Hitotsubashi University

International Aspects of the U.S. Tax Reform and the New Tax Games

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Hiroyuki KOHYAMA

Associate Professor

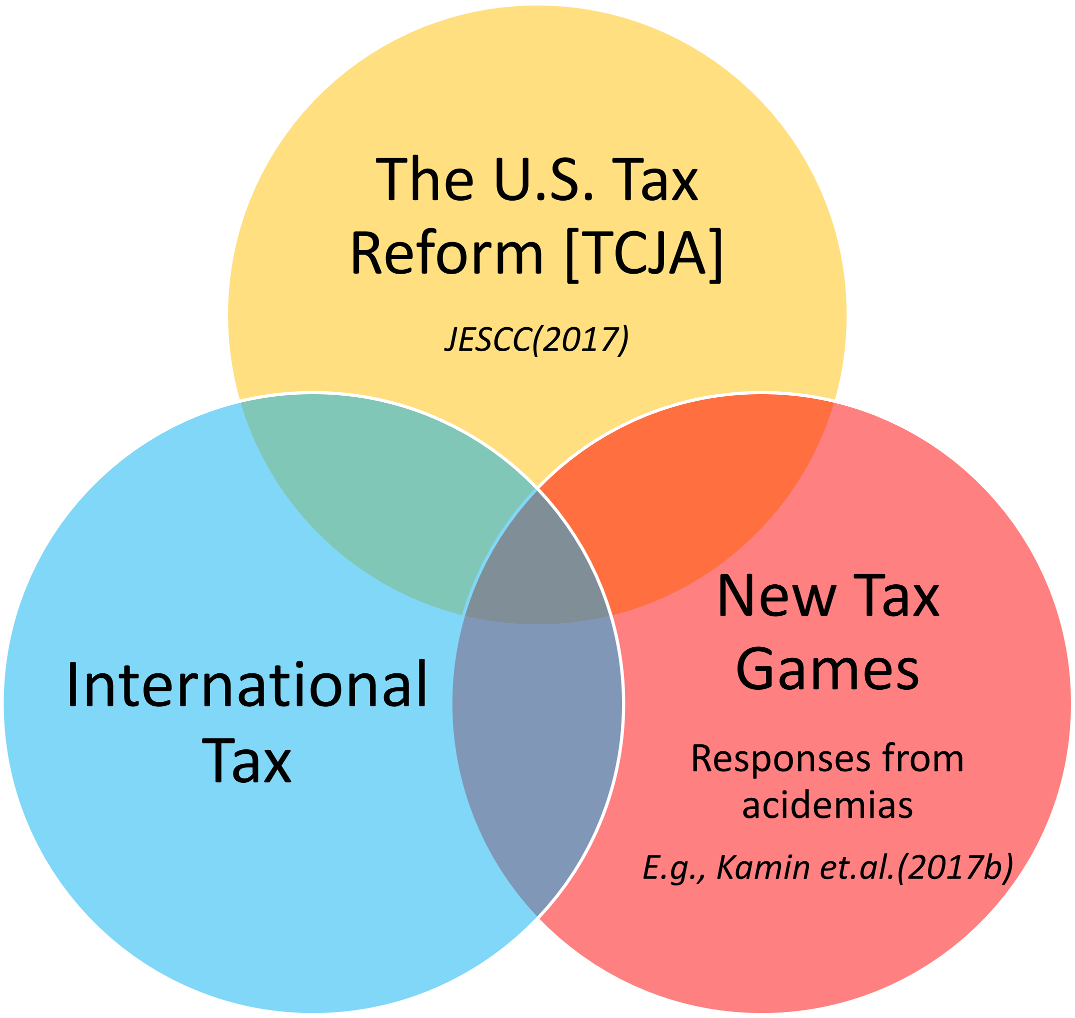
Hitotsubashi University, Graduate School of Law

Introduction

Today's Topic

"The new tax games in the era of the Tax Cuts and Jobs Act."

See, Kohyama(2018)



Focus

1. Participation Exemption System
2. GILTI (global intangible low-taxed income)
3. Deduction for FDII (foreign–derived intangible income) & GILTI
4. BEAT (base erosion and anti-abuse tax)

GILTI [IRC § 951A]
minimum tax on *intangibles*?

- "Under the provision, a U.S. shareholder of any CFC must include in gross income for a taxable year its global intangible low-taxed income ("GILTI") in a manner generally similar to inclusions of subpart F income." *[JESCC, at 515.]*

GILTI = Net CFC tested income − Net deemed tangible income return

Net deemed **tangible** income return = (QBAI × 10%) − interest expenses

QBAI means "the average of such corporation's aggregate adjusted bases as of the close of each quarter of such taxable year in specified tangible property". [§ 951(d)(1)]

New Tax Games under GILTI

- Kamin et.al. (2017b)

1. GILTI formula uses the "tangible income return" to calculate return from intangibles.
   - The U.S. firms will locate tangible asset (and accompanying jobs) overseas. *[id. at 18.]*
2. The high deemed return on tangible asset of 10%
   - A company can make its return (on investment in real assets abroad) completely exempt from U.S. taxation. *[id.]*
3. Global basis, not country-by-country
   - Firms are "incentivized to locate investment in low-tax countries and blend that income with income from high-tax countries". *[id. at 19.]*
4. Anti-taxpayer result
   - "If a firm borrows to buy an intangible asset, the interest expense reduces the exempt return rather than nonexempt income." *[id.]*

Kamin et.al.(2017b), at 18-19.

Implications?

GILTI formula

- the deemed tangible income return of 10%

U.S. firms

- Locate tangible assets on low-tax countries

Other countries

- Reducing their corporate tax rate?

Tax competition ?

Deduction for FDII & GILTI
[IRC § 250]

- A U.S. Domestic corporation shall deduct 37.5% of FDII and 50% of GILTI. *[After FY 2026: 21.875% of FDII and 37.5% of GILTI]*
- Reducing the effective (statutory) corporate tax rate
  - FDII: From [t = 21%] to [t =13.125%]
  - GILTI: From [t = 21%] to [t = 10.5%]

FDII = Deemed Intangible Income × Foreign-Derived Deduction Eligible Income ÷ Deduction Eligible Income

Deduction Eligible Income – Deemed tangible income return

QBAI × 10%

Total Tax Rate on GILTI

	Foreign tax rate on GILTI	US effective tax rate on GILTI	Total tax rate on GILTI
Case 1	0%	10.5%	10.5%
Case 2	13.125%	0%	13.125%
Case 3	16%	0%	16%

"Since only a portion (80 percent) of foreign tax credits are allowed to offset U.S. tax on GILTI, the minimum foreign tax rate, with respect to GILTI, at which no U.S. residual tax is owed by a domestic corporation is 13.125 percent." *[JESCC, at 498.]*

SOURCE: JESCC(2017), at 498-499.

New Tax Games under FDII

- Kamin et.al. (2017b)

1. The reduced rate on export income
   - U.S. firms have incentive to do resale transactions (or roundtripping transactions). *[id. at 19-20.]*
2. "The reduced rate on export income likely violates WTO obligations". *[id. at 20]*
3. The reduced rate on foreign derived intangible
   - "The export subsidy rate incentivizes firms to sell unfinished products to foreign manufacturers since these sales qualify for the lower rate whereas sales to domestic manufacturers do not". *[id. at 21.]*

Kamin et.al.(2017b), at 19-21.

BEAT
[IRC § 59A]

BEAT = 10% of the modified taxable income − (regular tax liability) – (tax credits)

(Taxable income) – (base erosion tax benefits)

"A base erosion payment includes any premium or other consideration paid or accrued by the taxpayer to a foreign person which is a related party of the taxpayer". *[JESCC, at 532.]*

New Tax Games under BEAT

- Kamin et.al. (2017b)

1. Non-compliance with WTO and tax treaty. *[id. at 21.]*
2. Causing double taxation *[id. at 22.]*
3. Additional planning opportunities
   - "If a foreign affiliate incorporates the foreign-held intellectual property into a product and then sells the product back to a U.S. affiliate, this could be considered cost of goods sold that is not captured by the inbound regime". *[id.]*

Implications ?

G20-OECD
BEPS projects

Minimum Tax

- U.S. BEAT
  U.K. & A.U. DPT
  EU proposal (2018)

BEPS Projects v. Minimum tax (BEAT & DPT)

- U.S. BEAT
- U.K. DPT, Australia DPT; "Google Tax"
- EU proposal (2018): Taxation on revenue from digital activities

BEPS projects		**Country B**	
		Honest	Fake
Country A	Honest	(3, 3) (A, B)	(1, 4)
	Fake	(4, 1)	(2, 2)

Reference

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