In this issue:

GOP tax reform framework long on rate cuts, short on pay-fors

The "Big Six" negotiating team of congressional Republican leaders and White House officials released a long-awaited tax reform framework on September 27 that calls for ambitious cuts to tax rates for corporations, passthrough entities, and individuals; a more generous – albeit temporary – expensing regime; significant increases to the individual standard deduction and the child tax credit; and repeal of the estate tax and the individual alternative minimum tax.

But even though the plan contemplates that tax reform will result in the modification, scaling back, or outright repeal of many current-law business and individual tax incentives, it provides relatively few specifics on the policy tradeoffs that will be necessary to enact reform within the confines of budget rules that prohibit legislation moved under fast-track reconciliation protections from increasing the federal deficit outside the 10-year budget window.

Members of the Big Six include House Ways and Means Committee Chairman Kevin Brady, R-Texas, Senate Finance Committee Chairman Orrin Hatch, R-Utah, House Speaker Paul Ryan, R-Wis., Senate Majority Leader Mitch McConnell, R-Ky., Treasury Secretary Steven Mnuchin, and National Economic Council Director Gary Cohn.

Business provisions

In general, the framework calls for restructuring the business tax rules to create a more competitive environment for large and small businesses alike.

Corporate rate reductions: The framework calls for reducing the US statutory corporate rate from 35 percent down to 20 percent, which would place the US below the OECD average of 22.5 percent. President Trump had pushed for a rate of 15 percent, however most members of the Big Six indicated in public comments in recent weeks that a 15 percent corporate rate would be unrealistic given the large revenue loss associated with that level of rate reduction.

Integration in the mix?: The framework also leaves the door open for a corporate integration proposal – an approach favored by Finance Committee Chairman Hatch – noting that the congressional taxwriting committees "may consider methods to reduce the double taxation of corporate earnings." (Hatch has been an outspoken advocate of corporate integration and has spent considerable time over the past few years developing a plan that would couple a dividends-paid deduction with a withholding tax on both interest and dividend payments, although he has not released a formal proposal. Senate taxwriter John Thune, R-S.D., recently told reporters that a Finance Committee tax reform bill could include a "partial corporate integration" plan that likely would not have a withholding component.)

Corporate AMT: Under the framework, the corporate alternative minimum tax would be repealed, though no mechanism is specified for dealing with existing AMT credits.

Passthroughs: The framework calls for a top rate of 25 percent on "small businesses" – defined as a business organized as a sole proprietorship, partnership, or S corporation – which are currently taxed on the individual side of the code. To address concerns that a special passthrough rate will lead to gaming, the framework also says that the taxwriting committees will be tasked with drafting rules to prevent recharacterization of wage income as partnership income. The framework does not, however, provide guidelines for what those anti-abuse rules should look like, though in the past, Secretary Mnuchin has commented that the lower rate will not be available for professional services income.

Treatment of capital expenditures, net interest expenses: The framework would allow businesses to immediately write off 100 percent of the cost of new capital investments – other than structures – for "at least five years," effective for investments after September 27, 2017.

The ability of C corporations to deduct net interest expenses would be "partially limited"; however, the framework leaves it to the taxwriting committees to determine how any limitations will operate.

Changes to business incentives: According to the framework, the substantial reduction in marginal business tax rates will eliminate the need for additional business incentives so many will be pared back or repealed.

Although it generally does not elaborate on the fate of specific current-law business tax incentives, the framework explicitly identifies the section 199 deduction for domestic manufacturing activity as a target for repeal. It also specifically calls for retaining current-law credits for research and development and for low income-housing.

Credits for specific industries: The framework states without further elaboration that the taxwriting committees will look to "modernize" rules governing the tax treatment of "certain industries and sectors" to ensure "that the tax code better reflects economic reality and that such rules provide little opportunity for tax avoidance."

International taxation

For US multinationals, the framework proposes switching from a worldwide system, where all profits are subject to the US statutory rate upon repatriation regardless of where they were earned, to a territorial system that provides for a 100 percent exemption for dividends paid by a foreign subsidiary to a US parent with at least 10 percent ownership.

Deemed repatriation: To transition to the new system, accumulated overseas earnings would be deemed repatriated and taxed over an unspecified period at one of two rates (one for earnings held in illiquid assets and one for cash or cash equivalents). The framework does not specify the rates, but presumably, as in prior proposals, the rate for cash and cash equivalents will be higher.

Minimum tax: The framework calls for "rules to protect the US tax base by taxing at a reduced rate on a global basis the foreign profits of US multinational corporations," but leaves the specifics of those rules – including the applicable rate – to the taxwriting committees.

Individual provisions

On the individual side, the drafters of the framework indicate that their primary focus is on reducing tax burdens on the middle class and "creating a healthier economy [to] give American families greater confidence and help them get ahead."

Income tax brackets and rates: The framework calls for compressing the current seven income tax rate brackets into three: 12 percent, 25 percent, and 35 percent.

However, the framework leaves the option open for Congress to create an additional new top bracket for "the highest-income taxpayers" – at an unspecified rate – to ensure the tax code is "at least as progressive as the current tax code."

Increased standard deduction: The framework essentially would double the current-law standard deduction to $12,000 for single filers and $24,000 for married filers. The personal exemption would be repealed as would, presumably, the "head of household" filing status.

The framework states that the increased standard deduction is meant to create more taxpayers within the "zero bracket" as well as address some concerns over raising the lowest tax rate from 10 percent to 12 percent.

Capital gains rates: The framework does not mention changes to tax rates on capital gains, although it notes that the taxwriting committees will be tasked with examining "additional measures to meaningfully reduce the tax burden on the middle class."

Carried interests: The framework does not discuss the tax treatment of income from carried interests.

Estate tax, AMT: The estate tax and the individual alternative minimum tax would be repealed.

Individual incentives: To replace the personal exemptions for dependents, the framework would increase the child tax credit as well as the income threshold at which the credit begins to phase out. (Neither amount is given in the framework, but it specifies the first $1,000 of the credit will remain refundable.) There is an additional nonrefundable credit of $500 for nonchild dependents.

Itemized deductions: The framework proposes – largely without elaboration – to eliminate the vast majority of current-law itemized deductions other than those for charitable contributions and mortgage interest payments. In their recent public comments, however, members of the Big Six have specifically identified the deduction for taxes paid to state and local governments as a current-law incentive that would be eliminated under tax reform. This has already been flagged as an issue by congressional lawmakers in both parties who represent higher-tax states.

Work, education and retirement savings: The framework generally calls for retaining current-law incentives that promote work, education, and retirement savings, but tasks the taxwriting committees with streamlining them to increase their efficiency.

Ambitions of the framework meet reality of budget rules

A critical aspect of tax reform missing from the framework is its overall net impact on the federal budget. Taken together, it is likely that the revenue-losing policies enumerated in the plan – including the reduced rates on individual, corporate, and passthrough business income, enhanced expensing, the territorial system, plus the repeal of the corporate and individual AMT and the estate tax – would cost several trillion dollars over the next decade.

But under the special legislative process Republicans are eyeing to move a tax bill through the Senate on a simple-majority basis – *i.e.*, "budget reconciliation" – legislation generally cannot increase the deficit in any year beyond the budget window (which is typically 10 years), lest it be subject to procedural hurdles under the "Byrd Rule" that require 60 votes to waive. (Because Republicans currently control 52 of 100 Senate seats and more-than-token Democratic support for a tax reform bill that follows these general contours is not anticipated, Byrd Rule waivers presently seem very unlikely.)

In practical terms, this means Republicans eventually also must identify several trillion dollars' worth of revenue-*raising* provisions (in addition to the few alluded to in the framework such as partially limiting interest deductibility for C corporations, repealing the section 199 domestic manufacturing deduction, and repealing the itemized deduction for state and local taxes) if they want to enact the framework's tax cuts on a permanent basis – or, absent that, scale back their tax-cutting ambitions to something they are, in fact, able to fully finance over the long-run.

These difficult trade-offs are exemplified in a recent analysis by the nonpartisan Tax Policy Center which concludes that, even if Congress were to eliminate *all* business tax expenditures – including the research credit, which the framework says should be maintained in some form – the lowest top corporate rate achievable on a long-run revenue-neutral basis is 26 percent.

Another possibility, which has been alluded to by Republican leaders including Speaker Ryan, would be to sunset certain revenue-losing provisions such that they no longer score as deficit-increasing over the long run, perhaps with the hope that a future Congress and president would act to extend them further, or even make them permanent – similar to what ultimately occurred with respect to a large share of the individual tax cuts originally passed under budget reconciliation in 2001 and 2003.

Senate budget process to kick-off next week: Before any tax bill can be moved under reconciliation, however, the House and Senate GOP first must adopt a budget resolution for fiscal year 2018 that includes reconciliation instructions to the taxwriting committees in both chambers. Senate Majority Leader Mitch McConnell, for his part, signaled this week that a budget mark-up would occur in the Senate Budget Committee during the week of October 2.

Based on reports recent reports, the Senate budget resolution – the text of which may be made public as early as September 30 – could differ significantly from the budget resolution that cleared the House Budget Committee on July 19. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 32, September 22, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170922_1.html

Specific to tax reform, the Senate budget is expected to incorporate a handshake deal struck by Budget Committee Republicans Bob Corker of Tennessee and Pat Toomey of Pennsylvania on September 19 that would instruct the Senate Finance Committee to report legislation that reduces revenues by as much as $1.5 trillion over the next decade. According to comments made by Sen. Corker, this would give taxwriters some political flexibility to pursue tax legislation on a filibuster-proof basis that is not fully-financed. (Note, however, that the "Byrd Rule" mentioned above would continue to constrain the GOP's ability to enact a fully *permanent* tax bill that increases the deficit beyond the budget window.)

House budget developments: Meanwhile, the budget plan advanced by the House Budget Committee earlier this summer includes a broad set of reconciliation instructions to 11 committees aimed at expediting both revenue-neutral tax reform and significant cuts to entitlement programs. (For details, see *Tax News & Views*, Vol. 18, No. 26, July 21, 2017.) But a vote by the full House had been held up by members of the conservative House Freedom Caucus who demanded details of the tax reform proposal first. (Because no Democrats are expected to support the budget resolution, Republican leaders can afford to lose only about two dozen votes, and the House Freedom Caucus has about three dozen members.) The Freedom Caucus officially endorsed the new framework on September 27, clearing the path for a possible floor vote as soon as the week of October 2.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170721_1.html

Challenges for the taxwriting committees

With the release of the framework, it now falls to the congressional taxwriting committees to turn the high-level guidance into legislative language – filling in the gaps in a way that ensures the bill meets budgetary requirements and crafting the complex but crucial transition rules – something Senate Majority Leader Mitch McConnell has labeled a "daunting task."

Ways and Means likely up first: The Ways and Means Committee is expected to act first, meeting the requirement that all revenue measures must originate in the House. While Chairman Brady has not set an official timeline, he reportedly has said he hopes to release a legislative product sometime in October and complete a mark-up and vote in the committee before Thanksgiving.

"Now it's time for the Ways and Means Committee to build on this momentum and deliver legislation that President Trump can ultimately sign into law," said Brady in a September 27 press release. "We are closer than ever to finishing what we have started for the American people – and 2017 is our year to make it happen."

But Brady has noted that release of draft legislation won't take place until the House completes its work on the fiscal year 2018 budget resolution, which will carry reconciliation instructions and revenue targets for the tax reform process.

One potential challenge to a GOP tax reform plan in the House is likely to come from a group of 52 Republicans representing districts where taxpayers disproportionately use the current state and local tax deduction slated for repeal under the new framework. Rep. Peter King of New York, who calls the incentive "absolutely essential to my district," says he'll vote against any package that includes repeal – and he believes he has the support of enough colleagues to force the issue.

"I intend to fight it with everything I know how," said Rep. Tom MacArthur of New Jersey.

The elimination of the deduction is estimated to raise a significant amount of revenue that will help offset lower rates and other beneficial changes (last year, the Joint Committee on Taxation estimated the deduction's cost at more than $368 billion through 2020), so removing the provision from the bill would make the math even harder for taxwriters.

Similar political battles are likely to be waged over the many still-to-be-unveiled revenue raising provisions that will be necessary to offset the cost of the large proposed rate reductions.

Whither the Senate?: The Senate poses an additional challenge for tax reform. With Republicans holding only 52 seats and with few Democrats currently expected to support a GOP tax reform package, the margin for error is extremely small and – as leadership has experienced with health care legislation this year – it can be challenging to draft a bill that satisfies the diverse interests of senators even within a single party.

Moreover, while the Big Six framework means the House and Senate are starting from the same point, Finance Committee Chairman Hatch recently made it clear that his panel will not necessarily reach the same conclusions as its House counterpart.

"Any forthcoming documents may be viewed as guidance or potential signposts for drafting legislation, but at the end of the day, my goal is to produce a bill that can get through this committee." he said during a September 14 hearing on the individual side of the tax code. "Anyone with any experience with the Senate Finance Committee knows that we are not anyone's rubber stamp," he added.

Emphasizing the challenge ahead to reporters today, Sen. Bob Corker of Tennessee said that "tax reform is going to make health care look like a piece of cake."

No bipartisan kumbaya expected: While both Hatch and Brady have said they welcome input from their Democratic colleagues and would like bipartisan support for tax reform legislation – and President Trump continues to try and woo several Senate Democrats from deep red states – the framework is an entirely Republican-crafted product unlikely to get any support from the other side of the aisle.

"If this framework is all about the middle class, then Trump Tower is middle-class housing," said Sen. Ron Wyden of Oregon, the Finance Committee's senior Democrat, in a September 27 press release. "It violates Trump's tax pledge that the rich would not gain at all under his plan by offering sweetheart deals for powerful CEOs, giveaways for campaign coffers and a new way to cheat taxes for Mar-a-Lago's loyal members. This continued lack of detail for the middle class guarantees that average Americans will be the ones hit with shrinking paychecks and higher tax bills," Wyden said.

Finance Chairman Hatch offered his own take on bipartisanship in the tax reform process during a September 27 interview on Fox Business.

"I hope we don't need Democratic votes, but I hope we get them…I think we can hold together the Republicans on this matter."

— Alex Brosseau (Washington, DC)
Senior Manager
Deloitte Tax LLP
abrosseau@deloitte.com

United States Tax Alert: Notice 2017-57 defers applicability date of section 987 regulations

On October 2, 2017, Treasury and the IRS issued Notice 2017-57 (the "Notice"), announcing their intent to defer the applicability date of the final section 987 regulations (and certain temporary section 987 regulations) by one year.

In the Notice, the government pronounced that it intends to amend the final and certain temporary section 987 regulations to defer the applicability dates. In the meantime, taxpayers can rely on the Notice regarding such proposed amendments. Specifically, the final section 987 regulations (and related temporary regulations) will apply to "taxable years beginning on or after two years after the first date of the first taxable year following December 7, 2016." For example, for calendar year taxpayers, the regulations will apply to the taxable year beginning on January 1, 2019.

Importantly, certain temporary regulations, including the section 987 deferral rules under Temp. Treas. Reg. §1.987-12T and the section 988 anti-abuse rule under Temp. Treas. Reg. §1.988-2T(b)(16), are not subject to the deferred applicability date and, therefore, are still currently applicable.

The Notice also provides that taxpayers may early-adopt the final section 987 regulations, provided that they apply the regulations consistently to all qualified business units (QBUs) owned directly or indirectly on the transition date. Thus, taxpayers can apply the final regulations to taxable years beginning after December 7, 2016 (starting with the first or second taxable year beginning after December 7, 2016).

Finally, the Notice provides that the government is considering changes to the final section 987 regulations to allow taxpayers to elect alternative rules to (i) transition to the new regulations and (ii) determine section 987 gain or loss.

Second Report to the President issued by Treasury

In addition to the Notice, on October 4, 2017, Treasury issued the Second Report to the President on Identifying and Reducing Tax Regulatory Burdens (the "Second Report") providing further guidance with respect to section 987. The government first acknowledges that the final section 987 regulations "have proved difficult to apply for many taxpayers." As a result, the government intends to propose modifications to the final section 987 regulations to permit taxpayers to elect a simplified method of calculating section 987 gain or loss, subject to certain limitations on the timing of recognition of section 987 loss.

One of the methods under consideration would allow all assets and liabilities of a section 987 QBU to be treated as "marked" items, and all taxable income of a QBU to be translated at the yearly average rate. This method is similar to the approach set forth in the 1991 proposed regulations. The amount of section 987 gain or loss computed under such method would generally be consistent with any translation gain or loss determined under financial accounting rules. The government is considering alternative loss-recognition timing limitations that would apply to taxpayers who elect the above method. One alternative is to allow taxpayers the ability to recognize section 987 losses only to the extent of the net section 987 gains recognized in prior or subsequent years. The other alternative is to defer a taxpayer's section 987 gains and losses until the earlier of (i) the year the QBU's trade or business ceases to be conducted by any member of the taxpayer's controlled group or (ii) the year substantially all of the assets and activities of the QBU are transferred outside of the taxpayer's controlled group.

The government is also considering alternative methods for transitioning to the new regulations. One alternative would allow taxpayers that elect to apply the loss limitations (applicable to the simplified methodology described above) to elect to carry forward unrealized section 987 gains and losses, measured as of the transition date with certain adjustments. This alternative is similar to the "deferral" transition method in the 2006 proposed regulations and would be used in lieu of the "fresh start" method.

For those applying the "fresh start" transition method, the government is considering an election to use the spot exchange rate to translate all items on the opening balance of a QBU on the transition date. This would effectively result in the complete elimination of pre-existing section 987 gains and losses at the time of the fresh start. In comparison, under the default fresh start method, some of such gains or losses are preserved in the form of section 987 gain or loss on marked items or a basis difference in historic items.

Importantly, these transition alternatives and the simplified method alternatives would be elective. It appears that the government will retain the approach under the final section 987 regulations as the default method. By doing so, the government effectively compels taxpayers who find compliance with the final regulations to be unduly complex and financially burdensome to elect into some sort of a simplified method with loss limitations.

ASC 740 considerations

From an ASC 740 perspective, the Notice effectively establishes an administrative practice pursuant to which companies are not required to adopt final regulations (and related temporary regulations) until "taxable years beginning on or after two years after the first date of the first taxable year following December 7, 2016." Taxpayers should assess, in the financial reporting period that includes October 2, 2017, whether they intend to rely on the Notice to defer the applicability date of the regulations. Taxpayers intending to rely on the Notice should account for any impact the deferral of the applicability date will have in the financial reporting period that includes October 2, 2017. Specifically, such taxpayers should revise what impact the change in applicability date will have on their assessment of temporary differences and associated deferred taxes that will reverse before and after the revised applicability date, and record such impact in the financial reporting period that includes October 2, 2017. Taxpayers not intending to rely on the Notice as a means of deferring the effective date would not be impacted from an ASC 740 perspective and would continue to account for the final regulations (and related temporary regulations) in preparing their income tax provision.

Any subsequent actions by the government that modify the final regulations (and related temporary regulations) would be accounted for in the reporting period of such subsequent actions. All taxpayers should continue to monitor subsequent guidance that may be issued by the government as there could be further ASC 740 consequences when any future guidance is issued.

— Michael Mou (Washington, DC)
Principle
Deloitte Tax LLP
mmou@deloitte.com

Paul Vitola (Phoenix)
Partner
Deloitte Tax LLP
pvitola@deloitte.com

Patrice Mano (San Francisco)
Partner
Deloitte Tax LLP
pmano@deloitte.com

Tax Reform: Human Resources and Global Mobility – Setting the tax reform stage

Tax reform is a top priority for President Trump and Republican leaders in Congress. With major health care legislation almost certainly off the agenda for the remainder of the year, comprehensive tax reform is poised to take center stage as a key legislative focus.

Congressional Republicans, the President, and top Administration officials worked together over the summer to refine proposals and now the "Big Six" team of negotiators1 has released a unified tax reform framework ("the framework").

The framework provides high-level guidance regarding the priorities for the tax reform process and it challenges the Congressional taxwriting committees to work out the details to make those priorities a legislative reality. Core elements include reducing corporate, passthrough, and individual tax rates and encouraging the "on- shoring" of profits and jobs to the US.

The potential impact of tax reform on US companies is a high priority issue and the effect to HR and global mobility programs should not be overlooked.

Top considerations and planning for human resources and global mobility

Refreshing global mobility strategy: Changes to individual income tax rates could have a direct impact on the cost of global mobility programs for companies that apply a tax equalization policy. Lower US tax rates, with no change in foreign tax rates, will result in a rebalancing between hypothetical and actual taxes, thereby impacting overall tax reimbursement costs. Whether this change will result in overall increase or decrease to a company's costs will depend on the mix of assignments into high-tax or low-tax countries. A holistic review of policies can help companies determine whether the structure and costs of global mobility are in-line with the company's business needs.

Analyze impact of reduced tax rates on rewards programs: As corporate tax rates are reduced, deductions become less valuable and companies may realize additional benefit by accelerating deductions to a higher tax year. Employee benefit and rewards plans may present several opportunities to accelerate business deductions; for example, accelerating the accrual of bonus payments and pre-funding Voluntary Employees Beneficiary Association Plans (VEBAs) each present opportunities to take deductions in a higher-tax year. Companies should analyze the potential impact of reduced tax rates on their rewards programs and review opportunities to enhance corporate tax deductions.

Consider impact of "on-shoring" of profits on rewards programs: The framework calls for switching from the current worldwide system, where all profits are subject to the US statutory rate upon repatriation regardless of where they were earned, to a territorial system that provides for a 100 percent exemption for dividends paid by a foreign subsidiary to a US parent. To transition to the new system, the framework proposes a one-time deemed repatriation that would subject existing foreign profits to US tax (at a to-be-determined but lower rate than the corporate rate). In light of these proposed changes, companies may want to analyze tax deductions associated with contributions and accruals under foreign pension arrangements to determine whether they can reduce the impact of any deemed repatriation.

Additionally, with respect to equity programs, changes in the repatriation rules may cause a company to revisit cost-charging arrangements related to share plans and may create an opportunity to repatriate reimbursements in "real time." Under existing rules, such charge out and repatriation prior to share delivery may create some risk of taxation to repatriated reimbursement payments.

Addressing timing around individual income inclusion relating to employee benefit and equity programs: In anticipation of potentially lower individual income tax rates, employees may be motivated to defer income to future tax years through delayed exercise of stock options or greater participation in deferred compensation programs. While the lower tax rates may present a tax planning opportunity for individuals, the increased deferral of income may also delay the corporate tax deductions related to that income, which could impact a company's ability to accelerate compensation deductions into a higher-tax year.

Monitoring changes to the Affordable Care Act (ACA): Congress has made several attempts to repeal and replace the ACA; however, as these efforts have been unsuccessful to date, the ACA remains the law. In addition, the reporting requirements have been retained in each of the many bills that have considered repeal and replace. Identifying full-time employees based on the tax law and regulations can be complex and employers could face a significant liability for non-compliance with ACA requirements. Employers should continue to assess whether internal processes are adequate to determine the potential risk liability for each month of 2017 reporting.

Next steps

Tax reform will be one of Congress' highest priorities for the remainder of 2017, and possibly into the first quarter of 2018, as they work to enact significant legislation before the 2018 election cycle gets into high gear. Deloitte Tax LLP's Global Employer Services group will continue to publish updates as the legislative process progresses and new developments emerge. In the meantime, companies can begin to conduct impact analyses to assess the potential cost of these changes to their global mobility and rewards programs and analyze potential cash tax savings that could be realized through acceleration of corporate tax deductions related to employee benefit plans.

OECD releases additional implementation guidance on CbC reporting and appropriate use of information in CbC reports

The OECD on 6 September released additional guidance on the implementation of the country-by-country (CbC) reporting requirement introduced in the BEPS Action 13 final report. In addition, the OECD released guidance on the appropriate use of information contained in CbC reports (CbCRs).
URL: https://www.oecd.org/tax/guidance-on-the-implementation-of-country-by-country-reporting-beps-action-13.pdf
URL: http://www.oecd.org/tax/beps/beps-action-13-on-country-by-country-reporting-appropriate-use-of-information-in-CbC-reports.pdf

The new guidance consolidates and expands on all of the implementation guidance issued by the OECD since the release of the Action 13 final report. Also included in the text of the new guidance, therefore, is the additional implementation guidance issued on: (i) 29 June 2016; (ii) 5 December 2016; (iii) 6 April 2017; and (iv) 18 July 2017.1 Because the 6 September release includes all the information found in the prior four releases, when consulting OECD additional guidance on the Action 13 final report, it will only be necessary to refer to the 6 September guidance going forward.

New implementation guidance

The new implementation guidance addresses four specific issues:

- Items reported as revenues in Table 1 of the CbCR, when financial statements are used as the source of the data to complete the CbC template;
- Income taxes paid in advance in Table 1 of the CbCR;
- Treatment of tax refunds in Table 1 of the CbCR; and
- Transitional relief for multinational enterprise groups (MNE groups) with a short accounting period that starts on or after 1 January 2016 and ends before 31 December 2016.

Definition of revenues for Table 1 of the CbCR (new): The 6 September guidance addresses which items should be reported as revenues in Table 1 of the CbCR. The guidance explains that, when financial statements are used as the source of the data to complete the CbC template, all revenue, gains, income, or other inflows shown in the financial statement prepared in accordance with the applicable accounting rules relating to profit and loss (such as the income statement or profit and loss statement) should be reported as "Revenues" in Table 1.

For example, if the income statement prepared in accordance with the applicable accounting rules shows:

- Sales revenue;
- Net capital gains from sales of assets;
- Unrealized gains;
- Interest received; and
- Extraordinary income

Then the amount of those items reported in the income statement should be aggregated and reported as revenues in Table 1.

The 6 September guidance further explains that comprehensive income/earnings, revaluations, and/or unrealized gains reflected in net assets and the equity section of the balance sheet should not be reported as Revenues in Table 1. Finally, the guidance states that the amount of any income items shown on the income statement need not be adjusted from a net amount.

Members of the Inclusive Framework on BEPS – over 100 countries and jurisdictions that collaborate on the implementation of the BEPS project – are expected to implement this guidance as soon as possible, taking into account their specific domestic circumstances. The OECD recognizes that some MNE groups may need time. As a result, the 6 September guidance states that jurisdictions may allow some flexibility during a short transitional period. For US MNEs, the guidance appears to be consistent (or at least not in conflict) with the CbC regulations in Treas. Reg. §1.6038-4, so no change may be needed for implementation in the United States.

How to treat taxes paid in advance in Table 1 of the CbCR (new): The new implementation guidance also addresses how to report the income tax for a fiscal year that has been paid in advance. Specifically, it addresses whether the amount reported in the "Income Tax Accrued-Current Year" column should be linked to the amount reported in the "Income Tax Paid (on Cash Basis)" column of Table 1.

According to the new implementation guidance, the amount listed in the column "Income Tax Accrued-Current Year" is the amount of accrued current tax expense recorded on taxable profits or losses for the reporting fiscal year of all constituent entities resident for tax purposes in the relevant tax jurisdiction, irrespective of whether or not the tax has been paid (for example, based on a preliminary tax assessment).

The guidance further explains that the amount listed in the column "Income Tax Paid (on Cash Basis)" is the amount of taxes actually paid during the reporting fiscal year, which should include not only advance payments fulfilling the relevant fiscal year's tax obligation but also payments fulfilling the previous year(s)' tax obligation (for instance, payment of the unpaid balance of corporate income tax accrued in relation to the previous year(s), including payments related to reassessments of previous years), regardless of whether those taxes have been paid under protest. The new implementation guidance concludes by saying that the amount of "Income Tax Accrued-Current Year" and "Income Tax Paid (on Cash Basis)" should be reported independently.

For example, assume that an MNE group accrues $100 of taxes in year 1 and $150 of taxes in year 2, but pays $75 of taxes in year 1 and $175 of taxes in year 2 (that is, $25 for the year 1 obligation and all $150 of the year 2 obligation). The relevant columns of the MNE group's CbCR would read as follows:

Example 1	Year 1	Year 2
Income Tax Accrued-Current Year	$100	$150
Income Tax Paid (on Cash Basis)	$75	$175

In the alternative, assume instead that the MNE group accrued $100 in taxes in year 1 and $150 in year 2, but then paid $125 in year 1 and $125 in year 2 (that is, all $100 of its obligation in year 1 and $25 in advance for year 2 and then the remaining $125 in year 2). The relevant columns of the group's CbCR would read as follows:

Example 2	Year 1	Year 2
Income Tax Accrued-Current Year	$100	$150
Income Tax Paid (on Cash Basis)	$125	$125

The amounts of "Income Tax Accrued-Current Year" and "Income Tax Paid (on Cash Basis)" would thus be reported independently.

As with the first issue discussed above, Inclusive Framework members are expected to implement this new guidance as soon as possible, taking into account their specific domestic circumstances. The OECD recognizes that MNE groups may need some time to take the guidance into account. As a result, the new guidance states that jurisdictions may allow some flexibility during a short transitional period. For US MNEs, the guidance appears to be consistent with the CbC regulations in Treas. Reg. §1.6038-4, so no change may be needed for implementation in the United States.

How to treat refunds in Table 1 of the CbCR (new): The 6 September guidance addresses how tax refunds should be reported. In general, an income tax refund should be reported in the column entitled "Income Tax Paid (on Cash Basis)" in the reporting fiscal year in which the refund is received. The new implementation guidance states that an exception to this may be permitted when the refund is treated as revenue of the MNE group under the applicable accounting standard or in the source of data used to complete Table 1.

Inclusive Framework members again are expected to implement this guidance as soon as possible. The OECD recognizes that MNE groups may need time to take the guidance into account. As a result, the 6 September guidance says that jurisdictions may allow some flexibility during a short transitional period, during which the OECD encourages taxpayers to provide the following statement voluntarily in Table 3, if relevant: "Tax refunds are reported in Revenues and not in Income Tax Paid (on Cash Basis)."

Short accounting periods (new): Finally, as a transitional measure, the 6 September guidance states that jurisdictions may allow the reporting entity of an MNE group with a short accounting period beginning on or after 1 January 2016 and ending before 31 December 2016 to file the CbCR in accordance with the same timelines as for MNE groups with a fiscal year ending on 31 December 2016. The date by which the CbC report is to be exchanged would be similarly extended. The guidance concludes by stating this transitional relief would not frustrate the policy intention of the Action 13 minimum standard.

Guidance on appropriate use of information in CbC reports

According to the BEPS Action 13 final report, a jurisdiction's ability to obtain and use CbCRs is conditional on it using CbCR information appropriately. For these purposes, appropriate use is restricted to:

- High-level transfer pricing risk assessment;
- Assessment of other base erosion and profit shifting related risks; and
- Economic and statistical analysis, when appropriate.

The BEPS Action 13 final report makes clear that information contained in CbCRs should not be used by itself as a basis for proposing changes to transfer prices or adjusting a taxpayer's income using global formulary apportionment.

The appropriate use guidance clarifies how tax authorities may use CbC information by defining the term "BEPS-related risk." In addition, the guidance expands on the consequences of noncompliance with the appropriate use condition and sets out steps a jurisdiction may take to ensure the appropriate use of CbCR information.

The meaning of "BEPS-related risk": The guidance explains that the term "assessment of other BEPS-related risks" should be understood to refer to the high- level assessment of tax risks that may result in the erosion of a country's tax base. The guidance notes that, in practice, it will usually be possible to understand a tax arrangement giving rise to that risk only when further inquiries have been made. Nevertheless, the guidance reiterates that CbCR information should be limited to use in risk assessment, and only as a basis for making those further inquiries (and economical and statistical analysis, when appropriate).

Consequences of noncompliance with the appropriate use condition: The Action 13 final report includes a number of consequences for a jurisdiction resulting from noncompliance, or possible noncompliance, with the appropriate use condition. These consequences are given effect through the model competent authority arrangements (CAAs) that are used in implementing CbC reporting.

The consequences are as follows:

- Appropriate use as a condition for receiving and using CbCRs.
- A commitment by competent authorities to disclose breaches of appropriate use to the Coordinating Body Secretariat (for exchanges pursuant to the multilateral CAA) or other competent authority (for exchanges pursuant to the model bilateral CAAs, such as the exchanges the United States will engage in).
- A commitment by competent authorities promptly to concede inappropriate adjustments in competent authority proceedings.
- The ability of competent authorities to suspend the exchange of CbCRs temporarily following consultation in cases of noncompliance.

With respect to the first consequence, the appropriate use guidance explains that a jurisdiction may not require local filing, unless: (i) that jurisdiction satisfies the appropriate use condition; and (ii) the other conditions of local filing in the BEPS Action 13 final report are met. When a jurisdiction imposes local filing in circumstances that are not permitted under the BEPS Action 13 final report, this will be identified during the jurisdiction's peer review evaluation.

With respect to the second consequence, when the notification is made to the Coordinating Body Secretariat (that is, in the case of an exchange pursuant to the multilateral CAA), the secretariat will notify all competent authorities that have an exchange relationship under the multilateral CAA with the competent authority that provided notice of the noncompliance.

The appropriate use guidance also explains that any noncompliance with the appropriate use condition will be considered "significant non-compliance." When a competent authority determines that there is or has been significant noncompliance in another jurisdiction, that competent authority may temporarily suspend the exchange of CbCRs by giving notice in writing. Nevertheless, the guidance further states that the competent authority should, before suspending the exchange of CbCRs, consult with the competent authority in the other jurisdiction on whether significant noncompliance has occurred.

Approaches to determine appropriate use of CbCR information: The appropriate use guidance lists steps that jurisdictions may take, if necessary, to implement the appropriate use restriction into their domestic rules and processes. The guidance states that a jurisdiction should be able to answer in the affirmative six basic questions, which are provided in a checklist, that assess the robustness of its processes to ensure compliance with the appropriate use condition, or should expect to be able to do so before the first exchange of CbCRs takes place.

The appropriate use guidance recognizes that, in practice, jurisdictions may be able to rely on existing policies and procedures. In such a case, the initial step will likely entail confirming that CbCR information is covered by these policies and procedures. As a result, additional steps to ensure compliance with the appropriate use condition may be reasonably modest.

— David Varley (Washington, DC)
Principal
Deloitte Tax LLP
dvarley@deloitte.com

Joseph Tobin (Washington, DC)
Principal
Deloitte Tax LLP
jtobin@deloitte.com

Ivan Mullinax (New York)
Managing Director
Deloitte Tax LLP
imullinax@deloitte.com

Calendars to watch

Each edition, be sure to mark your calendars for some of the more important events (recent and upcoming) as well as tax developments making in impact on businesses investing into the United States.

Recent and Upcoming Activities

November 1
2:000 p.m. ET

Dbriefs webcast: (Special Edition) IRS update: Recent initiatives and tax controversy trends
Watch
URL: https://www2.deloitte.com/us/en/pages/dbriefs-webcasts/events/november/2017/dbriefs-irs-update-recent-initiatives-and-tax-controversy-trends.html?id=us:2em:3na:usic:awa:tax:103017

November 16
2:000 p.m. ET

Dbriefs webcast: Transfer pricing update: Focus on Eastern Europe
Watch
URL: https://www2.deloitte.com/us/en/pages/dbriefs-webcasts/events/november/2017/dbriefs-transfer-pricing-update-focus-on-eastern-europe.html?id=us:2em:3na:usic:awa:tax:103017

November 28
2:000 p.m. ET

Dbriefs webcast: Tax accounting and provisions: Year-end updates and other hot topics
Watch
URL: https://www2.deloitte.com/us/en/pages/dbriefs-webcasts/events/november/2017/dbriefs-tax-accounting-and-provisions-year-end-updates-and-other-hot-topics.html?id=us:2em:3na:usic:awa:tax:103017

November 29 2:000 p.m. ET	**Dbriefs webcast:** US tax reform: What businesses and individual taxpayers should know Watch **URL:** https://www2.deloitte.com/us/en/pages/dbriefs-webcasts/events/november/2017/dbriefs-us-tax-reform-what-businesses-and-individual-taxpayers-should-know.html?id=us:2em:3na:usic:awa:tax:103017
December 4 2:000 p.m. ET	**Dbriefs webcast:** Robotic process automation: From A to eXecution Watch **URL:** https://www2.deloitte.com/us/en/pages/dbriefs-webcasts/events/december/2017/dbriefs-robotic-process-automation-from-a-to-execution.html?id=us:2em:3na:usic:awa:tax:103017