21 June 2019

Global Tax Alert

Report on recent US international tax developments – 21 June 2019

NEW! EY Tax News Update: Global Edition

EY's new Tax News Update: Global Edition is a free, personalized email subscription service that allows you to receive EY Global Tax Alerts, newsletters, events, and thought leadership published across all areas of tax. Access more information about the tool and registration here.

Also available is our EY Global Tax Alert Library on ey.com.

The United States (US) Senate Foreign Relations Committee will vote on protocols amending US tax treaties with Japan, Luxembourg, Spain, and Switzerland during a business meeting scheduled for 25 June 2019. The tax protocols have been awaiting action in the Senate for years and were held up over Committee member Rand Paul's concerns regarding information sharing provisions. Foreign Relations Committee Chairman Jim Risch has said the plan is to move rapidly on the protocols and that Senate floor time may be allocated to advance them.

The Committee's business meeting agenda does not list new US tax treaties with Chile, Hungary, and Poland. Foreign Relations Ranking Member Robert Menendez wrote to Treasury on 11 June regarding his concerns about possible reservations for the Internal Revenue Code[1] Section 59A Base Erosion and Anti-abuse Tax (BEAT) – enacted by the *Tax Cuts and Jobs Act* – that may be necessary for the Chile, Hungary, and Poland treaties. The issue could require more work to sort out and the proposed treaties could be scheduled for Committee action at a later date. If the Senate approves the agreements with any reservations, the Trump Administration would need to engage with each treaty partner to determine if the reservation is acceptable. Even if the Senate were to complete all the steps needed to approve one or more of the pending agreements before its August recess, the entry-into-force date would depend on the actions of the treaty partner.

Building a better working world

On the regulations front, the US Treasury and the Internal Revenue Service (IRS) late last week, on 14 June, released eagerly anticipated final regulations (TD 9866) on global intangible low-taxed income (GILTI) under Section 951A that are largely consistent with proposed regulations published in September 2018, but with certain modifications. Significantly, the final regulations provide an aggregate approach to partnerships for determining GILTI inclusions. (Proposed regulations issued at the same time, which taxpayers may rely on, would provide similar treatment for subpart F income inclusions.) The final regulations generally adopt the applicability dates of the proposed regulations, and therefore apply to taxable years of foreign corporations beginning after 31 December 2017 and to taxable years of US shareholders in which, or with which, such taxable years of foreign corporations end.

Along with the final regulations, Treasury also proposed new regulations (REG-101828-19) under Sections 951A and 958. The new proposed regulations include an election that would apply an elective high-tax exception to GILTI when the tax imposed on a tentative net tested income item exceeds an 18.9% corporate tax rate. The high-tax exception is proposed only; taxpayers may not rely on the exception. The applicability of the high-tax exception would be tested at the level of a single qualified business unit and would apply to all controlled foreign corporations (CFCs) controlled by the same domestic shareholders.

Also on 14 June, the Government released temporary regulations (REG-106282-18) under Sections 245A and 954(c)(6). The regulations deny, in whole or in part, the Section 245A dividends received deduction (DRD) to dividends sourced from earnings and profits generated from certain transactions occurring after 31 December 2017, but prior to the close of a taxable year to which the provisions of Section 951A do not apply (known as the GILTI gap period). They also deny, in whole or in part, the Section 245A DRD to dividends sourced from earnings and profits generated from tested income or subpart F income that would have been included in a US shareholder's income under Sections 951(a) or 951A(a), but for the transfer or dilution of that shareholder's direct or indirect interest in a CFC. The regulations extend these provisions to dividends received by an upper-tier CFC from a lower-tier CFC by denying the Section 954(c)(6) exception to foreign personal holding company income to similarly sourced dividends. The regulations apply retroactively to a dividend paid that occurs after 31 December 2017.

In a recent 2-1 ruling, a Ninth Circuit Court of Appeals panel reversed the Tax Court's 2015 holding in *Altera v. Commissioner*, and upheld a 2003 regulation that requires participants in a cost-sharing arrangement to share stock-based compensation costs. The Ninth Circuit panel concluded that the 2003 regulations were valid under the *Administrative Procedure Act* (APA). The Ninth Circuit panel held that, "[i]n sum, we disagree with the Tax Court that the 2003 regulations are arbitrary and capricious under the standard of review imposed by the APA. While the rulemaking process was less than ideal, the APA does not require perfection."

The ruling was the second time the Ninth Circuit had reversed the Tax Court's opinion. The Ninth Circuit in August 2018 withdrew its original opinion in *Altera* that was issued in July 2018 because one of the three judges on the panel that had heard the appeal died prior to the issuance of the opinion, but after oral arguments and after formally concurring in the majority opinion. The withdrawal of the original opinion was to allow time for a reconstituted panel to confer on the appeal.[2]

Finally, the IRS has indicated that the US and Cyprus are negotiating a competent authority agreement to exchange Country-by-Country reports. The arrangement would be based on the exchange of information provision in the 1984 Cyprus-US tax treaty.

Endnotes

1. All "Section" references are to the Internal Revenue Code of 1986, and the regulations promulgated thereunder.
2. See EY Global Tax Alert, *US Ninth Circuit panel reverses Tax Court opinion in Altera, holding stock-based compensation to be a compensable cost under IRC Section 482*, dated 17 June 2019.

For additional information with respect to this Alert, please contact the following:

Ernst & Young LLP, International Tax Services, Washington, DC

- Arlene Fitzpatrick arlene.fitzpatrick@ey.com
- Joshua Ruland joshua.ruland@ey.com

EY | Assurance | Tax | Transactions | Advisory

About EY

EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

EYG no. 003005-19Gbl

1508-1600216 NY
ED None

ey.com