WASHINGTON TAX UPDATE:
CONGRESS, TREASURY, GLOBAL

Potomac LAW GROUP PLLC

April 2019 **Susan Rogers**

The House **failed to override the President's veto of a congressional resolution that would have prevented him from using a national emergency declaration to fund a border wall** so the issue will now go the courts. Other issues being considered by the House include health care, equal pay, climate change, ethics and campaign reform, and investigations related to the Mueller report on Russian interference in US elections, while the Senate will consider the Green New Deal, which was approved by the House. House Democratic leadership introduced legislation that aims to update and strengthen the **Affordable Care Act** at the same time that the White House announced that it would move forward with efforts to repeal and replace the ACA. With Republicans in control of the Senate and action unlikely on issues of importance to Democrats, most of this activity is designed to provide messaging tools for Democrats going into the 2020 elections.

Brexit chaos continues after the U.K. Parliament voted on March 13th to rule out the possibility of leaving the European Union without a withdrawal agreement, which eased fears that Britain would crash out of the EU's legal and regulatory framework without a transition period. The Parliament voted on March 14th on a delay of three months from the March 29th departure date to gain more time for reaching a deal, which will require EU agreement. **Voting continues in the Parliament in an effort to find a plan that can be approved by Parliament and agreed to by the EU.** EU officials have stated that no delay will be approved without an explanation from the UK of what will be accomplished with the extra time.

In This Issue

Ms. Rogers also publishes "Washington & the World: US & International Tax" covering newsworthy tax issues affecting cross-border business.

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Susan Rogers has 30 years of experience in the tax policy field in Washington including five years as Majority Tax Counsel to the US House Ways & Means Committee and several years of experience managing global tax issues for a Fortune 100 multinational.

Additional Tax Resources at Potomac Law Group:

- **Viva Hammer joined the firm from the Joint Committee on Taxation where she was a leader on the international provisions of the 2017 tax reform, the Tax Cuts & Jobs Act. She has also served at the Office of Tax Policy at the Treasury Department, focusing on the taxation of financial institutions and products.**
- **Matthew Lykken has 3 decades of planning and audit experience in international corporate tax in a variety of industries, including roles as global head of tax and regional director.**

The Tax-Writing Committees

House Ways & Means Committee: The Committee held a **hearing on March 27th that focused on taxpayers who did not benefit from the TCJA**. Republican members of the Committee argued that the TCJA has resulted in major capital business investments, historic wage growth, and increased employment. Democratic members disagreed with these conclusions stating that the law has created disparities between income levels and between capital investments in the US and abroad. The hearing highlighted the disagreement over several provisions of the law including the deduction for state and local taxes (SALT), the 20 percent deduction for passthrough business income, the earned income and child tax credits, charitable contributions, corporate tax rates, the standard deduction, and international tax reforms.

The Committee is scheduled to hold its **first legislative markup on April 2nd** with bills covering **retirement savings incentives and IRS reform**. Bipartisan legislation was released on March 28th called the Taxpayer First Act of 2019 covering changes to the IRS's organizational structure, enhancements to its information technology and cybersecurity operations, revisions to its enforcement policies, and improvements in customer service. Bipartisan legislation was also introduced on retirement savings covering a $500 credit for employers that automatically enroll employees in retirement accounts, removing the age limit for taxpayers who want to contribute to IRAs, and changing the age at which account holders have to start making withdrawals, which is currently 72. A second bill that is expected to be added during the markup would implement a framework whereby small businesses could pool their retirement accounts into a system called Open Multiple Employer Plans. There was some disagreement within the Senate Finance Committee on how to proceed on the IRS with two bipartisan bills being produced, but the differences reportedly have been worked out, although no Committee action is scheduled. Ways & Means Committee Chairman Neal is reportedly considering the introduction of a national retirement savings program later in 2019.

Two members of the Committee introduced legislation that would **end capital gain treatment for income from carried interests**, which has a companion bill in the Senate. Two members of the House introduced legislation that would impose a **financial transactions tax** on the sale of stocks, bonds, and derivatives with a companion bill in the Senate.

Senate Finance Committee: Senators Scott (R-SC) and Booker (D-NJ) are considering legislation that would require the Treasury Department to track metrics on the **Opportunity Zone program**, which was included in the TCJA but without reporting requirements. The two Senators were the original sponsors of the program. SFC Chairman Grassley and Ranking Democrat Wyden released legislation that would retroactively extend through 2019 several temporary tax deductions, credit, and incentives that expired at the end of 2017 and 2018, but no action has been taken in the Committee.

Extenders: Chairman Neal had planned to include the issues of the extenders in the April 2nd markup, but **Committee Democrats were unable to reach a consensus on whether to reinstate all of the expired provisions** and whether the cost of the extensions would have to be offset. If agreement is reached, this legislation could be marked up later in April. Senate Minority Leader Schumer (D-NY) made recent statements that suggested that concessions might be needed from Republicans not only with respect to agreement on technical corrections to the TCJA, but also to agreement on certain extenders. It is unlikely that an extenders package would move forward in Congress until this fall when a number of issues are typically considered prior to adjournment for the year.

Joint Committee on Taxation (JCT): The JCT issued an **overview of the deduction for qualified passthrough business income under Code section 199A**, which was enacted as part of the TCJA and is effective for tax years starting in 2018. The new qualified business income deduction allows certain passthrough owners to deduct up to 20 percent of their qualified business income, plus 20 percent of the aggregate amount of qualified real estate investment trust (REIT) dividends and qualified publicly traded partnership (PTP) income. The IRS issued final regulations in February. The JCT also issued a new report called the "**Overview of the Federal Tax System as in Effect for 2019**." It does not include provisions that are scheduled to take effect after 2019, and it does not discuss termination dates for provisions that are due to sunset after 2025.

Congress & The Budget

The **FY 2020 budget submission** from the White House was released on March 11th. Treasury Secretary Mnuchin testified on the budget on March 14th before both the Ways & Means Committee and the Senate Finance Committee. The $4.7 trillion budget proposal for FY 2020 calls for a 5 percent reduction in non-defense spending and states that it balances revenue and spending within 15 years. The proposal includes increased spending for the IRS. In the past, the Treasury Department would typically issue a Green Book with more detailed explanations of the revenue proposals, but this practice has not been followed by the Trump Administration and this report is not expected this year.

The Republican-controlled Senate Budget Committee held a markup on March 27-28th and approved on a party line vote a proposed **FY 2020 budget resolution** with broad tax and spending goals for the next five years. The non-binding plan includes a reconciliation bill that would include $94 billion in deficit reductions over five years, with more than half of that coming from Senate Finance Committee issues. The Democratic-controlled House Budget Committee has not yet scheduled action on a budget resolution and is likely to take a different approach. Even if agreement were reached between the two houses of Congress on this issue, budget resolutions are not submitted to the President for approval and therefore, they do not carry the force of law.

Treasury and the IRS

Tax Cuts & Jobs Act Guidance

Treasury and the IRS have released a significant amount of guidance on the TCJA to date. Businesses should not delay in submitting comments on proposed rules. Treasury has until June 22, 2018, which is 18 months after the TCJA was enacted, to issue final rules that can operate retroactively back to the enactment date. On several key regulatory projects, Treasury has issued proposed rules and received public comments, but it has not yet released final rules. The intention is to complete all final international rules by late summer before companies are required to file their 2018 returns.

Underpayment Penalties for Individuals: The IRS lowered the withholding underpayment threshold to 80 percent for the 2018 tax year, down from the 85 percent cutoff announced earlier this year and the 90 percent threshold usually in effect. That means that filers who paid at least 80 percent of what they owe will avoid underpayment penalties.

Opportunity Zones: The Office of Information and Regulatory Affairs at OMB received the second set of regulatory guidance for review from the IRS concerning the Opportunity Zone (OZ) incentive. These rules are expected to address what type of property qualifies as qualified OZ business property, steps an OZ business must take to be qualified, and the penalty for a qualified opportunity fund's failure to meet the 90% investment standard.

Foreign Derived Intangible Income (FDII): The **IRS issued proposed regulations under Code section 250 on the deductions for foreign derived intangible income (FDII) and global intangible low-taxed income (GILTI).** The TCJA provides domestic corporations with a deduction for FDII and GILTI, applicable to tax years after 2017. A US shareholder of a controlled foreign corporation for any taxable year is required to include in gross income the shareholder's GILTI for the year. The proposed rules outline a series of rules and tests that companies have to satisfy to verify that their income is from foreign sales, and also include exemptions to some of the documentation rules for small businesses (less than $10 million in annual sales or less than $5000 from an individual customer), which were not included in the TCJA statute. Treasury also indicated that there would be distinction between sales and services, which received different treatment in the statute, based on the "overall predominant character of the transaction." This is a categorization area that could present challenges for taxpayers in interpretation and administration. The proposed rules cover applicability of the rules to partnerships, individuals, consolidated groups, and tax-exempt corporations. Written comments were due by March 6th.

Global Intangible Low-Taxed Income (GILTI): The proposed regulations issued on March 4th also covered issues related to the global intangible low-taxed income deduction in Code section 250, which requires a US shareholder of a controlled foreign corporation for any taxable year to include in gross income the shareholder's GILTI for the year and is designed to restrict a company's ability to shift profits offshore. The proposed rules allow individuals owning foreign corporations to use Code section 962 to be treated as if they were corporations, allowing them benefit from GILTI's 50 percent deduction, which under the statue was only available to corporations. Both FDII and GILTI are key elements of the international framework of the TCJA.

Base Erosion and Anti-Abuse Tax (BEAT): The IRS held a hearing for March 25th on proposed regulations relating to the Base Erosion and Anti-Abuse Tax which were issued on December 31, 2018. The tax is designed to serve as a minimum tax on certain taxpayers that reduce their overall tax liability by making deductible payments to related foreign parties.

Foreign Tax Credit Rules: The IRS held a public hearing on March 14th on its proposed regulations regarding changes to the foreign tax credit (FTC) and related rules for allocating and apportioning expenses for determining the FTC limitation that were made by the TCJA.

Treasury and the IRS - Other Issues

Regulatory Policy Announcement: Treasury and the IRS issued a joint policy statement announcing important **changes to the tax regulatory process and clarifying their views on less-formal "sub-regulatory" guidance,** which includes revenue rulings, revenue procedures, notices, and announcements. The new policy is more aligned with the established principles of the Administrative Procedure Act (APA) that historically has not always been applied to tax regulations. The key issue in the statement relates to the category of sub-regulatory guidance, which do not carry the force of law and therefore are interpretive rules that are not subject to the APA's notice-and-comment requirements, but courts have held that the IRS is bound by these forms of guidance. The statement holds that sub-regulatory guidance should not be used to modify legislative rules or create new ones, and therefore the IRS will not receive deference from courts for its interpretations, based on the *Auer* and *Chevron* cases. The statement also addresses issues related to a commitment to notice-and-comment rulemaking, limited use of temporary regulations, and notices announcing the intent to propose regulations.

Code Section 355 Spin-offs: The IRS issued Revenue Ruling 2019-09, which **suspends two long-standing rulings pending the completion of a study on the active conduct of a trade or business** under Code sections 355(a)(1)(C) and 355(b). The suspended rulings are Revenue Ruling 57-464 and Revenue Ruling 57-492. The IRS states that it is conducting a study "to determine, for purposes of section 355, whether a business can qualify as an ATB [active trade or business] if entrepreneurial activities, as opposed to investment or other non-business activities, take place with the purpose of earning income in the future, but no income has yet been collected."

International Issues

Digital Services Taxation/OECD—Global Minimum Tax: The OECD announced on January 29th that it is working toward a **consensus plan to taxing digital commerce** as part of the BEPS initiative. A **Consultation Document was issued on February 13th**, and interested parties were invited to comment by March 1st, and a public consultation meeting was held on March 13-14th in Paris. A detailed program of work will be considered at the Inclusive Framework meeting in May and presented to the G20 Finance Ministers meeting in June with a goal of a consensus-based long-term solution in 2020.

The OECD released more than 200 comment letters received in response to the public consultation, which began with the focus on the tax challenges of the digitalization of the economy but has now **broadened to a general discussion of countries' right to tax multinational group profits in all sectors.** Proposals under debate include a **minimum tax on multinational profits** and proposals that would allocate more taxing rights to market jurisdiction or jurisdictions where the users of digital services live.

EU Action on Digital Tax: EU Finance Ministers dropped their effort to adopt a proposal for an immediate, temporary, EU-wide digital tax on large global companies, which had been intended to be a stop-gap measure until a global consensus was reached on a long-term solution. The EU will focus on the discussions proceeding at the OECD and G20 level, and only revisit the issue on the EU level if consensus is not reached in 2020. The EU has called on France and other countries pursuing unilateral measures, including Belgium, Spain, the UK, Italy, and Austria, to focus their efforts on reaching consensus at the EU level and at the OECD.

France Digital Tax: After the failure to adopt an EU-wide digital tax, the French government published a draft bill proposing a new 3 percent tax on the revenue of large digital companies applying retroactively to January 1, 2019. The bill was presented to the cabinet and is expected to be presented to the Parliament in early April. The tax would apply to online marketplaces, the sale of data for targeted advertising, and the sale of targeted online advertising. France has said that it would terminate its tax once an OCED solution has been agreed. Treasury Secretary Mnuchin has expressed his opposition to a unilateral French proposal, and **Chip Harter, Treasury's Deputy Assistant Secretary for International Tax Affairs called the new tax "highly discriminatory**," stating that Treasury, the US Trade Representative's office and US lawmakers are studying whether the discriminatory impact would give the US rights under trade agreements, WTO and treaties. During a hearing on the Administration's budget proposal, **Ways & Means Committee Chairman Neal commented on the OECD work on the taxation of digital commerce** stating, "That work has the potential to affect a wide range of US businesses and taxpayers, and the US tax base." He said he intends to pay close attention to those developments, especially in light of France's recent unilateral imposition of a digital services tax, and he asked Secretary Mnuchin to keep him fully informed on the issue as the OECD works on a consensus plan.

OECD: The **OECD released a report** assessing whether the 127 members of the "Inclusive Framework on BEPS" are following through on their commitments to add provisions to their tax treaties to stop a practice known as "**treaty shopping**," which allows multinational businesses to avoid tax on cross-border transactions. The report finds that 82 of the 116 members as of June 30, 2018, have either some agreements that are already compliant with the standards or that are expected to be compliant soon.