

# WASHINGTON TAX NEWS



Potomac Law Tax Newsletter—March 2018

Susan Rogers

The President delivered his first **State of the Union address** on January 30<sup>th</sup> with comments focusing on immigration reform and infrastructure spending. The White House released its FY 2019 budget proposal on February 12<sup>th</sup> with the Treasury releasing its annual **Greenbook**, which provides an explanation of the Administration’s revenue proposals. Tax proposals are included in the following areas: international, small business, job creation and manufacturing, infrastructure, the financial sector, individuals and families, retirement and health benefit plans, tax administration, and the imposition of an oil fee.

The **Bipartisan Budget Act of 2018** (“Budget Act”), which was approved by Congress and signed into law by the President in early February, is a two-year budget agreement that sets defense and non-defense spending levels for two years, extends several expired temporary tax provisions (“extenders”), provides tax relief for victims of several 2017 natural disasters, and includes a handful of changes to the tax reform legislation enacted in late 2017, the Tax Cuts and Jobs Act (“TCJA”).

The bill was agreed to by Congressional leadership after a brief government shutdown with the key focus of the bill being to lift the statutory caps on defense and domestic appropriations for the remainder of fiscal year 2018 and for fiscal year 2019 which begins on October 1<sup>st</sup>. The deal allows for increased appropriations of nearly \$300 billion with \$165 billion allocated to defense and \$131 billion for domestic spending.

***For more information on these issues, please contact Susan Rogers at [srogers@potomacclaw.com](mailto:srogers@potomacclaw.com) or 202.492.3593.***

***Due to the scope of the Budget Act of 2018, there is speculation that it will be the last piece of significant legislation Congress advances prior to the 2018 mid-term elections apart from appropriations legislation.***

***Susan Rogers***



## In This Issue

- 2018 Legislative Agenda
- Tax Extenders
- Treasury and the IRS
- Tax Reform Update
- International Issues

## 2018 Legislative Agenda

The Budget Act also included a **Continuing Resolution** (“CR”) that extends government spending at current levels until March 23<sup>rd</sup>, giving Congressional appropriators additional time to pass appropriations legislation that allocates the spending totals to specific programs. It is possible that Congress will cover an extension of the so-called Dreamers program in the CR if a bipartisan solution can be found.

The Budget Act extends the “**mandatory sequester**” mechanism for 2 years through fiscal year 2027. The mandatory sequester on discretionary spending, which is part of the Budget Control Act of 2011, operates to require mandatory cuts in certain non-exempt mandatory spending programs, and it was included as a means by which to offset part of the budgetary cost of the discretionary spending increases in the legislation.

As part of the deal, Senate leaders agreed to increase funding for infrastructure, child care programs, opioid abuse programs, and “adequate funding” for the IRS. Also included was suspension of the federal debt limit until March 1, 2019, taking a politically contentious issue out of the mix this year.

Finally, the Budget Act also included an extension of funding for the Children’s Health Insurance Program (“CHIP”) for four years through 2028, reauthorization of the Community Health Centers program, extension of several provisions known as the “health extenders,” and the establishment of two bipartisan, bicameral “Joint Select Committees” that will make legislative recommendations by November 30, 2018, to reform the budget and appropriations process and improve the solvency of multiemployer pension plans.

The Administration released a summary of its **infrastructure plan** stating that a more complete plan would be introduced in the future. Although the issue has generated bipartisan interest, it appears unlikely that this legislation will advance in the near future.

## White House FY 2019 Budget

The Ways & Means Committee held a hearing on the **Administration’s FY 2019 budget proposal** and the implementation of the TCJA including testimony from Treasury Secretary Mnuchin. The Senate Finance Committee held two hearings on the FY 2019 budget proposal and TCJA implementation with testimony from both Treasury Secretary Mnuchin and Acting IRS Commissioner and Assistant Secretary for Tax Policy Kautter. In his opening statements, SFC Chairman Hatch (R-UT) restated his position that it is Congress’ responsibility to clarify and, if needed, fix questions about the TCJA.

## Tax Extenders

The Budget Act included the **extension of a number of temporary tax deductions, credits, and incentives** that expired at the end of 2016 generally through 2017 including: (1) commercial and residential investment tax credits for certain energy property; (2) several energy provisions including the Code section 45 production tax credit, the credit for new energy-efficient homes, credits for fuel cell and plug-in electric vehicles, and incentives for biodiesel and renewable diesel fuels; (3) several economic development incentives; and (5) individual incentives including the deduction for qualified tuition and related expenses and the gross income exclusion for discharge of indebtedness on a principal residence.

Following enactment of these extensions, the new Chairman of the W&M Tax Policy Subcommittee, Congressman Vern Buchanan (R-FL), stated that he plans to hold a hearing on March 14th to examine the provisions that are temporary and must be extended. W&M Chairman Kevin Brady has stated that the rationale of each expired provision must be re-evaluated “in a post-tax reform world.”

## Treasury and the IRS

The White House announced that the President plans to officially nominate **Charles P. Rettig** to become the next **Commissioner of the IRS**.

Treasury and the IRS issued a second quarter **update to the 2017-2018 Priority Guidance Plan**, which outlines the guidance the IRS expects to issue during the period from July 1, 2017 - June 30, 2018. This update reflects 29 additional projects resulting from tax reform and other priorities that relate to Treasury’s agenda to minimize regulations perceived as being unnecessary, imposing excessive burdens, and creating undue complexity. New projects include guidance related to (1) the 20% deduction for pass-through businesses; (2) withholding; and (3) international provisions, including the deemed repatriation tax.

The IRS issued a **proposed regulation aimed at repealing 298 regulations and modifying another 79** that would be affected by the repeals. This regulation relates to two executive orders directing agency heads to identify and reduce unnecessary, costly, and overly burdensome regulations.



## **State Governments React to Tax Reform**

*Federal tax reform has caused most states to consider what changes are needed to their state tax systems in response. While the new federal law affects every state with an income tax system, the states most affected are those that use federal taxable income as a starting point and those that use federal standard deductions or personal exemptions.*

*Several states have proposed legislation to deal with conformity issues, but the majority of states have not, because they have not had adequate time to review and assess the impact of the federal changes. Because the federal changes are effective for 2018, however, states need to consider changes to their state tax systems now so that they are prepared for the filing season in 2019.*

*States with high state and local taxes including California and New York are working on ways to mitigate the cap on deduction for state and local taxes paid, while a number of other states are working on similar ideas including Connecticut, Illinois, Maryland, Nebraska, New Jersey, Virginia, Washington and the District of Columbia. Governors of New York, Connecticut, and New Jersey have launched a coalition to sue the federal government over this issue.*

## **TAX REFORM UPDATE**

### **IRS Guidance**

**Limits on business interest:** At a recent ABA meeting, an Attorney-Advisor in the Treasury Office of Tax Legislative Counsel, commented that an anti-abuse rule for the new limitations on business interest expense may be considered by Treasury despite the fact that it is not specifically listed on the Treasury's Priority Guidance Plan. The Plan said that the IRS and Treasury were working on "computational, definitional, and other guidance" on the business interest deduction limitations under new Code section 163(j), and he stated that "other guidance" covers a possible anti-abuse rule. The TCJA amended Code section 163(j) to impose a 30 percent cap on net business interest expenses beginning in 2018. An exception to the limits is provided for the real estate and farming industries as well as for businesses with average annual gross receipts of \$25 million or less.

**Repatriation Tax:** The IRS issued Revenue Procedure 2018-17 under Code section 965(o), which modifies IRS procedures for changing the accounting period of foreign corporations owned by US shareholders subject to the tax on deemed repatriated earnings. The guidance prevents changes to the annual accounting periods of certain foreign corporations in 2017 under either the existing automatic or general procedures if such change could result in the avoidance, reduction, or delay of the transition tax. It applies to any request to change an annual accounting period that ends on December 31, 2017, regardless of when the request was made.

As part of its shift to a territorial system, the TCJA imposed a one-time tax on the deferred offshore earnings of US companies, applied either at 15.5% for cash or cash equivalent holdings or 8% for invested income. A number of measurement and definitional issues have arisen, and the IRS has identified this area as a priority for guidance with two pieces of guidance issued thus far. In the first notice, the IRS noted the risk that earnings and profits could be double-counted in cases when specified foreign corporations have inclusion years that don't align with the taxable years of a US shareholder. In the second notice, the IRS expanded on how debt is characterized when companies tally their offshore earnings.

Also, the US Chamber of Commerce has sent a letter to Treasury and the IRS asking for clarification of guidance that has been issued on this topic. Issues addressed include: (1) the November 2<sup>nd</sup> measurement date requirement for earnings and profits; (2) the definition of accounts payable; (3) the inclusion of current year 2017 taxable losses in the definition of "net operating loss"; and (4) the payment of tax liability in installments or deferral of inclusion of deemed repatriated income.

**Withholding:** The IRS issued Notice 2018-14, which provides additional guidance to employers on withholding changes in response to the enactment of the TCJA.

### **The Budget Act of 2018 Modifications**

The Budget Act which was enacted early in February included several modifications or clarifications to the TCJA covering the following areas: (1) the excise tax on the net investment income of colleges and universities; (2) the exception for the excess business holding rules for independently operated philanthropic business holdings; and (3) certain rules for craft beverages.

It also repealed a provision enacted in trade legislation in 2015 that increased corporate estimated tax payments otherwise due in July, August, or September of 2020 by 8% and reduced the payment due in October, November, or December of 2020 by the same percentage. Thus, payment for the third and fourth quarters of 2020 will be 100% of the amount due. Also included were a number of miscellaneous targeted tax law changes.

## **Technical Corrections**

**Carried Interest profits:** During an SFC hearing, Treasury Secretary Mnuchin was asked about reports that taxpayers will be able to avoid the new requirement that carried interests be held for three years to be taxed as capital gain, and he responded that IRS guidance to shut down this technique will be issued in the near future. Under the TCJA, general fund managers are required to hold investments for at least three years for carried interests to be treated as capital gains instead of ordinary income. The three-year rule, however does not apply when payments are made to companies rather than individuals, and some hedge funds have set up limited liability companies in Delaware to use the exception. He has met with IRS and Treasury staff and believes they will be able to close the loophole with existing authority under the code.

**Net Operating Loss Effective Date:** The net operating loss effective date no longer allows tax filers to spread out financial losses over past years, while under prior law, taxpayers could do so for two years.

**Repatriation tax:** Secretary Mnuchin has said that Treasury is working on issues related to the new repatriation tax and the calculation for deducting net operating losses under Code section 965(n).

## **International Issues**

The OECD released additional guidance and information on the **implementation of country-by-country reporting**. The additional guidance addresses two issues: the definition of total consolidated group revenue and whether non-compliance with the confidentiality, appropriate use, and consistency conditions constitutes systemic failure.

The European Commission Taxation and Customs Union has established a **website providing information about the impact of the United Kingdom's withdrawal from the European Union (EU) with respect to customs and tax matters**. According to the website, preparing for the UK's withdrawal in the area of customs and taxation is not just a matter for EU and national authorities but also for companies and individuals trading with the UK.

Eight members of the OECD Forum on Tax Administration (FTA), including Australia, Canada, Italy, Japan, the Netherlands, Spain, the United Kingdom, and the United States, launched a pilot for the voluntary **International Compliance Assurance Programme (ICAP)** for the multilateral risk assessment of large MNE groups. The ICAP pilot will use CbC reports and other information to facilitate open and co-operative multilateral engagements between MNE groups and tax administrations, with a view to providing early tax certainty and assurance.

### **For additional information and advice on these issues, please contact:**

**Susan Rogers, Partner**

Potomac Law Group, PLLC

One International Place, Suite 1400

Boston, MA 02110

**202.492.3593**

**[srogers@potomaclaw.com](mailto:srogers@potomaclaw.com)**

**Susan Rogers has 30 years of experience in the tax policy field in Washington including several years as Majority Tax Counsel to the House Ways & Means Committee and extensive experience managing global tax issues for a Fortune 100 multinational. Ms. Rogers' practice focuses on providing information and strategic advice to clients on US and international tax policy issues and advice on how to manage tax policy risks.**

Copyright 2017 Potomac Law Group, PLLC. All rights reserved. Any tax advice contained in this communication (or in any attachment) is not intended or written to be used, and cannot be used by any taxpayer, for the purpose of avoiding U.S. federal, state, or local tax penalties or promoting, marketing, or recommending to another party any transaction or matter addressed in this communication (or any attachment). The information contained herein is for informational purposes only and is based on our understanding of the current tax laws and published tax authorities in effect as of the date of publishing, all of which are subject to change. You should consult with your professional tax advisor to discuss the potential application of this subject matter to your particular facts and circumstances.