WASHINGTON TAX UPDATE: CONGRESS, TREASURY, GLOBAL

Potomac LAW GROUP PLLC

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Congress returned on June 3rd from a recess to face a number of pressing issues. **Negotiations on budget and spending legislation are in the hands of 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. The goal is a bipartisan deal that would cover 2019 and 2020. Another financial issue that must be dealt with by September is the need to increase the **debt ceiling limit**, which governs the federal government's ability to borrow. Absent an increase, automatic mandatory cuts in both defense and domestic federal spending will occur with draconian effect — and, at this point, there does not appear to be a plan for managing this issue in a timely fashion.

Congress passed a $19 billion disaster relief bill, which was signed by the President. The House passed an immigration bill, but it is unlikely to advance in the Senate, following the similar fate of other Democratic agenda items, including health care, gun control, climate change, and elections security. The **escalating conflict between the US and China on trade policy** has resulted in dueling tariff increases and significant drops in the US stock market with no clear resolution in sight. Many in the Republican Party disagree with Administration policy but do not appear ready to challenge them beyond some verbal complaining.

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.

She is based in Southern Maine with firm offices in Washington, DC, and Boston. Her practice focuses on federal, state, and global tax developments and strategic management of tax risks for those businesses who need to understand the substance, process, and politics of tax issues. She has extensive experience in training personnel on tax advocacy issues through seminars, webinars, and company meetings.

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

For additional information and subscription details, please contact:
Susan Rogers, Partner
202.492.3593
srogers@potomaclaw.com
Southern Maine, Washington DC, and Boston

The Tax-Writing Committees

House Ways & Means Committee: The Committee held a **hearing on May 15th on climate change** covering the economic and health impacts along with the use of the tax code to address the issue. Committee Democrats discussed carbon pricing as a way to reduce emissions, but no specific proposals for implementing carbon pricing were endorsed. The Baker-Schultz Carbon Dividends Proposal was discussed by the chairman of the Climate Leadership Council, which is supported by a number of large companies including from the energy industry. The proposal would implement an escalating fee on companies' carbon emissions, beginning at $40 per ton, in exchange for a rollback of regulations on greenhouse gases. The fees collected would be returned to US households in the form of quarterly dividend payments. Committee Republicans argued against a carbon tax stating their preference for new tax incentives for clean energy development and federal investment in innovative technologies. The Committee also held a **hearing on the "tax gap"** – the difference between federal taxes owed and paid on a timely basis – and how to reduce it. The IRS has estimated the tax gap to be around $450 billion for the 2008-2010 timeframe. Chairman Neal cited decreases in the IRS enforcement budget and audit efforts as contributing to the problem, and he also noted that the tax gap could be underestimated due to the fact that it does not cover international noncompliance.

Senate Finance Committee: Ranking Democrat Wyden (D-OR) introduced the **Clean Energy for America Act**, which would combine 44 energy-related tax incentives into 3 new permanent green energy incentives, while **repealing all tax incentives for fossil fuels**. The legislation would provide up to a $1-per-gallon tax credit for fuels that are at least 25% cleaner than average, a 30% investment tax credit to clean electricity or a 2.4 cent-per-kilowatt hour credit for production, a tax credit for energy-efficient homes, and a tax deduction for qualifying commercial buildings. Chairman Grassley (R-IA) and Ranking Democrat Wyden (D-OR) announced that the **Committee has initiated an investigation into potential abuse of the Code section 170 tax deduction for conservation-oriented land donations, which are known as syndicated conservation easements**.

Extenders: SFC Chairman Grassley announced the **formation of several bipartisan task forces** to examine the expired and expiring tax provisions designed to make decisions on the issue of permanency or permanent expiration. In connection with the announcement, the Joint Committee on Taxation issued a report on tax provisions that expired in 2017 and 2018, and those set to expire in 2019. Five of the task forces deal with the issue areas of: (1) workforce and community development; (2) health taxes; (3) energy; (4) business cost recovery; and (5) combined group of individual excise taxes and other temporary policies. These task forces will consider "whether a continued short-term extension is sufficient to achieve the policy goals, whether a long-term extension is desirable to force a future Congress to reevaluate the provision down the road, or if permanency is warranted. A sixth task force will focus on related issues of temporary disaster tax relief and consider whether a permanent disaster relief tax provision should be enacted. All task forces are due to issue reports and recommendations by the end of June.

Ways & Means Democrats have held several meetings to discuss tax extenders but have not been able to reach consensus on whether and how to offset the cost of an extender package and a concern that the benefit of most extenders goes to businesses who are already seen to have benefited disproportionately from the 2017 tax law. Chairman Neal has suggested the possibility of a Committee "walk-through" of the issues in the near future and said that he has spoken to Chairman Grassley about acting soon on extenders. Reports are that Ways & Means Democrats are considering attaching an extension of the Earned Income Tax Credit to the bill and possibly using the estate tax as a pay-for by terminating the TCJA estate tax changes in 2023 rather than 2025.

IRS Reform Legislation: **The House approved the IRS reform bill** on a voice vote in early April and sent the legislation to the Senate, where originally it was expected to also pass easily, but its progress has been blocked by several Democrats who have raised objections to a provision in the legislation that would codify the IRS Free File program, which is a partnership between the IRS and private software providers that was established to make no-cost tax return preparation software available to certain lower-income taxpayers. The initial concern was that codifying the program would prevent the IRS from developing its own return preparation software and offering it to the public directly. Then concerns arose about the current program due to press reports that some private software providers were hiding details about their Free File software on internet search engines and steering taxpayers instead to fee-based products. The IRS Commissioner has now said that the agency is bringing in an independent consultant to review Free File. Members of both parties appear to be interested in resolving this issue with the expectation that the legislation will move forward at some point.

Infrastructure Legislation: A second meeting between the White House and Democratic Congressional leaders to discuss funding for infrastructure legislation produced no progress on the issue, which was caught up in political disagreements about other issues. Also, the President had sent a letter to the leaders prior to the meeting stating that he was not willing to work on infrastructure issues until Congress passes the US-Mexico-Canada Agreement, which is a replacement for the North American Free Trade Agreement. Although there continues to be bipartisan support for moving ahead on an infrastructure bill, the issue is not on a fast track for action in 2019.

Retirement Legislation: The House approved by a bipartisan vote of 417-3 the Setting Every Community Up for Retirement Enhancement (SECURE) Act, which would encourage individuals to participate in retirement plans, make it easier for smaller businesses to offer tax-qualified retirement savings plans to their employees, and promote savings for certain nonretirement expenses. SFC Chairman Grassley and Ranking Democrat Wyden had introduced their own version of retirement legislation in April, but they are considering a process by which the Senate would approve the House-passed version of the bill. The resolution of these issues will be taken up after June 3rd when Congress returns from the Memorial Day recess.

Treasury and the IRS

Tax Cuts & Jobs Act (TCJA) 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.

The Treasury Department's Inspector General for Tax Administration issued a **report on the status of TCJA guidance** developed and published by the Office of Chief Counsel. As of the beginning of the 2019 Filing Season, Chief Counsel had issued 79 published TCJA guidance products with four additional guidance products issued prior to April 1st. The report stated that Chief Counsel planned to issue more than 90 published guidance products after March 29th. There are currently several guidance products under review by the Office of Management and Budget for publication in the Federal Register.

Global Intangible Low-Taxed Income (GILTI): Final GILTI regulations are expected to be issued in the near term. At a recent ABA tax meeting, a Treasury representative suggested that the final rules may include a high tax exception that would exclude income that is already subject to a foreign tax rate above 13.125%. Questions about US partners in partnerships that own controlled foreign corporations with a GILTI inclusion will likely be answered after June 22nd according to comments from an IRS official at the ABA meeting because they will be addressed in forthcoming regulations on previously taxed earnings and profits, which are on a longer timeline than the GILTI final regulations, that will focus on how corporations determine that type of income in general.

Section 956/Repatriation: The IRS issued final regulations that reduce the amount of income included under Code section 956 for certain domestic corporations. The final rules exclude corporations that are US shareholders (as defined in Code section 951(b)) from the application of Code section 956 to maintain symmetry between the taxation of actual repatriations and the taxation of effective repatriations. In general, under Code section 245A and the final regulations, respectively, neither an actual dividend to a corporate US shareholder, nor such a shareholder's tentative Code section 956 amount, will result in additional US tax.

Code section 163(j)/Limitation on Deduction of Business Interest: A Treasury official stated at the recent ABA tax meeting that they are reviewing guidance related to the debt interest deduction limit, and that the second set of rules under Code section 163(j) should include tax treatment of debt-financed distributions and the definition of interest subject to the deduction limit with the possibility of narrowing that definition.

Treasury and the IRS - Other Issues

IRS Personnel: The IRS announced the appointment of Peter Blessing to the position of Associate Chief Counsel, International, Office of Chief Counsel. The Associate Chief Counsel, International, is responsible for coordinating and directing all activities of the international component of the Office of Chief Counsel, which provides legal advisory services on all international and foreign tax matters, related to the activities of non-US taxpayers within the US and the activities of US or US-related taxpayers outside the US.

Ownership Attribution for CFCs: The IRS issued proposed rules that provide ownership attribution guidance for controlled foreign corporations. The IRS explains that the guidance provides rules "regarding the attribution of ownership of stock or other interests for purposes of determining whether a person is a related person with respect to a controlled foreign corporation (CFC) under section 954 (d)(3)." The proposed rules also provide guidance on determining whether "a CFC is considered to derive rents in the active conduct of a trade or business for purposes of computing foreign personal holding company income (FPHCI)."

IRS Compliance Campaigns: The IRS launched two new compliance campaigns by the Large Business and International (LB&I) Division focused on **offshore banking** and **the filing of information Form 5471** by officers, directors, or shareholders in certain foreign corporations. The offshore private banking campaign addresses tax noncompliance and the information reporting associated with these offshore accounts. The goal of the Form 5471 campaign is to improve compliance with the requirement to attach a Form 5471 to an income tax, partnership or exempt organization return.

Transfer Pricing Compliance Campaign: The IRS Large Business and International Division (LB&I) announced a new compliance campaign targeted at transfer pricing involving foreign captive service providers. The campaign is designed to ensure that US companies pay no more than arm's length prices to foreign subsidiaries that perform services exclusively for the parent or other members of the multinational group. The IRS said it would conduct issue-based examinations and issue soft letters as a part of the campaign.

Withholding & Reporting of Dispositions of Partnership Interests: The IRS issued proposed regulations on withholding, reporting, and paying tax under Code section 1446(f) upon the sale, exchange, or other disposition of an interest in a partnership described in Code section 864(c)(8) and proposed section 1.864(c)(8)-1 of the income tax regulations. The proposed guidance is based on guidance provided in Notice 2018-29.

International Issues

Brexit: Following the EU Council approval of an extension to Article 50 to delay the Brexit date to October 31, 2019, the UK Government continues to struggle to find a successful path to consensus. After failing again to gain Parliamentary approval of her compromise Brexit plan, PM May resigned on June 7th but will stay on as Prime Minister until the Conservative Party chooses a new leader. The UK was required to hold elections to the European Parliament, and the "Brexit Party," which ran a no-deal platform gained more votes than any other party. This result has pushed leading contenders for the Conservative Party leadership to include the possibility of a no-deal exit as an option, but that option is unlikely to be approved by Parliament and could result in a vote of no-confidence in the new Government. Under the agreement with the EU, the UK may reconsider their entire Brexit strategy, but the extension agreement precludes reopening the withdrawal agreement. The UK may also revoke Article 50 and cancel Brexit altogether.

Digital Services Taxation/OECD—Global Minimum Tax: The OECD is working toward a **consensus plan to tax digital commerce** as part of the BEPS initiative, but the debate has 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 has been released and will be presented to the G20 Finance Ministers meeting in June with a goal of a consensus-based long-term solution in 2020. An increasing number of EU countries are moving to adopt unilateral digital taxation proposals with most citing the failure of the EU to adopt an EU-wide tax during its March meeting. Countries moving ahead with proposals include Poland, Czechoslovakia, Israel, Mexico, Malaysia, Austria, India, Italy, New Zealand, and Spain.

US Activity/Digital Taxes: At an ABA tax meeting, Deputy Assistant Secretary of International Tax Affairs, Chip Harter, said there is interest on the part of several countries within the OECD in the adoption of a global minimum tax similar to that included in the 2017 US tax law, but that the technical challenge of drafting the rules will be great. Recent comments from the Treasury's Deputy International Tax Counsel suggested that any deal reached at the OECD level on a global minimum tax is likely to represent a "looser consensus" leaving the details of implementation to individual countries. At the ABA meeting, Mr. Harter stated that "vigorous diplomacy" is ongoing by the US in an attempt to stop countries from adopting unilateral tax measures that target digital companies, including from France and the UK. The US is arguing that the unilateral measures are political and should be deferred while the OECD is working toward a global consensus approach.

Netherlands Tax Ruling Practice: The Dutch government published a draft decree and guidance proposing higher standards for obtaining advance tax rulings and advance pricing agreements on international tax matters from the Dutch tax authorities as well as establishing new transparency rules and procedures for Dutch tax rulings. The proposals are expected to take effect on July 1st.

European Union: The European Commission prepared a document outlining 6 areas of taxation that need work, which will be used to prepare a strategic agenda for 2019-2024. The areas include: (1) enactment of a common consolidated corporate tax base (CCCTB); (2) EU list of non-cooperative tax jurisdictions; (3) transparency for multinationals with respect to aggressive tax planning (4) taxation of digital activities; (5) creation of a single VAT area; and (6) EU qualified majority voting on tax issues.