WASHINGTON TAX UPDATE:
CONGRESS, TREASURY, GLOBAL

May 2019 **Susan Rogers**

Congress returned to Washington after a 2-week recess to face a busy agenda including post-Mueller report investigations and continuing hearings on a number of oversight issues. They also must deal with budget and spending issues with a difference of opinion in the House and Senate over how to proceed this year. The Democratic-controlled **House Budget Committee** opted to **forego drafting a budget resolution** and instead chose to advance legislation that would lift the statutory caps on defense and nondefense discretionary spending for the next two years. The caps are enforced by the Office of Management and Budget through a mechanism known as the "sequester" which prevents spending in excess of the statutory caps. The Republican-controlled **Senate Budget Committee** had already approved a proposed **FY 2020 budget resolution** with broad tax and spending goals for the next five years.

A planned vote in the House on the budget legislation was cancelled due to disagreement within the Democratic party about the bill, including from progressives who wanted additional domestic spending and moderates, who were reluctant to support the changes necessary to satisfy progressives, citing concerns about the impact on the deficit. **Negotiations have now shifted to House Speaker Pelosi (D-CA) and Senate Majority Leader McConnell (R-KY)** with a goal of reaching agreement in time to prevent the need to pass a continuing resolution prior to the start of the fiscal year on October 1st.

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 Treasury Department has not met the request from Ways & Means Committee Chairman Neal (D-MA) for 6 years of **tax returns for President Trump**, pursuant to Code section 6103(f), which states that the Treasury Secretary "shall" provide tax return information of any individual at their request. Although Treasury Secretary Mnuchin has not yet refused to produce the returns, it is expected that this issue will end up in the courts for resolution. Three Democratic members of the Committee introduced legislation that would include energy storage technologies as eligible to collect the ITC, and over 100 House Democrats have sent a letter to Chairman Neal urging the committee to include several **clean-energy tax policies** in any upcoming tax legislation that advances, including tax credits for wind and solar energy.

Senate Finance Committee: Ranking Democrat Wyden (D-OR) has announced that he intends to introduce a proposal in the form of a white paper that would establish an **annual mark-to-market approach for taxing certain capital assets** with the intent of providing an idea for possible change should the Democrats retake the Senate, and he becomes Chairman again. This new idea is reportedly broader than his 2016 legislation which would have applied to derivative contracts not entered into to hedge business risks. Reports are that the new proposal would require some capital assets to be marked-to-market annually with any resulting gain taxed at ordinary rates, rather than the preferred rate which caps at 23.8 percent under current law for capital assets with long-term holding periods.

Extenders: Chairman Neal had planned to include the issue of the extenders in an early April 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. **Senate Finance Committee bipartisan leadership has introduced a bill** that would renew all the expired tax benefits through 2019 retroactive to the beginning of 2018, but since tax bills must originate in the House, they are waiting for a vehicle to come from the House with a tax title to which they could add their legislation. 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 Joint Committee on Taxation issued a pamphlet on **changes to income recognition** that resulted from the TCJA, titled "Overview of Modifications to Income Recognition under Section 451 by Public Law 115-97." The TCJA added two new provisions to Code Section 451 and the report explains the process for realizing and recognizing income, with examples illustrating the deferral of advance payments and the modification of the "all events test" for severable and non-severable services.

IRS Reform Legislation: The House approved the Taxpayer First Act with a bipartisan voice vote on April 9th, while SFC Chairman Grassley and ranking Democrat Wyden have co-introduced identical legislation but have not yet scheduled action in the Committee. The bills include provisions that would update IRS technology, address cybersecurity, and make various improvements to customer service and tax administration. This legislation has a good chance of final passage in Congress, but there are disagreements about a handful of provisions including the Free File program and limits on private debt collection.

Infrastructure Legislation: Democratic Congressional leadership met with President Trump to discuss infrastructure legislation, which enjoys bipartisan support, but may still have a challenging path to approval before the 2020 elections. Issues include the revenue offsets that would be needed to fund the legislation, including the approval of a proposed increased gas tax and cutbacks to the benefits included in the Tax Cuts & Job Act, and whether Democrats would agree to give the President a major achievement on this issue prior to the 2020 elections.

Retirement Legislation: Congress has started a **bipartisan, serious effort to pass retirement legislation** that would make a number of taxpayer-friendly changes for small businesses and individual taxpayers. The Ways & Means Committee approved the Setting Every Community Up for Retirement Enhancement (SECURE) Act, which would make more than two dozen policy and administrative rule changes to various retirement plan options. The revenue costs to the bill would be offset by changes within the framework of the legislation that raise revenue so that overall the bill would result in a small revenue gain. House leadership has suggested a Floor vote might occur prior to the Memorial Day recess.

In the Senate, **SFC Chairman Grassley and ranking Democrat Wyden reintroduced an updated version of the Retirement Enhancement and Savings Act (RESA)**, which includes many of the same provisions as the SECURE Act. A Committee markup has not yet been scheduled. In 2016, a similar RESA bill was approved by the SFC, but was never brought to the Senate Floor for action, and Congress failed to achieve consensus on this issue at the end of 2018. With both tax-writing committees giving priority to retirement legislation this year, it appears likely that Congressional approval could be achieved.

FASB—Tax Information in Financial Statements: The Financial Accounting Standards Board (FASB) has revised its proposals for companies to be more transparent in financial statements about their domestic and foreign income tax liabilities in order to protect the interests of investors and analysts. **FASB reissued its draft proposal requiring businesses to release more details about their tax liabilities following changes to the tax law included in the TCJA**. The first draft of proposals was released in 2016 and put on hold in anticipation of tax reform. The amendments require a summary of domestic and foreign income or losses from continuing operations before income tax is taken into account, as well as federal, state and foreign income tax expenses or benefits. Public companies would also be required to disclose the amounts of unrecognized tax benefits and the line items on which they are presented in their financial position statements with a clarification that the disclosure of income taxes paid is required for interim periods.

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. 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 released final rules.

Opportunity Zones: The IRS issued **additional regulations** under Code section 1400Z-2 to implement the Opportunity Zone provisions of the TCJA with a public hearing scheduled for July 9th. The IRS also issued a notice asking for input on developing information collection and tracking related to investments in QOFs. The **new guidance is intended to provide answers to many questions** investors have had about the program which expires at the end of 2019. Key issues have included which businesses operating in an opportunity zone could qualify under the program and the treatment of proceeds from opportunity investments that are sold.

SALT guidance: The IRS issued **Revenue Ruling 2019-11**, providing guidance for taxpayers affected by the reduced deduction for state and local taxes (SALT). It **addresses this question**: If a taxpayer received a tax benefit from deducting state and local taxes under Code section 164 in a prior taxable year, and the taxpayer recovers all or a portion of those taxes in the current taxable year, what portion of the recovery must the taxpayer include in gross income? The guidance discusses four examples with concluding advice on how to report. During testimony on Capitol Hill, IRS Commissioner Rettig stated that **final regulations on the SALT deduction cap** would be released in the next couple of months. Ways & Means Committee Chairman Neal has stated that his Committee will form a working group designed to investigate the impact of the cap and possible amendments to it.

Base Erosion and Anti-Abuse Tax (BEAT): The **Joint Tax Committee issued a report** that provides an overview of the BEAT, including an explanation of the application of the BEAT and several examples for calculating the tax. The BEAT applies to corporations that have average annual gross receipts of at least $500 million for the last three tax years and whose base erosion percentage is 3% or higher.

Code section 163(j)/Limitation on Deduction of Business Interest: The TCJA significantly expanded the scope of Code section 163(j) by extending its application to individuals and partnerships and applying the limitation to interest paid to both related and unrelated parties. The new rule generally limits a taxpayer's business interest expense deduction to the sum of: (1) its business interest income; (2) 30 percent of its adjusted taxable income (ATI), which shall not be less than zero; and (3) floor plan financing interest. For taxable years beginning before January 2, 2022, ATI is taxable income computed without regard to interest, taxes, depreciation, and amortization. Any business interest expense disallowed may be carried forward indefinitely. The limitation generally does not apply to small businesses (other than tax shelters), regulated public utilities, and electing farming or real property trades or businesses. The Joint Committee on Taxation issued a report covering several aspects of the changes including its application to pass through entities, including partnerships and small businesses.

The IRS issued **proposed regulations** in November 2018, and **recently held a public hearing** to receive comments and recommendations. Witness suggestions included: (1) the real property trade or business (RPTB) anti-abuse rule should be dropped given the separate, general anti-abuse rule; (2) the definition of interest is too broad and should be restricted to what is generally treated as interest elsewhere in the tax code: (3) certain clarifications related to the floor plan financing exception are needed: and (4) the use of asset basis to determine the extent to which a trade or business is an excepted trade or business for purposes of Code section 163(j) is a reasonable method.

Treasury and the IRS - Other Issues

EIN Application Requirements: The IRS announced **changes in the process for applying for an Employer Identification Number (EIN)** so that only individuals with a Tax Identification Number (TIN) may request an EIN as the "responsible party." Generally, the responsible party is the person who ultimately owns or controls the entity or who exercises ultimate effective control over the entity. This change will enhance security and transparency by prohibiting entities from using their EINs to get additional EINs. There is, however, no change for tax professionals who may act as third-party designees for entities and complete the paper or online applications on behalf of clients. The changes are effective May 13, 2019.

IRS Priority Guidance Plans: The IRS issued a **second quarter update to their 2018-2019 Priority Guidance Plan**, which was issued in November of 2018 covering the plan year from July 1, 2018 through June 30, 2019. The update states that the IRS has completed 44 of the 239 projects, added 38 additional projects, and comments that the partial government shutdown affected the release of some guidance. The IRS also issued **Notice 2019-30, which invites comment on the 2019-2020 Priority Guidance Plan** which will be released soon covering the period from July 1, 2019 through June 30, 2020. The deadline for comments is June 7, 2019, and the Notice summarizes several factors used when decisions are made about the inclusion of projects.

Transfer Pricing Litigation: **IRS Commissioner Rettig** recently spoke at a Washington tax conference, where he said that despite the fact that the IRS has seen a number of defeats in court on transfer pricing issues including in cases involving Amazon, Veritas Software, and Medtronic, the **IRS will continue to litigate the issue** as part of their enforcement plan. The IRS is also increasing its hiring in the criminal investigation unit demonstrating an emphasis on enforcement and deterrence.

International Issues

Brexit: Brexit chaos has continued in the UK as the Government struggles to find a plan that can be approved by Parliament and agreed to by the EU. The EU has now agreed to **delay the date for Britain's departure until as late as October 31st**, while including an option to leave earlier if the UK government can secure parliamentary approval for a departure plan. Without this agreement, the UK would have "crashed" out of the EU on April 12th without a regulatory relationship or transition period. The lengthy 6-month delay is intended to give the UK government time to build consensus around an exit plan without requiring repeated requests for extensions of the departure date. **Conditions are required** including that the UK will participate in the May 23rd elections for the European Parliament and will not use its veto on budget and project planning votes. In the interim, the UK remains a member state with full rights and obligations under EU law. EU leaders will meet in June to review the UK's progress. Although the EU has suggested Britain may have to resort to new elections or a second referendum, the Government continues to support a plan under which there would be a specific transition period with regulatory status quo while a trade relationship is worked out.

Digital Services Taxation/OECD—Global Minimum Tax: The OECD is working toward a **consensus plan to taxing digital commerce** as part of the BEPS initiative, but the debate has now broadened to a general discussion of global tax rules including addressing which countries are allowed to tax certain profits of multinationals and ensuring that multinationals pay their fair share of taxes. A detailed program of work will be presented to the G20 Finance Ministers meeting in June with a goal of a consensus-based long-term solution in 2020. The final plan will have to be agreed to by the 129-member Inclusive Framework on BEPS. The **Netherlands has now joined France and Germany in support of a global minimum tax proposal**, similar to the new US Global Intangible Low-Taxed Income Tax (GILTI), which would address the fairness issue. Having the Netherlands as an ally is an interesting development considering that the country has historically been a business-friendly jurisdiction.

US Activity/Digital Taxes: **Bipartisan leadership** of the two tax-writing committees issued a statement on April 10th **criticizing unilateral digital service taxes**. "The tax challenges that have arisen due to digitalization of the economy affect businesses headquartered all over the world, and solutions to these challenges are best negotiated multilaterally. We are supportive of the United States participating in the ongoing OECD negotiations on these solutions. We call on other countries to focus on and engage productively in the OECD dialogue in order to reach measured and comprehensive solutions and abandon unilateral measures." In an acknowledgement of unilateral action, including by France, the statement said that "even on an interim basis, unilateral actions, such as digital services taxes proposed by some countries, can adversely affect US businesses and have negative economic and diplomatic effects." Finally, the statement says that they look forward to engaging with the Treasury Department and evaluating the outcome of the OECD's work and its impact on US taxpayers and the US Treasury.

EU Action on Digital Tax: The EU's Competition Commissioner, Margrethe Vestager, has stated her **support for EU countries who are moving ahead with national digital tax proposals**, including France, noting that although a global solution is preferable, the national activity will deliver necessary pressure for action at the EU and global level. Multinationals who are affected had been hoping to pursue state aid cases with respect to the national digital taxes.