Matinée fiscale de l’IFA

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La réforme fiscale américaine

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Programme

- Réduction du taux d'IS et autres mesures pour encourager l'investissement aux Etats-Unis
- Limitation sur la déduction des intérêts, BEAT, et autres mesures pour décourager l'érosion de la base imposable
- Les organigrammes en « sandwich » et l'application du nouveau régime (quasi) territorial
- Q&A

H.R. 1 key business provisions

Lower Corporate Rate – 21%

Participation Exemption & Mandatory Repatriation Tax

Immediate Expensing But Strengthened Interest Expense Limitation Rules

Net Operating Loss Limitations and Enhancements

Base Erosion Provisions

Tax on GILTI vs. FDII

Mesures pour encourager l'investissement aux Etats-Unis (US domestic provisions)

Provision	Summary	Effective
Corporate tax rate	Reduces corporate tax rate to 21%. Blended rates for fiscal year filers.	TYBA 31 Dec 17
Alternative Minimum Tax (AMT)	Repealed	TYBA 31 Dec 17
NOL deductions	Limited to 80% of taxable income; generally no carrybacks; indefinite carryforward	Effective for losses arising in TYBA 31 Dec 2017
Research activities	Retains the research credit Costs amortized over 5-yr period beginning in 2022 (15 yrs if the research is conducted off-shore)	Amortization rules effective for TYBA 31 Dec 2021
Cost recovery for depreciable property	100% expensing for tangible property other than real property; not limited to original use property; phases out in 2023-2026	Investments after 27 Sep 17 and before 1 Jan 23

Mesures pour décourager l’érosion de la base imposable (US domestic provisions)

Provision	Summary	Effective
Net business interest expense limitation	Disallows net business interest deductions in excess of 30% of “adjusted taxable income” (EBITDA for 5 years, and EBIT thereafter) Applies regardless of whether the debt is related or unrelated Disallowed interest carried forward indefinitely	TYBA 31 Dec 17 No grandfather rule for existing debt
Disallowance of deductions for hybrid payments	Denies deductions for interests or royalties paid to related parties, if paid pursuant to hybrid transactions, or by or to a hybrid entity.	TYBA 31 Dec 17

Example – 30% net interest expense limitation

Facts and Assumptions

— US domestic corporation (US Co) has EBITDA of $50 and EBIT of $35
— US Co has unsecured foreign related party borrowings of $200 at 6%, giving rise to $12 related party net interest expense
— US Co has secured third party borrowings of $400 at 4%, giving rise to $16 of third party net interest expense

US tax reform impact

Prior rules:

– § 163(j) limited foreign related party borrowings and/or borrowings guaranteed by a related party to 50% of EBITDA
– This would give rise to a limitation of 50% x EBITDA of $50 = $25
– Related party interest expense is only $12
– The full $28 interest expense would be deductible
– **No net interest limitation**

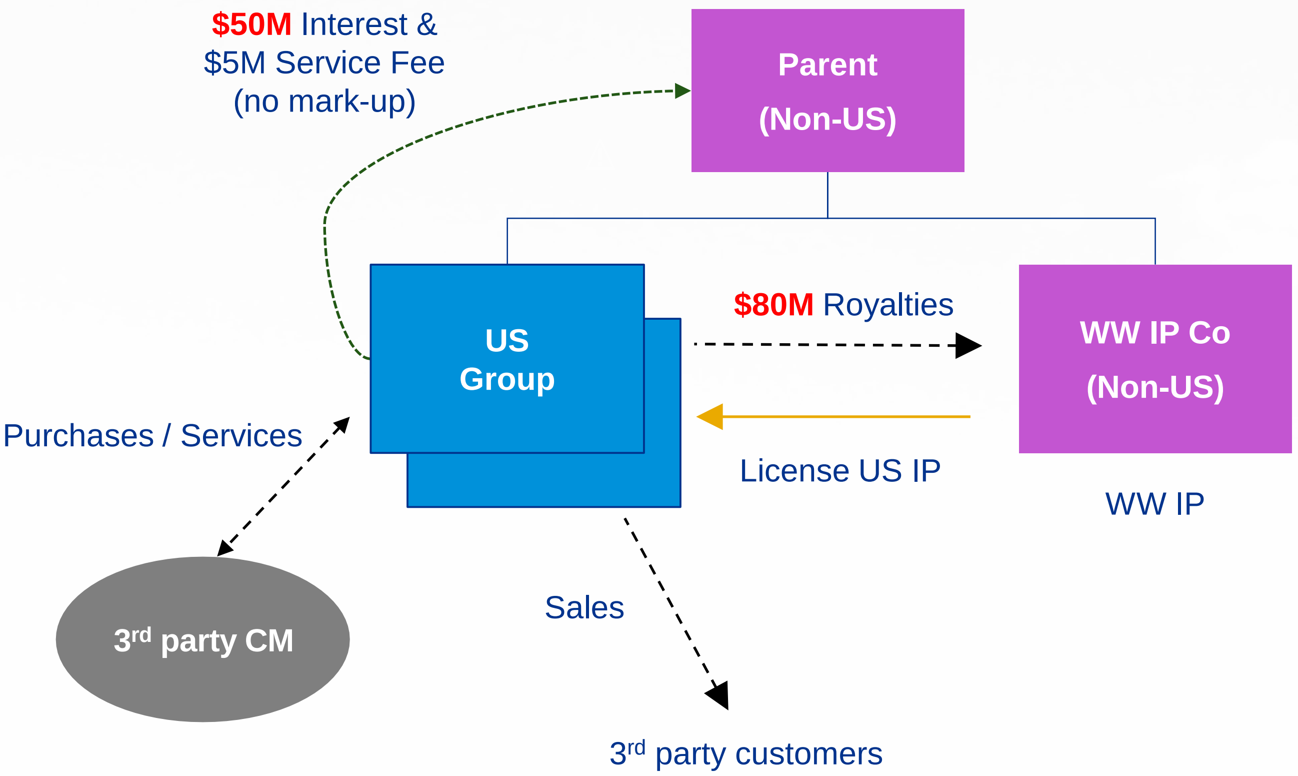
New rules H.R. 1:

— §163(j) amended to limit <u>all business net interest expense to 30% of **EBITDA**</u>
— This would limit net interest expense deductions to 30% x EBITDA of $50 = $15
— Interest deductions allowed = $15
— **Interest deductions denied = $13**

Mesures pour décourager l'érosion de la base imposable (US domestic provisions)

Provision	Summary	Effective
Base erosion anti-abuse tax (BEAT)	An anti-base erosion rule that would impose a minimum federal income tax (5% in 2018; 10% from 2019-2025; 12.5% afterward) on certain US taxpayers making certain base eroding payments to related (25% vote or value) foreign persons Applies to taxpayers with 3-yr average annual consolidated gross receipts of at least $500 million, if targeted base erosion payments exceed 3% of allowable deductions Minimum taxable income base is calculated without the effect of targeted base erosion payments, including related NOLs, but (until 2026) permitting allowance of R&E and certain other credits Targeted base erosion payments do not include – - COGS (unless paid to inverted group members) - Payments to the extent subject to US withholding tax - Payments for services that qualify for services cost method - Qualified derivatives payments	TBYA 31 Dec 17

Example - BEAT



- Parent, a non-US corporation, is the parent company of global multinational group, including WW IP Co and US Group, which sells products to the US market
- US Group's gross receipts for calendar tax year ends 2016 thru 2019 are $425M, $500M, $600M, and $500M, respectively
- Assume US Group makes the following related party payments:
  - $50 million interest paid to Parent ($5M limited under new section 163(j))
  - $80 million royalty payments to WW IP Co
  - $5 million shared services fees that qualify for use of the services cost method (and no mark-up on services) to Parent
- Assume Parent and WW IP Co are US tax treaty eligible (zero withholding tax on interest or royalties) and no US Group depreciation / amortization deductions in connection to property acquired from post-2017 related-party transactions
- US Group's 2019 Taxable Income = $100M

Example - BEAT

BEAT Computation Illustration – 2019 Tax Year

— US Group is within the scope of potential application of BEAT for its 2019 tax year because:

(i) US Group's 3-yr annual average gross receipts for 2016-2018 tax years exceeds $500M, <u>and</u>

(ii) Base erosion percentage:

<u>US Group's Base Erosion Tax Benefits</u> = <u>$45M allowable interest expense + $80M royalty payments</u> **> 3%**
Total Allowable Deductions $400M

— BEAT liability is the excess of (a) 10% of US Group's Modified Taxable Income (MTI) over (b) US Group's regular tax liability (assuming no credits)

- Here, <u>MTI</u> = (i) <u>Taxable Income</u> ($100M) *plus* (ii) aggregate <u>Base Erosion Tax Benefits</u> ($125M) = $225M
- US Group's regular tax liability = $21M ($100M x 21% corp tax rate)

— 10% x $225 million = $22.5M less $21M = **$1.5M** BEAT liability (in addition to its regular US corporate tax liability)

Example - BEAT

BEAT Computation Illustration – 2019 Tax Year

	Scenario 1		Scenario 2		Scenario 3	
	Regular	Modified	Regular	Modified	Regular	Modified
Sales	500	500	500	500	500	500
COGS - Inventory	(200)	(200)	(200)	(200)	(200)	(200)
COGS - Royalties	-	-	(50)	(50)	-	-
Gross Profit	300	300	250	250	300	300
SG&A	(70)	(70)	(70)	(70)	(70)	(70)
Interest after §163(j) limit	(45)	-	(45)	-	(45)	-
Royalties	(70)	-	(20)	-	(20)	-
Service Fees to Parent (at cost)	(5)	(5)	(5)	(5)	(5)	(5)
Service Fees to Foreign Affiliate	(10)	-	(10)	-	(10)	-
Total Deductions	(200)	(75)	(150)	(75)	(150)	(75)
Taxable Income before NOL	100	225	100	175	150	225
Tax Rate	21%	10%	21%	10%	21%	10%
Tax	21.0	22.5	21.0	17.5	31.5	22.5
Regular US Tax	21.0		21.0		31.5	
BEAT	1.5		-		-	
Total US Tax	22.5		21.0		31.5	

Mesures pour encourager l'investissement aux Etats-Unis (“sandwich” provisions)

Provision	Summary	Effective
Deduction for foreign derived intangible income (FDII)	Provides a 37.5% deduction (for a 13.125% effective tax rate) for “foreign derived intangible income,” i.e., income earned directly by a US corporation from foreign sales (including licenses and leases) or services Deemed intangible income eligible for deduction determined as excess of qualifying gross income over a deemed 10% return on average tax basis of certain tangible assets Intercompany sales will not qualify for FDII benefits unless the property is either (i) ultimately sold to an unrelated foreign person, or (ii) used in connection with property sold to, or services provided to, an unrelated foreign person, for use outside of the United States Starting in 2026, deduction drops to 21.875% (16.406% effective tax rate)	TYBA 31 Dec 17; phase-down takes effect TYBA 31 Dec 2025

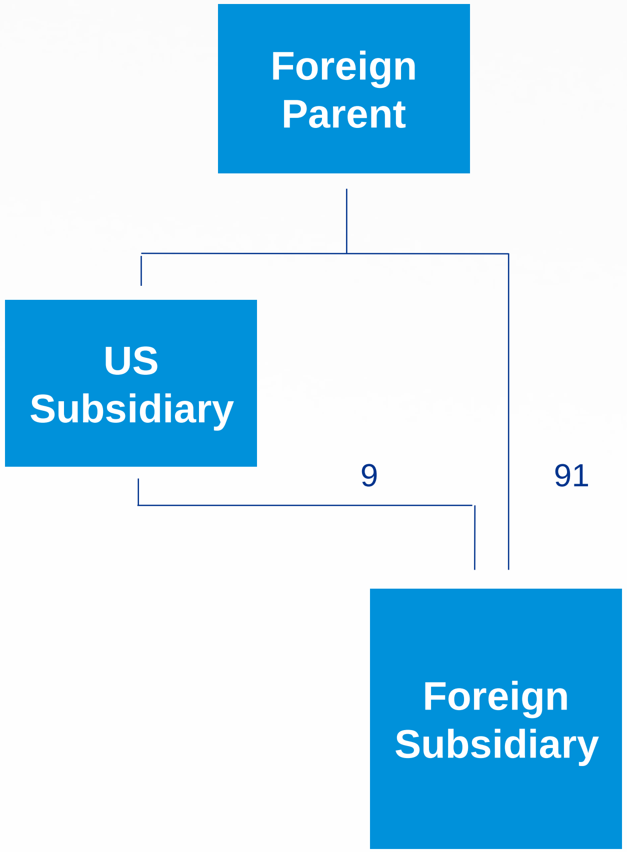
Mesures pour encourager l'investissement aux Etats-Unis ("sandwich" provisions)

Provision	Summary	Effective
Repatriation of existing earnings and profits (E&P)	Post-'86 untaxed foreign earnings subject to one-time tax; applies to ≥10% US shareholders; E&P determined as of 2 Nov or 31 Dec 17 (whichever is higher) Tax rate of 15.5% for cash/cash equivalent assets and 8% for remaining assets, payable ratably over 8 years (backloaded) Recapture rule targeting expatriated US entities anytime w/in 10 years after enactment Scaled back foreign tax credits; election to NOT utilize NOLs against Mandatory Repatriation inclusions	Last TYBB 1 Jan 2018
Participation exemption system	Creates a 100% dividends received deduction for US corporate shareholders receiving foreign source dividends (non-hybrid only) from qualifying 10% owned foreign corporations	TYBA 31 Dec 2017

Mesures pour décourager l'érosion de la base imposable (cross-border provisions)

Provision	Summary	Effective
Expansion of reach of Subpart F rules	Expands CFC stock attribution rules; creates CFCs and USSHs by attributing shares held by related foreign companies to US shareholder	Attribution rule effective for foreign corp's last TYBB 1 Jan 2018
	Also expands the US shareholder definition (10% vote *or* value test)	USSH rule effective for TYBA 31 Dec 2017
	Eliminates the 30-day CFC minimum holding period for exposure to subpart F inclusions	TYBA 31 Dec 2017

Example – CFC Creation via Constructive Ownership



Foreign Parent, the ultimate corporate parent of a multinational corporate group, owns two chains of subsidiaries, one US and one foreign. US Sub owns stock representing 9% (vote and value) of Foreign Sub. All corporations are calendar year taxpayers.

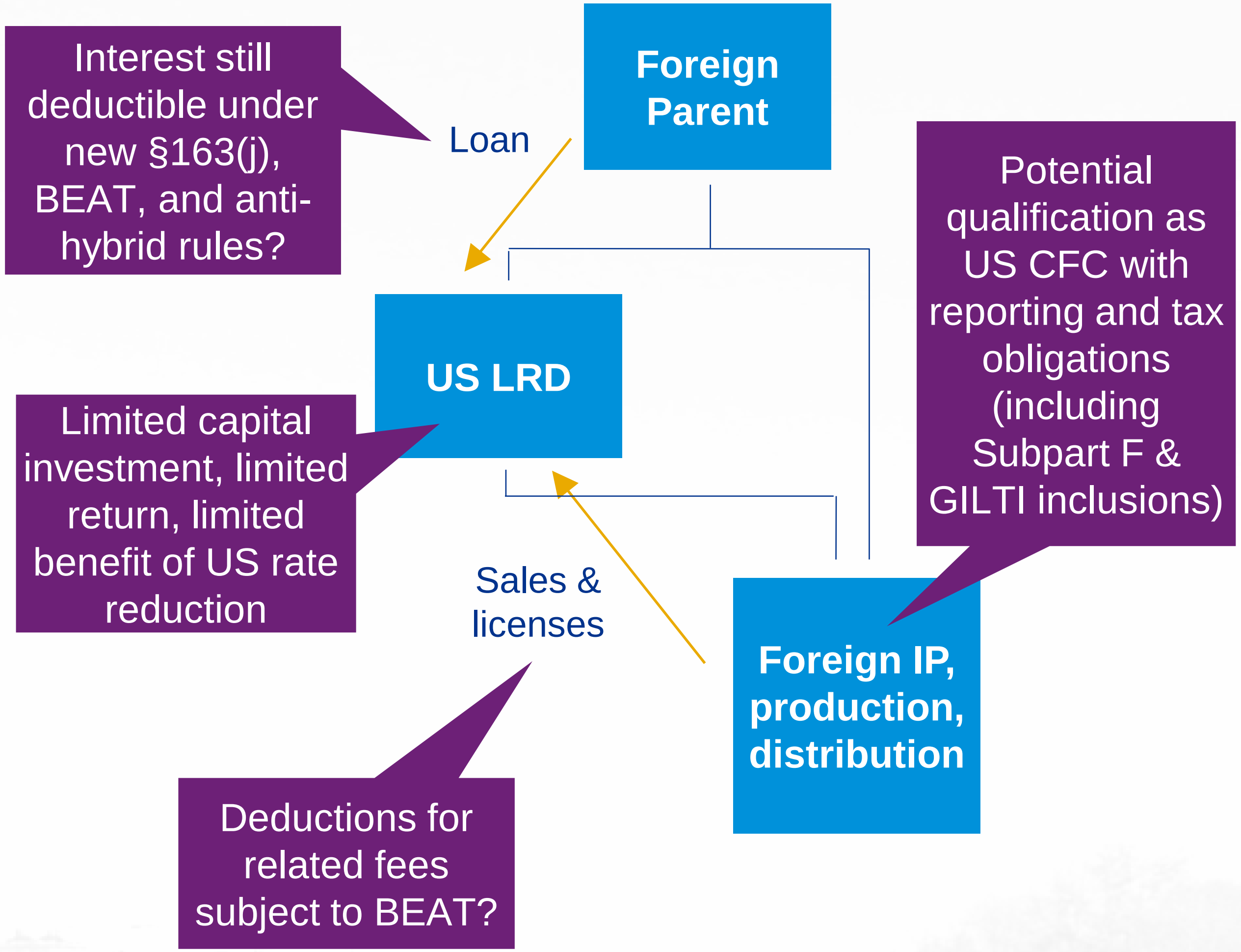
Tax Reform Considerations

- Under old rules, US Sub was not attributed any stock ownership via Foreign Parent; as a result, Foreign Sub was not a “controlled foreign corporation” and US Sub was not a “United States shareholder” for US tax purposes.
- Under new rules, Foreign Sub is a CFC and US Sub is a USSH, effective for Foreign Sub’s last TYBB 1 Jan 18 (and US Sub’s 2017 tax year). Therefore***, Foreign Sub is a CFC for purposes of mandatory repatriation.*** Note, the inclusion rule requires direct or indirect stock ownership by US Sub, resulting in a 9% pro rata share of Foreign Sub’s in-scope E&P.
- In addition, the Foreign Sub’s CFC status triggers 2017 information reporting requirements for the US Sub, i.e., Form 5471.

Mesures pour décourager l'érosion de la base imposable (cross-border provisions)

Provision	Summary	Effective
Current tax on global intangible low-taxed income (GILTI)	Creates a new current inclusion for global intangible low-taxed income (GILTI) Taxed amount is generally CFC income in excess of a 10% return on tangible depreciable property With GILTI deduction starting at 50% then phasing down to 37.5%, GILTI effective tax rate is 10.5%, then 13.125% 80% FTC offset permitted (GILTI-only basket, no carryforward) – break-even rate of 13.125% then, after phase-down, of 16.406%	TYBA 31 Dec 17; phase-down takes effect TYBA 31 Dec 25

Making America Great Again? Considerations for Inbounds



Foreign Parent, the ultimate corporate parent of a multinational corporate group, has IP, manufacturing and R&D offshore and sells to the U.S. market via a captive U.S. LRD

Tax Reform Considerations

— Lower US corporate tax rate facilitates higher profits in the United States

— Immediate expensing of capital assets and survival of the R&E credit facilitate expansion of US risks and activities (and BEAT potentially penalizes keeping IP offshore)

— With respect to US market sales, Foreign Parent's global profits are expected to be taxed at a rate closer to 21%

— Low tax attributable to US IP under IP incentives regime could facilitate US production and export model

On the Near Horizon – State Tax Considerations

Evaluate State Tax costs…

- With the drop in federal rates, state tax will represent a more significant portion of the total US tax cost
  - Not all states "piggyback" from the federal rules, and states are able to adopt changes to move away from the federal system
  - States are determining whether, from fiscal and competitive perspectives, they can afford to conform to federal-level incentives

As well as potential benefits…

- States also compete for new investment
  - Perform cost-benefit analysis of increasing US production, R&D or other activities in some US locations vs others
  - Potential additional benefit from investment and tax incentives

Q&A