THE TOLL-CHARGE PLAYBOOK

January 2018

ALVAREZ & MARSAL
TAXAND

A STEP-BY-STEP EXAMPLE

A & M
TAXAND

Step-by-Step Guide to Toll-Charge Calculation

Base Facts

US Shareholder ("USSH") holds interests in three Specified Foreign Corporations ("SFC"). USSH and all three SFCs have 12/31 year-ends.

- USSHs are any US persons who own (directly, indirectly, or constructively) at least 10% of a foreign corporation
  - Corporations, individuals, partnerships, S-corporations, trusts, and estates can all be USSHs and, therefore, can all be subject to the toll-charge

- Specified Foreign Corporations include:
  - Controlled Foreign Corporations; and
  - Any foreign corporation with at least one domestic corporation which is a USSH

This example assumes that the USSH's ownership interest in each SFC has not fluctuated during the course of ownership. Taxpayers with historical ownership of CFCs and/or other 10%-owned foreign corporations whose ownership has fluctuated will need to apply year by year ownership percentages to the underlying earnings to determine the amount of applicable E&P and FTCs.*

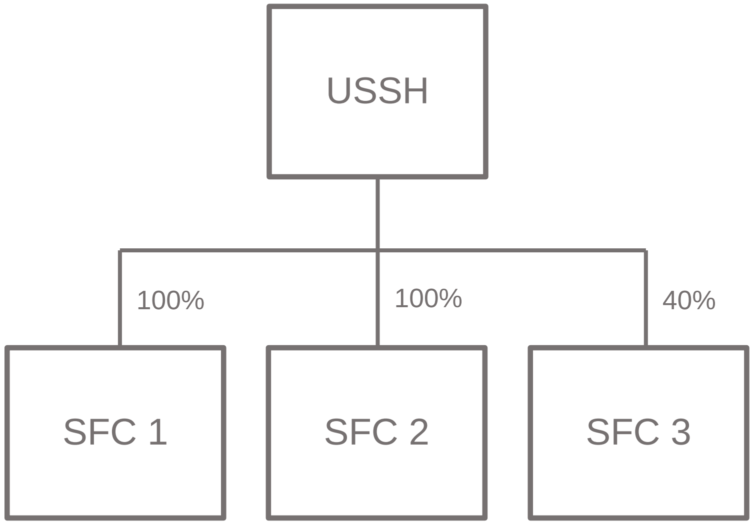
*A&M intends for the following sample playbook to serve as an illustrative guideline for assessing the time, resources and information necessary to calculate the transition tax (i.e., toll charge) under the Tax Cuts and Jobs Act. We have based this fact-specific example on numerous assumptions which would be different for each taxpayer, and would cause different results. Also, the underlying rules we have applied are subject to change, e.g., with the issuance of additional IRS Regulations or other guidance. Therefore, do not rely on this calculation. Please contact A&M with any questions.

Step-by-Step Guide to Toll-Charge Calculation

Base Facts

USSH COMPANY PROFILE	
2017 TI w/o Toll-Charge	100,000
NOL Carryforward	20,000
FTC Carryforward	10,000

Foreign Subs (Directly Owned by US)	SFC 1	SFC 2	SFC 3
Earnings and Tax Pools			
Ownership Percentage	100%	100%	40%
Earnings & Profits at 11/2/2017	140,000	(25,000)	50,000
Earnings & Profits at 12/31/2017	150,000	(30,000)	60,000
ECI E&P	20,000	-	-
Pre-2017 Previously Taxed Income	25,000	-	-
2017 Traditional Subpart F Income	10,000	-	-
2017 Actual Distributions	5,000	-	-
Tax Pool at 12/31/2017	50,000	10,000	15,000
Cash Position			
Cash Equivalents at 12/31/2015	45,000	25,000	5,000
Cash Equivalents at 12/31/2016	50,000	20,000	10,000
Cash Equivalents at 12/31/2017	60,000	15,000	5,000



ALVAREZ & MARSAL
TAXAND

Step-by-Step Guide to Toll-Charge Calculation

Step 1: Calculate Sec. 965(a) Earnings Amount (ADFI)

	SFC 1	SFC 2	SFC 3
E&P as of 11/2/2017	140,000	(25,000)	50,000
Less: ECI E&P	(20,000)	-	-
Less: Pre-2017 PTI	(25,000)	-	-
Less: PTI from 2017 Subpart F Income	(10,000)	-	-
ADFI as of 11/2/2017	85,000	(25,000)	50,000
Ownership Percentage	100%	100%	40%
USSH's Pro-Rata Share of ADFI as of 11/2/2017	85,000	(25,000)	20,000
Deferred Foreign Income Corporation?	YES	NO	YES
E&P as of 12/31/2017	150,000	(30,000)	60,000
Less: ECI E&P	(20,000)	-	-
Less: Pre-2017 PTI	(25,000)	-	-
Less: PTI from 2017 Subpart F Income	(10,000)	-	-
ADFI as of 12/31/2017	95,000	(30,000)	60,000
Ownership Percentage	100%	100%	40%
USSH's Pro-Rata Share of ADFI as of 12/31/2017	95,000	(30,000)	24,000
Deferred Foreign Income Corporation?	YES	NO	YES
Greater ADFI of DFICs	95,000	-	24,000
Sec. 965(a) Earnings Amount			**119,000**

Begin by calculating E&P of each SFC as of November 2, 2017 and December 31, 2017.

E&P will be reduced by ECI, Pre-2017 PTI, and PTI from 2017 Subpart F Income. The result is the Accumulated Foreign Deferred Income ("ADFI"), which refers to the modified E&P base used to determine the toll-charge.

Multiply ADFI by the USSH's pro-rata share (i.e. its ownership percentage in each SFC).

Aggregate only those SFC's in which the USSH has a *positive* ADFI. These entities are referred to as Deferred Foreign Income Corporations ("DFICs").

Compare the results from the two testing dates. The greater of which will be used moving forward.

Step-by-Step Guide to Toll-Charge Calculation

Step 2: Allocate E&P Deficits and Calculate Sec. 965(a) Inclusion Amounts

	SFC 1	SFC 2	SFC 3
Specified E&P Deficit as of 11/2/2017	NO	YES	NO
Specified E&P Deficit as of 11/2/2017	-	(25,000)	-
Aggregate Foreign E&P Deficit			**(25,000)**
Allocation of Aggregate Foreign E&P Deficit			
Pro-Rata Share of ADFI of DFICs	95,000	-	24,000
Percentage Share of Total ADFI of DFICs	79.8%	0.0%	20.2%
Allocated Foreign E&P Deficit	(19,958)	-	(5,042)
ADFI of DFICs after Deficit Allocation	75,042	-	18,958
Sec. 965(a) Inclusion Amount			**94,000**

Aggregate all SFC's with negative E&P.

Allocate deficit against the ADFI of DFICs (i.e. SFC's with positive E&P).

- Calculate percentage of SFC's positive E&P to the aggregate ADFI determined in Step 1.
- Allocate deficit by such percentage.

Aggregate the SFC's ADFI with deficit allocation.

ALVAREZ & MARSAL
TAXAND

Step-by-Step Guide to Toll-Charge Calculation

Step 3: Calculate Aggregate Foreign Cash Position

	SFC 1	SFC 2	SFC 3
Ownership Percentage	100%	100%	40%
Pro-Rata Share of Cash Position as of 12/31/2015	45,000	25,000	2,000
Pro-Rata Share of Cash Position as of 12/31/2016	50,000	20,000	4,000
Average of Prior 2 Years' Cash Positions	47,500	22,500	3,000
Aggregate Cash Position from Prior 2 Years			**73,000**
Pro-Rata Share of Aggregate Cash Position as of 12/31/2017	60,000	15,000	2,000
Aggregate Cash Position from Current Year			**77,000**
Greater of Current Cash Position of Prior 2 Years' Average			**77,000**

Determine USSH pro-rata share of cash position for each SFC as of 12/31/15, 12/31/16, and 12/31/17.

Average the cash positions as of 12/31/15 and 12/31/16, and then aggregate all SFC's. This results in the Prior 2 Year Aggregate Cash Position.

Compare Prior 2 Year Aggregate Cash Position to the USSH's pro-rata share of the cash position as of 12/31/17. The greater amount is deemed the Aggregate Foreign Cash Position.

Anti-Abuse rules may ignore transactions intended to manipulate cash position.

In Notice 2018-07, the IRS has indicated the Treasury's intent to issue regulations that will provide for certain receivables and payables between related SFCs will be disregarded in calculating cash and equivalents.

Step-by-Step Guide to Toll-Charge Calculation

Step 4: Calculate Tax Pools Deemed Distributed

	SFC 1	SFC 2	SFC 3
Tax Pool Available for Distribution before 2017 Inclusions	50,000	10,000	15,000
Total E&P Pool	150,000	(30,000)	60,000
Less: Pre-2017 PTI Pool	(25,000)	-	-
Undistributed E&P	125,000	(30,000)	60,000
Current Year Traditional Subpart F Inclusion	10,000	-	-
Percentage of E&P Deemed Distributed	8.0%	0.0%	0.0%
Tax Pool Deemed Distributed	4,000	-	-
Tax Pool Remaining after Traditional Subpart F	46,000	10,000	15,000
Undistributed E&P After Traditional Subpart F Inclusion	115,000	(30,000)	60,000
Toll-Charge Subpart F Inclusion	75,042	-	18,958
Percentage of E&P Deemed Distributed	65.3%	0.0%	31.6%
Tax Pool Deemed Distributed	30,017	-	4,739
Tax Pool Remaining after Toll-Charge Subpart F	15,983	10,000	10,261

Determine the tax pools available for distribution before 2017 inclusions. Note that for purposes of this example, these numbers are given.

Apply traditional rules to determine the tax pool remaining after Traditional Subpart F inclusions.

Divide toll-charge Inclusion (i.e. the amount determined in Step 2) by the Undistributed E&P after accounting for any current traditional Subpart F inclusions. The resulting percentage is then applied to the tax pools (as determined after traditional Subpart F inclusions). Such amounts are deemed distributed. Any remaining amounts remain in the tax pools, and may only be available as a credit in future years to the extent of future Subpart F income generated by such SFC.

ALVAREZ & MARSAL
TAXAND

Step-by-Step Guide to Toll-Charge Calculation

Step 5: Calculate Current Year Actual Distributions

	SFC 1	SFC 2	SFC 3
Actual Distributions	5,000	-	-
Ownership Percentage	100.0%	100.0%	40.0%
Pro-Rata Share of Actual Distributions	5,000	-	-
Pre-2017 PTI Pool	25,000	-	-
PTI from Current Year Traditional Subpart F	10,000	-	-
PTI from Toll-Charge Subpart F	75,042	-	18,958
PTI at End of 2017	110,042	-	18,958
Actual Distributions in Excess of PTI	-	-	-

In the case of any actual distributions – determine whether actual distributions are in excess of PTI.

For purposes of this example, we assume that actual distributions will not exceed PTI.

Step-by-Step Guide to Toll-Charge Calculation

Step 6: Calculate Participation Exemption on Toll-Charge Subpart F Inclusion

	USSH Level
Gross Subpart F Income Under Toll-Charge	94,000
Amount Subject to 15.5% Rate (Aggregate Foreign Cash Position)	77,000
Amount Subject to 8% Rate (Remainder)	17,000
Participation Exemption on Cash-Equivalent E&P	
Sec. 965(a) Inclusion Amount Subject to 15.5% Rate	77,000
Deduction Allowable against Subpart F	(42,900)
Net Taxable Income Attributable to Cash E&P	34,100
Participation Exemption on Non-Cash E&P	
Sec. 965(a) Inclusion Amount Subject to 8% Rate	17,000
Deduction Allowable against Subpart F	(13,114)
Net Taxable Income Attributable to Non-Cash E&P	3,886
Net Taxable Income Attributable to Deferred Foreign Income	**37,986**

The participation exemption excludes a portion of the toll-charge Subpart F inclusion.

Determine the amounts subject to the varying rates:

- Amount subject to 15.5% rate is the Aggregate Foreign Cash Position as determined in Step 3.
- Remainder amount (Non-Cash E&P) is subject to 8% rate.

Participation Exemption allows the following deductions:

- A deduction equal to 55.7% of the amount subject to the 15.5% rate.
- A deduction equal to 77.1% of the amount subject to 8% rate.

ALVAREZ & MARSAL
TAXAND

Step-by-Step Guide to Toll-Charge Calculation

Step 7: Calculate Participation Exemption on Sec. 78 Gross-Up

	USSH Level
Taxes Deemed Paid by USSH on Toll-Charge Subpart F	34,756
Aggregate Sec. 965(a) Inclusion Amounts	94,000
Deductions Allowed by Sec. 965(c)	(56,014)
Net Income Subject to Toll-Charge	37,986
Proportion of Includible Amounts that are Taxable	40.4%
Deemed Paid Taxes Creditable and Includible Under Sec. 78	14,045

Aggregate tax pools deemed distributed with respect to toll-charge amount in Step 4. This equals the taxes deemed paid by the USSH on the toll-charge Subpart F inclusion.

Determine the percentage that the aggregate taxable amounts bears to the aggregate section 965(a) inclusion amounts. Multiply that percentage by the deemed paid taxes to determine the portion of the deemed paid taxes that are creditable under section 901 and includible in income under section 78.

Step-by-Step Guide to Toll-Charge Calculation

Step 8: Calculate 2017 Tax with and without Toll-Charge

	USSH Level
With Toll-Charge	
Taxable Income Without Regard to Subpart F	100,000
Traditional Subpart F Inclusion (Including Sec. 78 Gross-Up)	14,000
Toll-Charge Net Income (Including Sec. 78 Gross-Up)	52,031
Taxable Income before NOLs	166,031
Less: NOL Carryforward	(20,000)
Taxable Income after NOLs	146,031
Tax Rate	35%
US Income Tax before Credits	51,111
Current Year FTCs	(18,045)
FTC Carryforwards	(10,000)
US Tax Liability	23,066
Without Toll-Charge	
Taxable Income Without Regard to Subpart F	100,000
Traditional Subpart F Inclusion (Including Sec. 78 Gross-Up)	14,000
Taxable Income before NOLs	114,000
Less: NOL Carryforward	(20,000)
Taxable Income after NOLs	94,000
Tax Rate	35%
US Income Tax before Credits	32,900
Current Year FTCs	(4,000)
FTC Carryforwards	(10,000)
US Tax Liability	18,900
Increase in Tax Liability as a Result of Toll-Charge	**4,166**

Determine the increase in tax liability as a result of the toll-charge by calculating 2017 tax with and without the toll-charge.

Note that this example assumes that USSH has excess foreign tax credit limitation available to allow full credit for all creditable taxes. The existence of Overall Domestic Losses ("ODLs") and/or Overall Foreign Losses ("OFLs") may affect USSH's foreign tax credit limitation.

Step-by-Step Guide to Toll-Charge Calculation

Step 9: Calculate Payment Schedule Under Installment Election

	USSH Level
Year 1 Normal Tax Liability	18,900
Year 1 Toll-Charge Liability (8%)	333
Total Year 1 Tax Due	19,233
Year 2 (8%)	333
Year 3 (8%)	333
Year 4 (8%)	333
Year 5 (8%)	333
Year 6 (15%)	625
Year 7 (20%)	833
Year 8 (25%)	1,041

The toll-charge may be paid over a 8 year period with an election made at the time of the first payment. The first year will include the normal tax liability plus 8% of the toll-charge liability.

The toll-charge liability will be added to each following year in the indicated proportions.

USSHs may elect to not use NOLs to offset toll-charge liability.

Failure to fully and timely pay any portion of the toll-charge installments may result in acceleration of all remaining liability.

Step-by-Step Guide to Toll-Charge Calculation

Additional Issues to Consider

Sec. 904 Foreign Tax Credit Limitation:

- Current year foreign source income
- Overall Foreign Loss (OFL) and Overall Domestic Loss (ODL) recapture
- Current Year Excess Limitation Position

Election to forego NOL utilization

Foreign currency issues (e.g. 986 gain/loss)

Inconsistent year-ends between USSH and/or SFCs

Pro-ration of current year ECI E&P (if applicable)

Intercompany transactions between SFCs between measurement dates (11/2 and 12/31)

Alternative minimum tax calculations

Multiple US controlled groups

Non-corporate shareholders subject to toll-charge

Dividend distributions between SFCs

Non-CFC SFCs with PTI from prior year Subpart F inclusions

Changes in SFC percentage ownership before year-end

E&P from years that foreign entity was not an SFC

Cash and equivalents from non-corporate foreign entities

Foreign tax pools attributable to entities that made Sec. 338 elections (i.e. Sec. 902(m) limitation

State tax impacts

ALVAREZ & MARSAL
TAXAND

KEY CONTACTS

Alvarez & Marsal
Taxand

A&M Tax Reform International Specialists

ALBERT LIGUORI

Managing Director
New York
aliguori@alvarezandmarsal.com
+1 212 763 1638

JILL HARDING

Managing Director
San Francisco
jmharding@alvarezandmarsal.com
+1 415 490 2279

JUAN CARLOS FERRUCHO

Managing Director
San Francisco
jferrucho@alvarezandmarsal.com
+ 1 786 554 1771

KRISTINA DAUTRICH RAYNOLDS

Managing Director
Washington D.C.
kdautrichreynolds@alvarezandmarsal.com
+ 1 202 688 4222

KENNETH BREWER

Senior Advisor
Miami
kbrewer@alvarezandmarsal.com
+ 1 781 248 4332

NICK MCBEE

Senior Director
New York
nmcbee@alvarezandmarsal.com
+ 1 212 763 9838

ALAN CATHCART

Senior Director
San Francisco
acatchcart@alvarezandmarsal.com
+ 1 415 490 2310

KENNETH DETTMAN

Senior Director
Miami
kdettman@alvarezandmarsal.com
+ 1 305 704 6691

Disclaimer

These slides are a brief overview of legislation, therefore it is not a complete analysis and is not intended to be advice to any particular reader. The descriptions may be oversimplifications intended to highlight areas that may warrant further attention. The points contained herein should be reviewed with counsel or advisors in respect of any particular circumstances.

The information contained herein is of a general nature and based on authorities that are subject to change. Readers are reminded that they should not consider this publication to be a recommendation to undertake any tax position, nor consider the information contained herein to be complete. Before any item or treatment is reported or excluded from reporting on tax returns, financial statements or any other document, for any reason, readers should thoroughly evaluate their specific facts and circumstances, and obtain the advice and assistance of qualified tax advisors. The information reported in this publication may not continue to apply to a reader's situation as a result of changing laws and associated authoritative literature, and readers are reminded to consult with their tax or other professional advisors before determining if any information contained herein remains applicable to their facts and circumstances.

This publication is not intended to be used, and cannot be used, by a client or any other person or entity for the purpose of avoiding tax penalties that may be imposed on any taxpayer.

A&M intends for the following sample playbook to serve as an illustrative guideline for assessing the time, resources and information necessary to calculate the transition tax (i.e., toll charge) under the Tax Cuts and Jobs Act. We have based this fact-specific example on numerous assumptions which would be different for each taxpayer, and would cause different results. Also, the underlying rules we have applied are subject to change, e.g., with the issuance of additional IRS Regulations or other guidance. Therefore, do not rely on this calculation. Please contact A&M with any questions.

TAXAND