IRS and Treasury's intention, but "it seems permissive."

Hermiller said that "it's good to see Treasury take note of the drastically altered landscape of the post-pandemic economy and allow [qualified Opportunity Zone businesses] to respond and react without being boxed in because of technicalities under the rules."

The proposed regulations stem from the final Opportunity Zone regulations (T.D. 9889), which include a 31-month working capital safe harbor under which a qualified business can hold cash as long as it has a written plan in place and a reasonable written schedule, and the plan is executed in a manner consistent with what's in writing. ■

Senate International Plan Not Without Taxpayer 'Silver Linings'

by Andrew Velarde

Senate Democrats' international tax framework contemplates partial relief from several Tax Cuts and Jobs Act taxpayer-unfavorable provisions, but without details, it's unclear how much those changes will lessen the sting of tougher proposals.

"There's a silver lining, but how much of a silver lining . . . is really hard to quantify because you don't know what's behind the curtain," Kevin M. Jacobs of Alvarez & Marsal said.

In some ways, the framework, released April 5 by Finance Committee Chair Ron Wyden, D-Ore., and committee members Sherrod Brown, D-Ohio, and Mark R. Warner, D-Va., is similar to proposed changes envisioned by the Biden administration. Both propose key changes to the global intangible low-taxed income provision, including removing the exemption for returns of qualified business asset investment and increasing the GILTI tax rate.

In other ways, the plans differ significantly, including as they relate to other aspects of GILTI and the base erosion and antiabuse tax.

According to Ken Brewer of Alvarez & Marsal, the Biden proposal "puts its finger on an important point" about the impact on U.S. competitiveness.

"In order for either proposal to not have a negative impact on the competitiveness of the U.S. in attracting companies, they need to rely on other countries to do similar things — raise rates and tax low-taxed foreign income," Brewer said. "The more dramatic changes that we have . . . [it] tends to make the U.S. a less attractive place to set up a headquarters company and even to set up operations."

A Devil of a Time Discerning

While the administration calls for the elimination of BEAT and its triggering mechanism, replacing it with a new proposal targeting related-party payments based on an effective tax rate threshold, the Wyden plan would reform the often criticized TCJA provision. The framework calls for a second increased BEAT rate, above the existing 10 percent rate on income, on base erosion payments. But it isn't all bad news for multinationals.

"The BEAT should be reformed to capture more revenue from companies eroding the U.S. tax base, and use that revenue to support companies that are actually investing in America," the framework states. "Tax credits that support investment and opportunity here in the U.S. need to have their full value restored under the BEAT."

In addition to calling for restoring the full value of domestic tax credits, the framework acknowledges the concern over the lack of foreign tax credits under the BEAT, which the reform measures could remedy. The lack of FTCs under the BEAT has long been a major criticism of the provision, and Treasury has acknowledged that despite taxpayer concerns, it couldn't budge on that aspect because it is "hard-wired into the statute."

"In those cases where BEAT's hitting [taxpayers] because they are not getting the credit, that really wasn't the intention of who BEAT would target. . . . BEAT was intended to be an inbound provision," Robert Russell of Kostelanetz & Fink LLP said, pointing to the header labeled "Inbound Transactions" in the TCJA under which the BEAT is found and arguing that the disallowance of the credit enabled the BEAT to target outbound companies. "By making this change in the Wyden [framework], it's saying . . . 'let's write it to say what it means and not just get these [companies] that are caught in it by a poorly worded statute.'"

Jacobs acknowledged the possible taxpayer benefit of allowing credits against the BEAT but cautioned against too much optimism, given the lack of details, especially regarding the second rate bracket and what might constitute a base erosion payment. As to whether taxpayers would prefer a reformed BEAT to Biden's new stopping harmful inversions and ending low-tax developments (SHIELD) proposal, he also said it was too early to tell.

"Obviously, the devil you know makes modeling a lot easier, as you've already built the models and you only have to tinker with it," Jacobs said. "But as everything the TCJA has demonstrated in determining the modeling associated with it, the devil's in the details and . . . there's so much uncertainty."

Retooling the GILTI Engine

While both the administration and the Senate framework contemplate movement toward country-by-country application of GILTI, they differ in the specifics. One Senate option to achieve the objective of limiting the blending of rates to avoid encouraging profit shifting to low-tax jurisdictions would apply GILTI to a designated category of low-taxed jurisdictions.

"Ironically, the Trump Treasury Department already provided all the necessary operational details as part of their regulations creating an elective high-tax exclusion for GILTI," the framework states. "While the regulations were a dubious interpretation of current tax laws, the vast majority of these rules can be co-opted in a mandatory high-tax exclusion, but in a more effective and fair system."

Brewer said that when compared with Biden's plan, some of the language used by the Senate framework struck him as more political.

It's an interesting turn for Senate Democrats. In February 2020 Wyden, when introducing a bill along with Brown to block the high-tax exclusion as applied to GILTI, said Treasury had overstepped its authority in allowing companies to have access to the election.

"It would be poor planning to not rewrite [the GILTI statute] the way [Congress] wants it and just rely on the existing Treasury regs," Russell said. "The question was whether old Treasury had any firm ground to extend [the high-tax exception] to GILTI. . . . It wouldn't be a stretch at all to have to say you have to rewrite that in the statute."

Regs on the high-tax exclusion (T.D. 9902, REG-127732-19) have sought conformity between the GILTI high-tax exclusion and the subpart F high-tax exception and, for the sake of administrability, have moved toward a more targeted approach of using tested units to determine eligibility and permit some income blending under a combination rule.

"They are using the mechanics, but not necessarily starting from scratch. It's sort of retooling an engine," Jacobs said about the framework's proposal. "We have this methodology that identifies two pools of income, one that qualifies for high-tax [exception] and one that doesn't. Maybe we utilize that machinery, and maybe it needs to be tinkered with."

Economics vs. Jobs

As an "incentive to onshore research and management jobs," the framework also outlines another change to GILTI, namely eliminating the foreign tax credit penalties under the provision by allowing expenses for research and management that arise in the U.S. to be treated as domestic expenses.

"The foreign tax credit rules were created and have evolved over time to police abuse, but the interaction of the GILTI regime with the foreign tax credit limitation can create perverse incentives," the framework states.

While the headline GILTI rate now sits at 10.5 percent, the math is more complicated, and the actual rate can be considerably higher for some taxpayers. First, since GILTI only offers an 80 percent foreign tax credit, the rate works out to 13.125 percent. And even though lawmakers voted for the TCJA assuming that would be the maximum rate, GILTI could be even higher in practice because of expense allocation rules further reducing the cap on foreign tax credits that companies can claim.

Any legislative change — a change that the framework labels "simple" — that provides relief on management and research expense allocation could be taxpayer beneficial. For years, taxpayers have lobbied to turn off the allocation of expenses to GILTI.

"Other than interest expense, two of the more significant items in the foreign tax credit limitation that can be problematic are research and development and stewardship expenses, and that's exactly what the [framework] is talking about here," Brewer said.

According to Russell, the whole economic reason behind the allocation of R&D expenses is to benefit future product sales everywhere.

"You develop the vaccine in the U.S. that is then sold anywhere around the globe. Shouldn't some of those expenses be allocated to what happens over there?" Russell said. "But layered on top of tax policy is what are you incentivizing in terms of red, white, and blue jobs. . . . [The change] would not only be taxpayer favorable. I think they are right; it would be jobs favorable."

Russell added that he thinks the change could win bipartisan support.

Retroactivity

For Jacobs, one major question left completely unanswered in the framework and by the administration as it considers international reform is what the effective dates would be for any changes.

Retroactivity has been contemplated at least two other times in recent tax bills.

In March several Democratic legislators, including Senate Finance Committee member Sheldon Whitehouse, D-R.I., and House Ways and Means Committee member Lloyd Doggett, D-Texas, introduced the No Tax Breaks for Outsourcing Act (S. 714). In strengthening the inversion rules, that bill looks at acquisitions going back to December 22, 2017. But practitioners have expressed skepticism at retroactive enactment.

Although it is unrelated to international tax, Jacobs also pointed to a discussion draft released in March by Maryland Democrat Chris Van Hollen. That bill would make major changes to the way assets are taxed at death by subjecting to income tax stepped-up basis amounts with an exemption of $1 million. That discussion draft has a proposed effective date of January 2021.

Jacobs wondered what this might portend for international changes and if those proposals might also consider retroactivity.

"Are you encouraged to migrate [intellectual property], or do you not migrate? . . . If you do, are you stuck in the U.S.?" Jacobs asked, adding that taxpayers "don't want to pull the trigger too fast . . . . They're not sure how it's going to impact their businesses." ■