Parker Fielder Oil and Gas Tax Conference

Continuation of FTC Issues

Moshe Spinowitz
Skadden, Arps, Slate, Meagher & Flom

Michael Caballero
Covington & Bruling

Glenn Leishner
Shell Oil Company

Danielle Rolfes
KPMG LLP

Karen Cate
Internal Revenue Service

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Agenda

- Overview
- Expense apportionment
- Basketing Under Section 904
- Section 960 and Timing Differences
- Transition Rules

Overview

- The GILTI regime dramatically expanded the subset of foreign source income subject to current U.S. tax by taxing most income of CFCs on a current basis.
- Under this expanded regime, the foreign tax credit and associated foreign tax credit limitation is key to reaching the intended U.S. taxation of most income of CFCs.
- With the removal of section 902 pooling, sections 901 and 960 are now the exclusive rules to get a FTC on foreign income taxes paid or deemed paid by a CFC.

Expense Allocation & Apportionment

Overview

— Interest expense continues to be apportioned between US and foreign source income based on the relative value of US and foreign assets, calculated either using the tax book value (**"TBV"**) or alternative tax book value (**"ATBV"**) method. It continues to be apportioned to FTC baskets based on the foreign asset's character.

— Expense allocation rules updated and applied to the Global Intangible Low-taxed Income (**"GILTI"**) basket.

— The Proposed Regulations would treat the §250 deduction with respect to Foreign Derived Intangible Income (**"FDII"**) and GILTI inclusions as a partial exemption, causing an asset producing such income to be treated in part as a §864(e)(3) exempt asset for purposes of interest expense apportionment.

— Separate computation for §904(b)(4), which adds back deductions attributable to §245A income / assets to the §904 FTC Limitation numerator and denominator.

— Despite this significant relief, taxpayers can end up paying US tax on high-taxed foreign income in the GILTI basket as a result of expense allocation, increasing the overall ETR on foreign income.

Valuing CFC Stock

— The starting point for interest expense apportionment is to determine the tax book value of the USSH's stock of a 10% owned corporation, including a CFC.

- Taxpayers must use the TBV or ATBV method to value assets for tax years beginning after December 31, 2017. Cannot use the fair market value (**"FMV"**) method.

— The TBV of a 10%-owned corporation's stock equals the stock's average tax basis in the taxpayer's hands using BOY and EOY basis (not including §961(a) or §1293(d) increases)

— Taxpayer increases TBV by the E&P attributable to the stock or decreases—but not below zero—by an E&P deficit attributable to such stock (the **"E&P bump"**):

- TBV + E&P bump = stock value
- E&P includes PTI
- E&P of an upper-tier CFC is adjusted for the E&P (and deficits) of lower-tier 10%-owned foreign corporations

— Taxpayer reduces TBV for deficits used under §965(b)(4) as if taxpayer had made a Prop. Reg. §1.965-(f)(2)(i) election (with no increase).

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