Feedback for REG-104390-18: Guidance Related to §951A[1] (Global Intangible Low-Taxed Income) as of 11/19/2018

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Prop. Regs. §1.951-1(a)	In General	Double taxation of high-taxed foreign income	Final regulations should include an aggregate high-tax exception for GILTI pursuant to which a U.S. shareholder's GILTI inclusion would be zero in any taxable year in which such shareholder's net CFC tested income is subject to an aggregate effective rate of foreign income tax of 13.125% or greater (16.406% for taxable years beginning after 2025). The aggregate effective tax rate would be determined by dividing (a) the U.S. shareholder's aggregate tested foreign income taxes under §960(d)(3) by (b) the sum of (i) such shareholder's net CFC tested income; and (ii) the amount described in (a). Treasury should consider making the exception elective, similar to the high-tax election in §954(b)(4). If Treasury does not believe it has the authority to provide for such an exception, Treasury should seek legislation from Congress in order to conform the statute to legislative intent, as expressed by the conferees in the Conference Report explanation. This issue also will be impacted by the regulation package coming out on foreign tax credits (FTCs); we will continue to work on recommendations on a solution to the double taxation of high-taxed foreign income.	An automatic inclusion of high-taxed income (rather than a high-tax exception prior to inclusion) subjects taxpayers paying relatively high foreign taxes to double taxation because (i) deductions and expenses allocated to the GILTI foreign tax credit basket cause the loss of foreign tax credits, (ii) GILTI inclusions are subject to BEAT, which denies foreign tax credits, and (iii) taxpayers with NOLs as a result of earnings volatility are taxed on GILTI inclusions at the full 21% corporate tax rate, with no access to the §250 deduction or foreign tax credits. Treasury should consider making the exception elective, similar to the high-tax election in §954(b)(4). The legislative history indicates Congressional intent to impose residual U.S. tax under the GILTI regime only where the aggregate foreign effective tax rate is less than 13.125% (see H. Rep. No. 115-466, at 626). Treasury should exercise its authority under §7805(a) to conform to this intent, and a straightforward way to do so would be to provide for a high-tax exception pursuant to which a U.S. shareholder would have no GILTI inclusion if

[1] Unless otherwise noted, all section references are to the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder.

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				the aggregate foreign effective tax rate imposed on net CFC tested income is at least 13.125%. If Treasury does not believe it has the authority to provide an overall GILTI high-tax exception, they should seek a legislative solution.
Prop. Regs. §1.951-1(e)	Pro-rata share of subpart F income defined	Anti-abuse rule	Clarify the scope and mechanics of the anti-abuse rule in Prop. Regs. §1.951-1(e)(6).	The preamble and recent statements by Treasury officials have stressed the intent for this anti-abuse rule to catch non-economic allocations of CFC income. The plain language of (e)(6) appears to be broader than necessary to capture these type of abusive transactions. For example, under a plain reading of (e)(6), if a taxpayer rushed to close the sale of an asset by the end of a particular year because an unrelated buyer would get more favorable depreciation treatment by closing that year instead of the next year, that transaction would appear to be disregarded if the selling taxpayer were a CFC and the gain from the sale impacted its pro rata share of unrelated sub-F income. Also unclear is how transactions or arrangements should be disregarded. In the example above, it is unclear if the selling CFC should still be treated as owning the asset for all taxable years going forward forever.

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				As another example, if a CFC ownership structure with both preferred and common shares is disregarded under (e)(6), it is unclear whether the structure should be disregarded by treating all the shares as common shares, by ignoring the existence of whichever shares were created by the transaction (and potentially also any property contributed to the CFC in exchange for such shares), or by some other mechanism. As another example, consider check-the-box elections. Generally, Regs. §301.7701-3 provides taxpayers with an election to classify a foreign entity as either a CFC or a disregarded entity ("DRE"). If a taxpayer elects to classify a foreign entity as a DRE, and this classification avoids the recognition of future Subpart-F income, query whether the election to be classified as a DRE can be disregarded by Prop. Regs. §1.951-1(e)(6)? This eliminates the certainty and simplicity created by Regs. §301.7701-3. Finally, consider the election provided in §338(g) to increase the value of a foreign target's assets to fair market value (the "step-up"). If the future depreciation or amortization created by the step-up is recovered against

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				Subpart-F income, query whether the §338(g) election can be disregarded by Prop. Regs. §1.951-1(e)(6)? The lack of clarity described above only increases over time, as taxpayers change their organizational structures or enter into transactions in response to commercial pressures, regulatory requirements, or other non-tax needs but where tax considerations play a role in the structure or timing. Clarity on how taxpayers should apply (e)(6) is crucial to allow taxpayers to keep accurate books and records and to continue running business operations smoothly.
Prop. Regs. §1.951A-2, Preamble I.C.1.	Tested income and tested loss	Section 245A application to CFC dividend income	With respect to dividends received by CFCs, provide that §245A(a) dividends received deduction applies to dividends that constitute subpart F income. For example, §245A should not be applied to (1) a distribution of PTI earnings, or (2) a dividend distribution (or a deemed dividend distribution) to which §954(c)(6) look-through rules, high tax exceptions (whether expanded to cover non-subpart F income) or the same country exceptions would also apply. Section 245A should apply last under an ordering rule that places the §245A DRD as the last item in the chain, and the regulations should provide that §1059 would not apply in situations where it would not have applied under pre-TCJA.	As stated in the legislative history, Congressional intent is that the §245A DRD should apply to subpart-F dividend income received by domestic corporations as well as CFCs. See Conf. Rep. at 599, fn. 1486 (citing Treas. Reg. §1.952-2). If the §245A DRD does not apply to subpart F dividend income, American firms would be disadvantaged against foreign competitors. CFC dividend income received from the following lower tier entities would not be eligible for the participation exemption:

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				1. 100% owned lower-tier CFCs: considered Subpart-F income and taxed at 21% if CFC look-through not extended, 2. 10/50 foreign corporations: considered subpart F income and taxed at 21%. There is no reason to treat dividends from lower-tier entities differently than dividends from first-tier entities. Applying §245A(a) to non-subpart-F dividend income (§954(c)(6) look-through, same country dividends, high tax exceptions) can create subpart F income due to the potential application of §1059(a). There is no indication that Congress intended to create subpart F income in circumstances that would not have resulted in subpart F income under prior law (other than where explicitly stated, for example, in section 245A(e) with respect to hybrid dividends.)
Prop. Regs. §1.951A-2(c)	Rules relating to the determination of tested income and tested loss	Lack of authority to issue *per se* rule disregarding deduction or loss due to basis step-up during disqualified period	Withdraw Prop. Regs. §1.951A-2(c)(5). In the alternative, this proposed rule should be substantially revised and re-proposed in a narrower manner to apply only to non-economic transactions, as provided in the legislative history.	The preamble to Prop. Regs. §1.951A-2(c)(5) indicates that it is issued under §§951A(d)(4) and 7805(a). Neither §951A(d)(4) nor §7805(a) provides the Treasury/IRS the authority to issue Prop. Regs. §1.951A-2(c)(5). For example, §951A(d)(4) deals with the computation of a CFC's qualified business

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				asset investment (QBAI), as opposed to the computation of a CFC's tested income. Moreover, the Conference Report explanation clearly states legislative intent for Treasury to address only non-economic transactions. Congress did not provide authority for Treasury to write a *per se* rule. (See Conf. Rep. at p. 645 (and cited on page 23 of Preamble).
		Calculation of a CFC's tested income or loss	The regulations should be amended to provide that a CFC computes its tested income/loss based on the E&P principles under §964.	Taxpayers already compute E&P for a CFC so to compute tested income/loss under a different approach adds undue administrative burden.
			If not tied to E&P principles as described above, regulations should at least be amended to provide that domestic company loss limitations subject to carryover/carryback rules are not applicable when computing tested income, since tested income does not have carryover/carryback rules.	For example, §1211 limits capital losses to capital gain and §1212 allows for a loss carryover/carryback. If CFCs must be treated as domestic companies for purposes of computed tested income and be subject to §1211, then limited capital losses would be permanently lost without a carryover/ carryback. See Regs. 1.952-2(c)(5)(i). Instead, these losses should not be limited to capital gains.
Prop. Regs. §1.951A-3(e)	Determination of adjusted basis of specified tangible property	Specified tangible property placed in service before enactment of §951A	The proposed regulations should be amended to provide that a CFC switching to ADS for pre-enactment assets will not need to file Form 3115 requesting an accounting method change for depreciation and that the cumulative adjustment will be taken into account to the tax basis of the fixed assets as of the CFC's first day of the first year that enactment applies.	It is very common practice for taxpayers to simply use U.S. GAAP depreciation for U.S. E&P depreciation. The administrative and practical burden to both taxpayers and the IRS would be substantial if Form 3115 is required. The cumulative adjustment should affect only

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				post-enactment tax years and not pre-enactment tax years.
Prop. Regs. §1.951A-3(h)	Anti-abuse rules for certain transfers of property	12-month rule	The 12-month rule is burdensome and does not provide appropriate exceptions. The regulations should provide exceptions for transactions that are unlikely to result in abuse. Exceptions could include: (1) an exception for property transferred during ordinary course of trade or business; (2) an exception for transfers from one tested income CFC to another tested income CFC, where the U.S. shareholder is the same and where the CFCs together hold the property for more than 12 months; (3) an exception for property purchased or sold to an unrelated party; and (4) a de minimis exception (e.g., the rule should not apply unless it would decrease a CFC's QBAI by more than 10%, or $20 million).	The per se rule is overly broad, arbitrary, and administratively burdensome to both the IRS and taxpayers, and may apply in circumstances where there is no potential for abuse. For example, transfers of assets from one CFC to a related CFC may be driven by valid business operation reasons and would not in fact reduce the U.S. shareholder's GILTI inclusion, because the U.S. shareholder for both CFCs does not change. Providing exceptions for transactions that are unlikely to result in abuse would avoid the harsh application of such an overly broad rule, without penalizing ordinary business operations. It could also help the enforcement of the rules by easing the administrative burdens for both the IRS and the taxpayer.
Prop. Regs. §1.951A-4(b)	Definitions related to specified interest expense	Tested interest expense	The regulations should be amended to provide that interest expense accrued/paid by a CFC to a U.S. shareholder or an affiliate in that U.S. shareholder's U.S. consolidated group is excluded from the definition of "tested interest expense."	Reducing QBAI for interest where the interest income is subject to tax in the United States does not comport with the policy of the rule, which is to deny the double benefit of an interest deduction and increased QBAI. Because here, the interest deduction does not provide a benefit when the interest income is subject to U.S. tax at full rates.

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Prop. Regs. §1.951A-6(e), Preamble I.G.3.	Adjustments to basis related to net used tested loss	Reduction in basis meant to prevent double benefit of losses likely to lead to denial of even a single benefit in many cases.	The basis reduction rules in Prop. Regs. §1.951A-6(e) should be withdrawn. Treasury has indicated that the downward adjustment is required to prevent a duplicative benefit of the net tested loss. This attempt to eliminate a double benefit for economic losses will often result in the denial of even a single deduction for economic losses, particularly when accounting for the FTC impact associated with the net GILTI inclusion. Alternatively, there are two options that provide relief. Alternative one is: • The amount of the downward basis adjustment is reduced by the GILTI deduction percentage in §250(a)(1)(B); • The amount of the downward basis adjustment is zero with respect to any tested loss used in a year in which the U.S. shareholder is in an excess foreign tax credit position in the GILTI basket OR the taxpayer has no GILTI inclusion because Net Deemed Tangible Income Return exceeds aggregate tested income. Alternative two is Treasury also could consider making the use of tested losses to offset tested income elective so that taxpayers can choose to forgo the tested income offset in exchange for not reducing stock.	Tested losses in many situations will not result in any reduction in GILTI tax owed even if such tested losses reduce net tested income. This may result from several factors including anticipated GILTI basket FTC limitations or highly taxed offshore earnings. Requiring the taxpayer to reduce stock basis (and thus increase gain or decrease loss on subsequent disposition) when the theoretical income offset has had no economic consequences is inappropriate. Example (assumes no expenses allocated to GILTI basket). USP owns all shares of CFC1 and CFC2. CFC1 has $1000 of tested income and pays $350 of local taxes on this income. CFC2 is a new start up and has $100 of tested losses. GILTI Tax Computation <u>without</u> use of tested loss: Tested Income = $1,000 Foreign Taxes = $350 Grossed Up GILTI Income =$1350 Section 250 deduction = $675

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				Taxable Income = $675 Tentative Tax = $142 FTC with 80% haircut = $280 GILTI Tax (Tentative tax less FTC) = $0 GILTI Tax Computation <u>with</u> use of tested loss: Tested Income = $900 Allowable Foreign Taxes (90% of taxes) = $315 Grossed Up GILTI Income =$1215 Section 250 deduction = $607.5 Taxable Income = $607.5 Tentative Tax = $127.58 FTC with 80% haircut = $252 GILTI Tax (Tentative tax less FTC) = $0 A tested loss generates, at most, a 10.5% tax benefit, or for a taxpayer with excess GILTI credits, a 0% tax benefit. If the taxpayer later sells the stock of the CFC generating a NUTLA to a third party, and the CFC has no earnings and profits, the gain is subpart-F, passive gain taxed at 21%. Consequently, there will be taxpayers that recognize no benefit from the tested loss, but nevertheless, these taxpayers are required to reduce the stock basis

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				of the CFC at disposition, and are taxed on the corresponding gain at 21%. Furthermore, a taxpayer may receive no U.S. tax benefit from a "used tested loss" if the taxpayer does not have a GILTI inclusion (e.g., because the taxpayer's net deemed tangible return exceeds the taxpayer's pro rata share of CFC tested income). The proposed basis reduction rules would apply even in a circumstance where a taxpayer did not receive any U.S. tax benefit at all from its pro rata share of "used tested losses."