generally precluded from also utilizing the payroll tax deferral provision, the IRS clarified on an FAQ page published in April (Question 4) that PPP loan recipients can, in fact, defer payment on wages paid up until the point of loan forgiveness, but not beyond that date.
URL: https://www.irs.gov/newsroom/deferral-of-employment-tax-deposits-and-payments-through-december-31-2020

Under H.R. 7010, even recipients of forgiven PPP loans would be able to continue to defer payment of payroll taxes on wages paid through the end of 2020. An identical provision is also included in The Heroes Act (H.R. 6800), the $3 trillion coronavirus response package that was approved in the House on May 15. (The Heroes Act is not expected to pass the Senate without substantial changes and has drawn a veto threat from President Trump. For additional details on that legislation, see *Tax News & Views*, Vol. 21, No. 27, May 15, 2020.)
URL: https://www.congress.gov/bill/116th-congress/house-bill/6800/text?q=%7B%22search%22%3A%5B%22h.r.+6800%22%5D%7D&r=1&s=2
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200515_1.html

Deadline for rehiring employees: As enacted, the CARES Act requires an employer participating in the PPP to rehire employees by June 30, 2020, to be eligible for loan forgiveness. H.R. 7010 would extend that deadline to December

31, 2020. The measure also includes a safe harbor for certain employers that are required to reopen at reduced capacity.

Loan terms: The measure also would eliminate restrictions in the CARES Act that limit the term of non-forgiven PPP loans to two years.

Treatment of 'otherwise deductible expenses' not addressed

H.R. 7010 does *not* include a provision to clarify that otherwise deductible business expenses funded with PPP loan proceeds would remain deductible even if the loan is forgiven.

The IRS recently held in Notice 2020-32 that these expenses are not deductible. (For prior coverage, see *Tax News & Views*, Vol. 21, No. 24, May 1, 2020). But some prominent congressional taxwriters, including Senate Finance Committee Chairman Charles Grassley, R-Iowa, and ranking member Ron Wyden, D-Ore., along with House Ways and Means Committee Chairman Richard Neal, D-Mass., subsequently challenged that position in a letter to Treasury Secretary Steven Mnuchin, arguing that it was contrary to congressional intent and urging the Service to reconsider. Grassley, Wyden, and several other Finance Committee members also introduced legislation that would clarify the treatment of these expenses. (For prior coverage, see *Tax News & Views*, Vol. 21, No. 25, May 8, 2020.)
URL: https://www.irs.gov/pub/irs-drop/n-20-32.pdf
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200501_1.html
URL: https://www.finance.senate.gov/imo/media/doc/2020-05-05%20CEG,%20RW,%20RN%20to%20Treasury%20(PPP%20Business%20Deductions).pdf
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200508_1.html

The House-passed Heroes Act also would clarify the deductibility of these expenses and would expand the list of expenses that can give rise to PPP loan forgiveness to include certain interest on debts incurred prior to the covered period of PPP and costs related to providing personal protective equipment to employees.

Senate Republican leaders this week "hotlined" a bill (S. 3612) from Finance Committee member John Cornyn, R-Texas, that provides that these expenses would be deductible, but that effort ran into unspecified objections from a few GOP senators. ("Hotlining" is an informal process that leaders can use to gauge member support for proposals that they want to move under expedited unanimous consent rules, which provide that a unanimous consent request is defeated if a single senator raises an objection.)

In the Senate, no objections but some 'concerns'

Although no senators ultimately objected to approving H.R. 7010 under unanimous consent, some cited potential problems with the measure before it reached the floor.

Small Business Committee Chairman Marco Rubio, R-Fla., and Sen. Susan Collins, R-Maine, contended that the bill was drafted in a way that would result in a business losing any chance of loan forgiveness if it did not spend at least 60 percent of its PPP loan proceeds on payroll expenses.

In a written statement, Collins said the House bill creates a "cliff," explaining that "[t]he current PPP program allows partial loan forgiveness if a company uses less than 75 percent of a loan for payroll, but the House bill appears to state that none of the loan would be forgiven if the 60 percent threshold isn't met. Instead, the employer is saddled with a debt for the entire amount, and no portion of the loan is forgiven or converted to a grant."

Rubio reportedly has contacted the Treasury Department to see if it can provide an administrative remedy to what he has called "inadvertent technical errors that could create unintended consequences for small businesses as they seek forgiveness." He noted in a statement on June 3 that if Treasury cannot address the issue, Congress will need to provide a legislative fix.

For their part, Republican Sens. Mike Lee of Utah and Ron Johnson of Wisconsin argued that the bill's language could be construed as extending the application period for a PPP loan through December 31 instead of simply extending the covered period for using PPP loan proceeds. A spokesperson from Lee's office said in a written statement that the senator agreed to support the bill after he "secured a letter signed by the chairmen and ranking members of the Small

Business Committee…clarifying that the amendments to the Paycheck Protection Program…only extend the program's spending deadlines and do not extend the deadline for the issuance of new loans."

That development also satisfied Johnson, who told reporters June 3 that "[w]e don't want to see this program automatically reauthorized until the end of December. Now there's some dispute as to whether the language actually does that. Sounds like the intent was not to do that, it was just to allow people to spend money through the end of December, which we have no problem with."

McConnell: Larger package still weeks away

In other developments, Senate Majority Leader Mitch McConnell, R-Ky., has continued to maintain that work on another large-scale coronavirus mitigation and response package will not begin in earnest for another few weeks; but he did make some news when he told reporters in Kentucky recently that he envisions the next such bill will be the last one to move through Congress.

"We're taking a careful look at a fourth and final bill," McConnell said May 29. "You can anticipate the decision being made on whether to go forward in about a month."

McConnell has said in recent weeks that he intends to gauge the effects of the recovery bills that have been enacted to date before taking up substantial new legislation.

But the majority leader still has revealed little about the specific contents of the next recovery bill, other than to say it should be narrowly targeted, have a price tag of roughly $1 trillion – significantly less than the House's Heroes Act, which the Congressional Budget Office recently estimated would cost nearly $3.5 trillion over 10 years – and include liability protections for health care workers, business owners, and employees as the country emerges from its lockdown over the coming weeks and months. (In remarks on the Senate floor last month, McConnell called liability protections "a hard red line.")
URL: https://www.cbo.gov/system/files/2020-06/56383-HR6800.pdf

McConnell also has indicated that he will not accept Democratic proposals to extend the CARES Act's enhanced unemployment insurance benefits without significant changes. Some congressional Republicans – including Senate Finance Committee member Rob Portman, R-Ohio, and House Ways and Means Committee ranking member Kevin Brady, R-Texas – are floating alternatives that would provide temporary back-to-work bonus payments to unemployed individuals who return to the workforce.

White House economic advisor Larry Kudlow recently told reporters that a back-to-work bonus is "something [the Trump administration is] looking at very carefully."

The administration has agreed with Majority Leader McConnell's position that another coronavirus mitigation package should wait until policymakers can measure the economic impact of previous legislative efforts. Although the White House has not released a formal list of tax provisions it would like to see in the next bill, officials are said to be considering, among other things, an employer-side payroll tax holiday, a reduction in the capital gains tax rate, and incentives to encourage individuals to travel and entertain in the US.

Coronavirus guidance update

On the guidance front, the Internal Revenue Service this week provided pandemic-related relief for Qualified Opportunity Funds (QOFs) and investors, retirement plan participants and beneficiaries, and certain trusts that hold real property.

Qualified Opportunity Funds: Notice 2020-39, issued on June 4, extends the deadline for certain taxpayers who sold property for an eligible gain to invest in a QOF and defer that gain; provides relief for certain failures by a QOF to meet the 90-percent investment standard and postpones the time periods for satisfying certain other requirements; and confirms that both the 24-month extension for the working capital safe harbor and the 12-month extension for QOFs to reinvest certain proceeds are available to otherwise qualifying QOFs and qualified Opportunity Zone businesses.
URL: https://www.irs.gov/pub/irs-drop/n-20-39.pdf

Retirement plans: Notice 2020-42, issued on June 3, temporarily allows retirement plan participants or beneficiaries who are making elections that must be witnessed in the physical presence of a plan representative or notary public to instead provide a remote signature using live audio-video technology as long as certain conditions are met. The relief is available through December 31. The Service explained that the guidance accommodates local shutdowns and social distancing practices and is intended to facilitate the payment of emergency coronavirus-related distributions and plan loans to qualified individuals, as permitted by the CARES Act.
URL: https://www.irs.gov/pub/irs-drop/n-20-42.pdf

Trusts holding real property: Rev. Proc. 2020-34, issued June 4, provides temporary safe harbors for determining the tax status of certain trusts that hold real property in cases where there is a COVID-related modification to or forbearance on a mortgage that secures the trust's real property or COVID-related modifications to a lease connected to real property held by the trust.
URL: https://www.irs.gov/pub/irs-drop/rp-20-34.pdf

Find out more: A running list of guidance and other resources that address significant tax issues stemming from the pandemic is available from Deloitte Tax LLP.
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/Stimulus-Resource-Table.pdf

— Michael DeHoff
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CBO: Coronavirus impact on economy will approach $16 trillion over next decade

The nonpartisan Congressional Budget Office (CBO) this week projected that by 2030, nominal gross domestic product (GDP) will be about $15.7 trillion lower on a cumulative basis than what it had estimated this past January in a report that predated the coronavirus pandemic's impact on the US economy.

A big hit to output

CBO's latest analysis – released in the form of a letter to Senate Minority Leader Charles Schumer, D-N.Y., who had requested information on how CBO's economic projections had shifted from its budget and economic outlook released on January 28 and interim numbers it had published on May 19 – notes that in the second quarter of 2020 alone, nominal GDP will be about $790 billion, or 14.2 percent, lower than what the agency projected just five months ago.
URL: https://www.cbo.gov/system/files/2020-06/56376-GDP.pdf
URL: https://www.cbo.gov/publication/56020
URL: https://www.cbo.gov/publication/56351

According to CBO Director Phillip Swagel, who penned the letter, those gaps will narrow over time, falling to $533 billion in the last quarter of this year, and to $181 billion by 2030.

Over the next 10 years, the cumulative drop in economic output amounts to about 5.3 percent of the total GDP the agency had predicted for that time period back in January.

Not surprisingly, Swagel attributes nearly all of the drop-off to the economic effects of the pandemic, offset partly by Congress's legislative response.

"The two largest differences between the two forecasts result from the economic effects of the COVID-19 pandemic in reducing output and the legislation enacted between January and early May in response, which partly offsets that reduction," Swagel wrote.

Inflation expectations marked down: The letter notes that – especially later in the decade – weaker inflation rates, and thus comparatively lower price levels, are a major driver of the decline in nominal GDP. In the near term, lower inflation will derive mainly from the energy, transportation, and travel sectors of the economy.

"Over the first few years of the 2020-2030 period, the revision to estimates of nominal GDP primarily reflects changes in real production, but as the effect of changes in real production wane in later years, the lower price level has an increasing influence," the letter states.

Relatedly, so-called "real" GDP – that is, nominal economic output adjusted for changes in price levels – is projected to be almost $8 trillion, or 3.0 percent, lower on a cumulative basis over the next decade, according to CBO.

Uncertainty abounds: CBO's long-term budget and economic projections are inherently uncertain, even in the best of times, and are especially so now, according to Director Swagel.

"An unusually high degree of uncertainty surrounds these economic projections, particularly because of uncertainty about how the pandemic will unfold this year and next year, how the pandemic and social distancing will affect the economy, [and] how recent policy actions will affect the economy…," Swagel wrote.

"Additionally, if future federal policies differ from those underlying CBO's economic projections – for example, if lawmakers enact additional pandemic-related legislation – then economic outcomes will necessarily differ from those presented here," he continued.

Deficits to spike

CBO's economic projections this week come on the heels of preliminary budget information released on April 24 that shows the federal deficit spiking to $3.7 trillion, or almost 18 percent of GDP, this fiscal year and more than $2 trillion in fiscal 2021, which begins on October 1, 2020, as a result of the several rounds of coronavirus relief legislation enacted thus far as well as impact on revenues and spending from the contracting economy. (For prior coverage, see *Tax News & Views*, Vol. 21, No. 24, May 1, 2020.)
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200501_3.html

Those figures do not factor in the possibility of additional stimulus legislation being enacted later this summer which – based on the fiscal ranges being discussed by both Republicans and Democrats (that is, $1 trillion to $3 trillion) – would add to deficits even further. (See separate coverage in this issue for a discussion of the current debate over the next coronavirus economic response proposal.)

In January, CBO had projected deficits would tally an already-elevated level of about $1 trillion both this year and next.

— Alex Brosseau
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House Democrats unveil massive infrastructure bill

With a September 30 deadline looming to reauthorize the Highway Trust Fund, House Democrats this week rolled out a proposal for a nearly half-trillion-dollar, five-year transportation and infrastructure bill, which also seeks to address climate change and help state and local transportation agencies recover from the coronavirus pandemic that has sapped revenue. Still needed, however, is a funding plan, which has long been a sticking point between Democrats and Republicans and will likely fall under the jurisdiction of the House Ways and Means Committee.

The Investing in a New Vision for the Environment and Surface Transportation (INVEST) in America Act, introduced June 3 by House Transportation and Infrastructure Committee Chairman Peter DeFazio, D-Ore., and subcommittee chairs Eleanor Holmes Norton, D-D.C., and Dan Lipinski, D-Ill., would authorize $494 billion over five years for improvements and building of highways, mass transit systems, and rail systems, as well as for safety measures. To help transportation agencies that have been hit by challenges related to the pandemic and the economic downturn, the bill would delay the implementation of new policies until after the first year, but the increased funding levels would take effect immediately. (A section-by-section summary is available from the Transportation and Infrastructure Committee staff.)

URL: https://transportation.house.gov/imo/media/doc/Final%20Bill%20Text%20of%20the%20INVEST%20in%20America%20Act.pdf
URL: https://transportation.house.gov/imo/media/doc/2020%20INVEST%20in%20America%20Act%20Section-by-Section.pdf

The committee has scheduled a mark-up of the bill for June 17, and DeFazio told reporters June 3 that the measure is tentatively scheduled for a vote on the House floor at the beginning of July.

Of the proposed authorization, $411 billion would come from the Highway Trust Fund (HTF). The bulk of the revenue stream for the HTF comes from excise taxes on gasoline and diesel fuel, and additional revenue is generated from a sales tax on heavy highway vehicles, an annual use tax on heavy vehicles, and an excise tax on heavy-vehicle tires. These taxes are authorized in multi-year surface transportation bills and must be renewed periodically. Spending has outstripped HTF revenue since 2001, and since fiscal year 2008 Congress has supplemented the HTF with transfers from the Treasury General Fund and occasionally has approved discrete revenue-raising provisions in transportation funding bills to address the shortfall.

The current authorization for surface transportation funding (the FAST Act, P.L. 114-94) will expire on September 30 of this year, and the taxes that provide the trust fund's dedicated revenue stream are scheduled to expire on September 30, 2022. The Congressional Budget Office (CBO) projects a shortfall will quickly re-emerge between the HTF and its spending needs: $68.8 billion over the first five years following the FAST Act, and $90.7 billion over the first six years. (The CBO projections are cited in a report from the Congressional Research Service and do not reflect the possible impact on revenues of the economic downturn related to the COVID-19 pandemic.)
URL: https://www.everycrsreport.com/reports/R45350.html

Stumbling over funding

The challenge of raising sufficient revenue is one that Congress has grappled with for years, most recently resulting in the 2019 breakdown of ambitious discussions between Democrats and the White House of a possible $2 trillion infrastructure package. Both parties generally support public-private partnerships but differ sharply on how to encourage these and what the public funding component should look like. While Democrats in recent years have favored retaining and increasing the gas tax, expanding bonds, and creating a national infrastructure bank to provide loans and other investment assistance, Republicans have staunchly opposed a gas tax increase and have focused on easing regulatory hurdles to investment. (For more on the debate over possible funding options, see *Tax News & Views*, Vol. 21, No. 4, Jan. 31, 2020.)
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200131_2.html

In 2018, Senate Democrats also released a proposal to raise $1 trillion in revenue by rolling back some of the tax cuts for the highest income earners from the Republicans' 2017 tax overhaul, as well as increasing the corporate tax rate to 25 percent and taxing carried interest income as ordinary income. The proposal, not surprisingly, was a non-starter with congressional Republicans.
URL: http://newsletters.usdbriefs.com/2018/Tax/TNV/180309_2_suppB.pdf

Ideas that may have more bipartisan interest include tax-preferred bonds and a vehicle-miles-traveled (VMT) tax that would be levied on vehicle owners based on the number of miles actually driven over a specified period of time. The House bill establishes a federal VMT pilot program, but that would likely not generate meaningful revenue in the near term.

Neal weighs in

Ways and Means Committee Chairman Richard Neal, D-Mass., said in January that his committee would not offer a funding proposal until he reached a deal with the White House and Treasury Secretary Steven Mnuchin. During an online event hosted by Tax Analysts June 3, Neal indicated he is eager to advance infrastructure legislation and said he is scheduled to talk to Mnuchin on June 5.

"I intend to raise [my] outline on Friday with him," Neal said, adding that he hopes to reinstate Build America Bonds and expand the New Markets Tax Credit and Historic Tax Credit.

A slow-moving train

In the Senate, meanwhile, it has been nearly a year since the Environment & Public Works (EPW) Committee unanimously passed its America's Transportation Infrastructure Act (S. 2302), which would authorize $287 billion for surface transportation building and maintenance and fund programs that incentivize carbon emissions-reducing projects and alternative fuel infrastructure in the states. (For further details, see *Tax News & Views*, Vol. 20, No. 26, Aug. 1, 2019.) Separately, the Senate Banking Committee, which has jurisdiction over urban mass transit, will draft that title of the bill; the Commerce, Science and Transportation Committee must address safety, rail, and freight; and the Finance Committee will presumably tackle the revenue title.
URL: http://newsletters.usdbriefs.com/2019/Tax/TNV/190802_3.html

EPW Chairman John Barrasso, R-Wyo., said last July that the EPW and Finance staffs would "work together…and come up with the [funding options] that they feel are most viable," but the taxwriting panel has not yet released any proposals or held any hearings on this issue.

House GOP reaction

Reps. Sam Graves, R-Mo., Rodney Davis, R-Ill., and Rick Crawford, R-Ark. – the ranking members of the full House Transportation and Infrastructure Committee, the Highways and Transit Subcommittee, and the Railroads and Pipelines Subcommittee, respectively – issued a joint statement June 3 in response to the release of the INVEST in America Act criticizing the legislation for including "numerous new green mandates and extreme progressive goals" and said they "were not given the opportunity to address any of our priorities."
URL: https://republicans-transportation.house.gov/news/email/show.aspx?ID=FNXSHXRYXUXXCRSIOXFDXPZO3A

In January, Republicans released their infrastructure principles, which included a focus on HTF solvency, core programs, a streamlined regulatory process, and rural infrastructure.
URL: https://republicans-transportation.house.gov/news/documentsingle.aspx?DocumentID=404655

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USTR opens new investigations into digital services taxes

The office of the United States Trade Representative (USTR) this week opened trade investigations into the proposed or enacted digital services taxes (DSTs) of nine countries plus the EU.

The USTR's action builds on its 2019 finding that France's DST is discriminatory towards US companies. After the US threatened retaliatory tariffs in that case, France agreed to hold off on further DST collections until the end of 2020, defusing a trade battle while countries worldwide continue to work through the Organisation for Economic Co-operation and Development (OECD) to revise international tax rules taking into account the digitalization of the economy. However, DSTs have continued to proliferate this year in both proposed and enacted form.

USTR Robert Lighthizer announced June 2 that his office is looking at DSTs that have been adopted or are being considered by Austria, Brazil, the Czech Republic, the EU, India, Indonesia, Italy, Spain, Turkey, and the UK. The investigations will be conducted under section 301 of the 1974 Trade Act, which gives the USTR broad authority to examine and respond to a foreign country's action that may be unfair or discriminatory and may negatively affect US commerce.

"President Trump is concerned that many of our trading partners are adopting tax schemes designed to unfairly target our companies," Lighthizer said. "We are prepared to take all appropriate action to defend our businesses and workers against any such discrimination."

These investigations could lead to the imposition of tariffs on those countries' exports to the US. The Federal Register notice issued by USTR requests comment from stakeholders by July 15.
URL: https://ustr.gov/sites/default/files/enforcement/301Investigations/DST_Initiation_Notice_June_2020.pdf

The USTR conducted a similar investigation last year into the French DST – the first meaningful DST to take effect as countries worldwide have looked to capture what they consider lost revenue from large tech companies – and concluded in December 2019 that the tax discriminated against US companies. As a result, the US announced it would consider tariffs of up to 100 percent on $2.4 trillion in French imports into the US such as wine, cheese, and handbags; but the imposition of such tariffs was held in abeyance when France agreed to delay collection of some estimated taxes this year pending work at the OECD on a global consensus. The deal with France expires in December, and if no global agreement is reached by then, France would be able to collect DSTs for 2020 and the US would be able to move ahead with identifying and imposing tariffs on French goods. (For more details, see *Tax News & Views*, Vol 20, No. 39, Dec. 6, 2019, and *Tax News & Views*, Vol. 21, No. 3, Jan. 24, 2020.)
URL: http://newsletters.usdbriefs.com/2019/Tax/TNV/191206_3.html
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200124_1.html

Another stumbling block for OECD talks?

The USTR's move comes at a delicate time in the OECD project, a two-pronged program of work that comprises a "unified approach" to addressing nexus and profit allocation challenges arising from digitalization (Pillar One) and the development of a global anti-base erosion minimum tax (Pillar Two). The global pandemic upended this spring's schedule of meetings and the original goal of agreement on Pillar One's key policy features in July, but the steering group of the more than 130 countries participating – known as the Inclusive Framework (IF) – will begin meeting virtually the week of June 15. The IF still has a goal of political agreement in 2020, although the target for policy agreement has been pushed to October, ahead of a meeting of the G-20 finance ministers.

There have already been hints that the timeline for Pillar One would slip – Pascal Saint-Amans, director of the OECD's Center for Tax Policy and Administration, said in May that he does not "exclude that we would have a staged process" in which some decisions would shift to next year – and this week's USTR announcement could add to the hurdles. As the COVID-19 pandemic and accompanying business shutdown in most countries has impacted the world's economy, the focus of finance ministers has dramatically changed since earlier this year, and it remains uncertain if and when they will shift attention back to the global tax project. In addition, the proposal by US Treasury Secretary Steven Mnuchin last December that Pillar One should be designed as a "safe harbor" – on which Treasury officials have not elaborated – has not been well received by other countries. (For more details, see *Tax News & Views*, Vol 20, No. 39, Dec. 6, 2019, and *Tax News & Views*, Vol. 21, No. 3, Jan. 24, 2020.)
URL: http://newsletters.usdbriefs.com/2019/Tax/TNV/191206_3.html
URL: https://newsletters.usdbriefs.com/2020/Tax/TNV/200124_1.html

A refined OECD proposal in January broadened the scope of Pillar One beyond "consumer facing businesses," to also include "automated digital services," whether consumer-facing or not (including, for example, cloud-based computing and other digital business-to-business transactions) – so the OECD project has arguably shifted towards a more digital-focused proposal even as the US has argued that the new tax rules should not discriminate against the technology sector.

Speaking at an online event hosted by the University of North Carolina Tax Center and the Tax Policy Center on May 21, Saint-Amans said that while the US opposes "ring-fencing" digital companies, some countries believe "the digital economy has ring-fenced itself" during the COVID-19 crisis because online businesses are perceived to be thriving while much of the brick-and-mortar economy has been at a standstill.

"What seems for sure is that digital is still the focus, not to say the target," he said. "Having something tangible on digital [as part of the OECD agreement] will be highly expected."

Pandemic pressure

The same dynamics that have led to delays in the OECD talks this year may also increase the pressure for international tax action. In early May, French Finance Minister Bruno Le Maire said the health emergency had further advantaged "the digital giants" and that increasing taxes on those businesses is the best solution for countries in need of new revenue. He repeated that sentiment June 3 during an online event with the European Leadership Network, a London-based policy research group.

"We are all aware that the winners of this crisis will be the digital giants," he said. "Nobody could understand that the winners of the crisis could avoid a fair taxation in the countries in which they are making profits."

OECD officials have raised the expectation that other countries may also seek to recoup COVID-related losses through extra taxes on digital companies. Viewed through this prism, this week's USTR announcement can be seen as a warning to countries that want to go down that path.

Engagement in Pillar One negotiations by the US business community and US government has always been premised on the idea that a worldwide agreement was necessary to preclude unilateral measures such as DSTs – and, in fact, they have pushed for specific language that would ensure DSTs are eliminated as part of the agreement. The USTR approach announced this week adds another item to the US toolbox to push back against DSTs, but the use of tariffs in this arena is controversial in the US business community. The DSTs that have been implemented and proposed generally impact digital advertising and intermediation platforms (although India's recently enacted tax is much broader), so some companies and sectors that are not within the scope of the current taxes may be concerned about potential US tariffs that could lead to retaliatory action hitting US business more broadly.

A broad group of businesses organizations from around the world sent to the G-20 June 3 a set of "Recommendations for Promoting Innovation, Digital Technologies, and Trade" that did not directly address the USTR announcement but urged G-20 governments to "[c]ommit to achieving a multilateral solution to the taxation challenges arising from the digitalisation of the global economy, and refrain from pursuing unilateral digital tax measures that are discriminatory in nature and contravene long-standing principles of international taxation."
URL: https://www.ccianet.org/wp-content/uploads/2020/06/Multiassociation-G20-2020-Recommendations_6-3-2020.pdf

International reaction

Several of the trading partners named in USTR's new investigation, including the EU, the UK, and the Czech Republic, indicated that they intend to proceed with their DSTs despite the threat of possible US tariffs, and France's Le Maire criticized the move, telling Bloomberg News there is "a real contradiction" between a US call for unity within the G-7 nations "and the possibility of new trade sanctions."

The EU said June 3 that it will respond to any US trade sanctions with similar measures.

"In this, as in all other trade-related matters, the European Union will react as one," a spokesman for the trading bloc said, adding that the USTR probe must "comply with the international law and in particular the rules of the World Trade Organization."

A UK Treasury spokesperson defended its DST – which went into effect April 1 but does not involve any tax collection until 2021 – as a "fair and proportionate tax," saying, "Our digital services tax ensures that digital businesses pay tax in the UK that reflects the value they derive from UK users, and is compatible with the UK's international obligations."

Czech Finance Minister Alena Schillerova called tax policy "a sovereign matter of every state" and insisted that the Czech Republic's DST remains on track to go into effect at the beginning of 2021 to "actively [address] the imbalance between companies operating on the basis of traditional business models and companies that operate under completely new business models of the digital economy."

Congressional response

Congressional tax leaders have weighed in on DSTs numerous times in the past few years, arguing that a global consensus like that being sought at the OECD is the most appropriate way to handle international tax changes. In response to the USTR announcement, Senate Finance Committee Chairman Charles Grassley, R-Iowa, and the committee's ranking Democrat, Ron Wyden of Oregon, issued a joint statement June 2 in support of the investigations, saying, "Actions taken by [OECD] member states to enact digital services taxes are contrary to the organization's goals and are counter to the OECD process."

House Ways and Means Committee Chairman Richard Neal, D-Mass., said, "My position on this matter hasn't changed – I continue to oppose unilateral digital services taxes and support a multilateral solution. I hope Treasury can continue to engage with the OECD and work towards an outcome the protects US workers and businesses. I also intend for the committee to remain in close contact with USTR and Treasury regarding this issue. I hope that USTR is able to diversify its tools for enforcement and use them strategically in service of an optimal outcome."

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OIRA receives carried interest proposed regs for another review

In an update published on its web site this week, the Office of Information and Regulatory Affairs (OIRA) indicated that proposed regulations under section 1061, pertaining to the treatment of partnership interests held in connection with the performance of services, have been submitted for review for the second time by the Treasury Department.
URL: https://www.reginfo.gov/public/do/eoDetails?rrid=130643

Section 1061 was enacted in the 2017 tax code overhaul known informally as the Tax Cuts and Jobs Act (P.L. 115-97). Generally, in order for partners holding carried interests to obtain long-term capital gain treatment, the person who disposed of the property must have held the property for more than three years.

OIRA is part of the White House Office of Management and Budget. Its review of a regulatory project is one of the final actions taken before the guidance is released to the public.

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