

Quarterly tax developments

Things to know about this quarter's tax developments and related US GAAP accounting implications

September 2021

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Welcome to our September 2021 Quarterly tax developments publication.

Here we describe certain tax developments previously summarized in Tax Alerts or other EY publications or identified by EY tax professionals or EY foreign member firms. These developments may affect your tax provision or estimated annual effective tax rate.

We compile this information because we recognize that, for many companies, the most challenging aspect of accounting for income taxes is identifying changes in tax law and other events when they occur so the accounting can be reflected in the appropriate period. However, this publication is not a comprehensive list of all changes in tax law and other events that may affect income tax accounting.

This edition covers certain enacted and effective tax legislation, as well as regulatory developments, legislative proposals and other items identified through 15 September 2021, except as noted.

We list EY publications that you can access through our [Tax News Update website](#), if you are registered. Anyone interested in registering should contact Joan Osborne at joan.osborne@ey.com.

See our [previous editions](#) for additional tax developments.

Tax developments

Legislation enacted in the third quarter

Companies are required to account for the effects of tax law changes on their deferred tax assets and liabilities in the period the legislation is enacted. Similarly, companies must reflect the effects of an enacted change in tax laws or rates in their annual effective tax rate computation in the period the changes are enacted.¹ If an interim change is significant, temporary differences may need to be estimated as of the enactment.

Federal, state and territories

California – On 21 July 2021, California enacted legislation establishing a new tax credit for production companies that film a qualified motion picture (including a television show) within a specified time in one or more sound stages constructed in California (i.e., a “certified studio construction project”). The credit equals 20% or 25% (depending on the project) of qualified expenditures paid or incurred for the qualified motion picture during the tax year. The credit is effective for tax years beginning on or after 1 January 2022 and before 1 January 2032. See [the State and Local Tax Weekly for 13 August 2021](#).

Connecticut – On 13 July 2021, Connecticut enacted legislation that effectively allows businesses to exchange their accumulated research and development credits for a 5% corporate income tax credit if they make certain human capital investments. Examples of these investments include child-care subsidies for certain employees, donations or capital contributions to in-state colleges or universities for improvements or advancements of technology, and investments in in-state job training for in-state employment. The change applies to tax years beginning 1 January 2021. See [the State and Local Tax Weekly for 13 August 2021](#).

Delaware – On 30 July 2021, Delaware enacted legislation limiting the extent to which taxpayers may deduct federal carryforwards of net operating losses (NOLs) for state tax purposes. The legislation limits these deductions to the amount of the deduction claimed on the taxpayer’s federal income tax return for the tax year in which the taxpayer was included as a party. The change is effective upon enactment. See the [State and Local Tax Weekly for 31 August 2021](#).

Minnesota – On 1 July 2021, Minnesota enacted legislation conforming to select provisions of the Internal Revenue Code (IRC) that were enacted after the state’s general conformity date of 31 December 2018. These provisions include:

- ▶ The income tax exemptions for loans forgiven under the Paycheck Protection Program (PPP) and advances through the Economic Injury Disaster Loan (EIDL) and targeted EIDL Advance programs that do not need to be repaid
- ▶ Deductions for business expenses paid with PPP loans or EIDL grants
- ▶ An extension of the deduction for commercial building property that is energy efficient
- ▶ Expensing rules for certain film, television and live theater production
- ▶ The special rule for sales or dispositions to implement electric restructuring policies of Minnesota or the Federal Energy Regulatory Commission for qualified electric utilities
- ▶ Certain disaster-related tax relief provisions

The legislation also introduces a nonrefundable credit equal to 25% of eligible film production costs paid during the tax year. The credit is available from 2021 through 2024. Companies may claim the credit against Minnesota income taxes or other taxes and may carry unused credits forward for up to five years. Other changes include a one-year extension, through 2022, of the Minnesota historic structure credit. The effective dates for these changes vary. See [Tax Alert 2021-1393](#), dated 20 July 2021.

¹ Companies that have not adopted Accounting Standards Update (ASU) 2019-12, *Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes*, should reflect the effects of enacted changes in tax law or rates in estimates of their annual effective tax rate in the first interim period in which the change is effective. For more information on ASU 2019-12, see our [Financial reporting developments publication on income taxes](#).

New Jersey – On 2 July 2021, New Jersey enacted legislation modifying the requirements that companies must meet to claim income tax credits under various economic incentive programs. The legislation also includes up to \$350 million in funding for income tax credits for qualified offshore wind projects. The changes are generally effective upon enactment. See [Tax Alert 2021-1351](#), dated 13 July 2021.

Rhode Island – On 26 July 2021, Rhode Island enacted legislation allowing companies to exclude up to \$250,000 of loans forgiven under the PPP from their gross income when computing state corporate income tax for tax years beginning on or after 1 January 2020. Rhode Island corporate income tax will apply to the portion of forgiven PPP loans exceeding \$250,000. The new law also requires the Rhode Island tax authorities to waive interest and penalties on the taxable portion of a PPP loan that is forgiven during the 2020 tax year, provided the taxpayer pays the tax by 31 March 2022. [State and Local Tax Weekly for 23 July 2021](#).

IRC conformity

The following chart lists the states that enacted legislation this quarter updating their date of conformity to the US IRC. The chart also includes the dates on which the new conformity date was enacted and became effective. Further information on a state's IRC conformity can be found in the cited reference.

State	Enactment date	Date of conformity	Effective date	Reference
Maine	1 July 2021	30 April 2021	Applies to tax years beginning on or after 1 January 2021 and to any prior tax years as specifically provided by the IRC	State and Local Tax Weekly for 23 July 2021
Oregon	14 July 2021	1 April 2021	Applies generally to transactions or activities occurring on or after 1 January 2021	State and Local Tax Weekly for 23 July 2021

International

Colombia – On 10 July 2021, Colombia enacted legislation broadening eligibility for existing tax incentives for nonconventional renewable energy projects. The incentives include an income tax deduction equal to 50% of the investment claimed over 15 years and an increase in the accelerated depreciation rate for these projects to 33.33% from 20%. Eligible projects for carbon capture and storage now qualify for accelerated depreciation and an income tax credit equal to 25% of the investment made. The benefits are available for 30 years, beginning 1 July 2021. See [Tax Alert 2021-1388](#), dated 20 July 2021.

On 14 September 2021, Colombia enacted legislation increasing its corporate income tax rate to 35% from 31% and eliminating the scheduled decrease to 30% in 2022. For financial institutions with taxable income over 120,000 tax units (approximately \$1.1 million), a 3% surtax applies from 2022 through 2025, raising the total income tax rate to 38%. Other changes include:

- ▶ Retaining the 50% limit on the amount of turnover taxes that companies may claim as corporate income tax credits by repealing a previously scheduled increase to 100% in 2022
- ▶ Increasing to 10 years from 5 years the period that companies engaged in concession and public-private agreements may carry forward certain excess profits to determine the applicable withholding tax on dividend distributions

The changes are effective upon 1 January 2022. See [Tax Alert 2021-1698](#), dated 20 September 2021.

Dominican Republic – On 6 August 2021, the Dominican Republic enacted legislation reducing the tax rate on capital gains on shares that trade on the Dominican Republic Stock Exchange to 15% from 27% and exempting capital increases from public offerings of stock from the capital gains tax. Both changes are effective for three years, beginning 9 August 2021. Other changes that are generally effective on that date include exempting capital gains on a stock sale from withholding tax if the shares were part of a public offering. See [Tax Alert 2021-1575](#), dated 26 August 2021.



France* – On 20 July 2021, France enacted legislation allowing companies to carry NOLs generated during a tax year ending from 30 June 2020 through 30 June 2021 back three years and use them to offset 100% (rather than €1 million or less) of taxable income, provided certain conditions are satisfied. Companies may then use a 25% corporate tax rate to determine the corresponding income tax credit (based on the losses actually carried back) to be used to offset income tax liabilities over the following five years.

Gibraltar* – On 26 July 2021, Gibraltar enacted legislation increasing the corporate income tax rate to 12.5% from 10%. The change is effective 1 August 2021.

On 30 July 2021, Gibraltar enacted legislation to increase amortization allowances and introduce other business incentives. These changes are effective for tax years ending from 1 July 2021 through 30 June 2023.

Maldives – On 20 July 2021, Maldives enacted legislation that:

- ▶ Broadens the definition of permanent establishment (PE) to include the exploration, extraction and use of natural resources if those activities last more than 90 days
- ▶ Broadens the PE definition to include the installation or use of substantial equipment under a contract or agreement for more than 90 days
- ▶ Denies deductions for royalties paid by the PE for the use of patents or other rights
- ▶ Denies deductions for commissions paid for specific services
- ▶ Reduces the threshold for the creation of a construction-based PE to 90 days from six months

The changes are effective upon enactment. See [Tax Alert 2021-1496](#), dated 13 August 2021.

Nigeria – On 16 August 2021, Nigeria enacted legislation introducing a new hydrocarbon tax to be paid by oil companies on certain income from crude oil, field condensates and some liquid natural gas. A 30% rate applies to companies with petroleum mining leases across onshore and shallow water terrain, while a 15% rate applies to companies with petroleum prospecting licenses in the same terrain. When calculating the hydrocarbon tax, companies may not deduct the following costs:

- ▶ Expenses and fees incurred as a penalty for flare of natural gas
- ▶ Head office costs incurred outside Nigeria
- ▶ Tax inputted in a contract or an agreement on a net tax basis and paid by a company on behalf of the vendor or contractor
- ▶ Tertiary education taxes, company income taxes or similar income taxes

The legislation also extends the company income tax to income of oil producing companies. A 20% or 30% rate may apply, depending on the size of the company's turnover. When calculating their income tax, companies may not deduct the hydrocarbon tax. Other changes include:

- ▶ Limiting certain cost deductions and capital allowance relief to 65% of the gross revenue
- ▶ Allowing tax authorities to disregard transactions between related parties or adjust the parties' tax liability if the transactions are not at arm's length
- ▶ Permitting certain companies to consolidate costs for purposes of the company income tax

The changes are effective on 27 August 2021. See [Tax Alert 2021-1603](#), dated 2 September 2021.

Peru – On 14 August 2021, Peru enacted legislation creating a tax-free zone in the district of San Ignacio, Cajamarca (northern Peru). Corporate income taxes, among others, will not apply to the following activities conducted in the district:

- ▶ Manufacturing
- ▶ Commercialization

* A Tax Alert has not been published on this development.

- ▶ Industrial activities
- ▶ Agribusiness
- ▶ Maquila factories
- ▶ Services

The changes are effective 15 August 2021. See [Tax Alert 2021-1537](#), dated 19 August 2021.

Spain – On 10 July 2021, Spain enacted legislation aligning its rules for controlled foreign corporations (CFCs) with the CFC rules in the Anti-Tax Avoidance Directive (ATAD) of the European Union (EU). Specific changes include:

- ▶ Broadening the rules' scope so they apply to income from a foreign PE and not only to subsidiaries
- ▶ Allowing companies and PEs that reside in the European Economic Area to qualify for the same safe harbor to prove valid business purpose as subsidiaries that are EU tax residents
- ▶ Abolishing the safe harbor for certain holding companies
- ▶ Broadening the scope of income that qualifies as CFC income

Other changes include:

- ▶ Replacing the Spain tax haven list with a list of “noncooperative jurisdictions” and using broader criteria to determine whether a jurisdiction is noncooperative
- ▶ Tightening the requirements that open-ended investment companies (SICAVs) must meet to qualify for the reduced 1% corporate income tax rate (beginning 1 January 2022) and providing transition rules for SICAVs that are affected by the new legislation and are dissolved in 2022
- ▶ Taxing certain undistributed profits of Spanish real estate investment trusts annually

The changes are generally effective for tax years beginning 1 January 2021, except for certain provisions that will apply to tax years beginning on or after 1 January 2022. See [Tax Alert 2021-1373](#), dated 16 July 2021.

Legislation effective in the third quarter

Federal, state and territories

Indiana – Effective 1 July 2021, the corporate income tax rate decreases to 4.90% from 5.25%. The change was enacted 25 March 2014. See the [State and Local Tax Weekly](#) for 24 March 2014.

Mississippi – Effective 1 July 2021, companies may claim 100% bonus depreciation for new or used aircraft, equipment, engines, or other parts and tools used for aviation. The change was enacted on 6 April 2021. See the [State and Local Tax Weekly for 9 April 2021](#).

International

Australia – Effective 1 July 2021, new rules apply under Australia’s tax incentive regime for research and development (R&D) that may increase the benefits available for eligible companies. The change was enacted on 14 October 2020. See [Tax Alert 2020-2716](#), dated 14 October 2020.

Canada – Effective 1 July 2021, employers may deduct the value of stock options granted to their employees to the extent that the options are nonqualified securities. Options are nonqualified securities if the employer designates them as such, or if they do not qualify for preferential tax treatment under Canadian law. For large public companies, preferential tax treatment is now limited to options valued at \$200,000 or less. The changes were enacted 29 June 2021. See [Tax Alert 2021-1356](#), dated 14 July 2021.

Denmark* – For tax years beginning on or after 1 July 2021, new rules govern the taxation of CFCs. The changes, which implement the ATAD of the EU, were enacted on 9 June 2021.

* A Tax Alert has not been published on this development.

Japan – Effective 2 August 2021, income tax credits or additional depreciation are available for eligible companies that invest in technology that will lower carbon emissions or help digitize the economy. The amount of the credits and depreciation depends on how much is invested under certified business plans and whether the company meets other requirements. Other changes include allowing eligible companies to use more of their COVID-19-related losses (previously limited to 50% of taxable income) to offset future taxable income for five years. The limit on how much taxable income may be offset depends on how much a company invests and whether its business plan satisfies certain requirements. The changes were enacted 26 March 2021. See [Tax Alert 2021-1571](#), dated 27 August 2021.

Mexico – Effective 1 September 2021, companies may not deduct payments for subcontracted services that relate to a corporation’s purpose or primary economic activity. Companies may, however, deduct payments for subcontracted services that do not relate to their purpose or primary economic activity (i.e., specialized services), provided certain requirements are met. The changes were enacted on 23 April 2021. See Tax Alerts [2021-0857](#), dated 26 April 2021, and [2021-1456](#), dated 2 August 2021.

Taiwan – Effective 1 July 2021, a progressive tax rate structure applies to capital gains from certain property transfers, rather than a flat 20% rate. The new rates vary depending on how long the property is held, with some rates exceeding 20%. Gains from corporate transfers of pre-sold condominiums/ homes are now subject to the new rates, as well as gains from indirect transfers of shares that are “real property rich” (i.e., more than 50% of the shares’ value or the company’s share capital comes from Taiwanese real property). The changes, among others, apply to transfers of real property acquired on or after 1 January 2016, and were enacted on 28 April 2021. See [Tax Alert 2021-1344](#), dated 14 July 2021.

Treaty changes

Tax treaties are agreements between countries that typically address withholding tax rates or exemptions on dividends, interest and royalties paid in multiple jurisdictions. Exceptions may apply based on the tax treaty (for instance, reduced rates may apply to certain categories of investors, capital gains from immovable property or property-rich companies may be taxable). All of the following tax treaty changes were effective in the third calendar quarter, except where indicated.

Countries involved		Summary of changes
Bangladesh	Czech Republic	Provides general withholding tax rates of 15% on dividends and 10% on interest and royalties; generally exempts capital gains from tax (effective 1 January 2022 in Czech Republic).
Botswana	Luxembourg	Provides general withholding tax rates of 10% on dividends and 7.5% on interest and royalties; generally exempts capital gains from tax (effective 1 January 2022 in Luxembourg).
Lesotho	Mauritius	Provides general withholding tax rates of 10% on dividends, interest and royalties; generally exempts capital gains from tax (effective 1 April 2022 in Lesotho).

Other considerations

Court decisions, regulations issued by tax authorities and other events may constitute new information that could trigger a change in judgment in recognition, derecognition or measurement of a tax position. These events also may affect your current or deferred tax accounting.

Federal, state and territories

Federal – The US and United Kingdom (UK) competent authorities agreed to interpret the term “North American Free Trade Agreement (NAFTA),” which appears in the US-UK income tax treaty, as referencing the 2018 trade agreement that replaced NAFTA. The US and UK competent authorities also agreed that a “resident of a Member State of the European Community,” which also appears in the treaty, still includes UK residents. See [Tax Alert 2021-1448](#), dated 30 July 2021.

In a revenue ruling, the Government ruled that an investor could claim an IRC Section 45Q credit for carbon dioxide sequestration based on components it purchased and added to a methanol plant’s carbon capture equipment. Noting that no one else had claimed the credit, the Government reasoned that the investor only had to own part of the equipment, not all of it, to claim the credit under the final IRC Section 45Q regulations. See [Tax Alert 2021-1402](#), dated 22 July 2021.

In a revenue procedure, the Government outlined procedures for taxpayers to use to implement the income recognition regulations under IRC Section 451, including a detailed explanation of what aspects of the regulations will and will not be treated as automatic changes going forward. The revenue procedure is generally effective for Forms 3115 filed on or after 12 August 2021. See [Tax Alert 2021-1572](#), dated 26 August 2021.

In a separate revenue procedure, the Government introduced a safe harbor that will allow employers to exclude forgiven PPP loans and certain grants from their gross receipts when determining their eligibility to claim employee retention credits. See [Tax Alert 2021-1529](#), dated 18 August 2021.

In corrections to the final opportunity zone regulations under IRC Section 1400Z-2, the Government outlines how to evaluate whether a qualified opportunity zone business (QOZB) meets the requirement for at least 70% of its property to be qualified opportunity zone property while the QOZB falls within the regulation’s safe harbor for working capital. See [Tax Alert 2021-1519](#), dated 16 August 2021.

In a generic legal advice memorandum, the Government asserted that it could adjust cost-sharing transactions to reflect stock-based compensation, even if the taxpayer’s cost-sharing agreement previously excluded those costs from the transaction but provided for their inclusion at a later time. The Government reasoned that it could make the adjustment because excluding that compensation would skew the relationship between the agreement’s allocated costs and benefits. See [Tax Alert 2021-1389](#), dated 20 July 2021. See [Tax Alert 2021-1389](#), dated 20 July 2021.

Colorado – In revised guidance, the Government discussed how recent federal law changes made by the Coronavirus Aid, Relief, and Economic Security Act (CARES Act) (P.L. 116-136) and the Consolidated Appropriations Act, 2021 interact with Colorado law. Changes addressed in the guidance include NOL treatment, the limitation on business interest expense under IRC Section 163(j), qualified improvement property, PPP loans, and emergency grants of economic injury disaster loans. See [the State and Local Tax Weekly for 13 August 2021](#).

Florida – In revised guidance on Florida’s conformity with recent federal law changes, the Government noted that Florida will not conform to changes made by the CARES Act to NOLs, bonus depreciation, the limitation on business interest expense, certain qualified improvement property, and deductions for business meal expenses, among others. Florida will conform to the federal tax treatment of PPP loans, economic injury disaster loans and Small Business Administration loans. See [the State and Local Tax Weekly for 13 August 2021](#).

Separately, the Government announced that the state’s corporate income/franchise tax rate decreased to 3.535% from 4.458% for tax years beginning on or after 1 January 2021, but before 1 January 2022. The tax rate will return to 5.5% for tax years beginning on or after 1 January 2022. See the [State and Local Tax Weekly for 27 September 2021](#).

Hawaii – In new guidance, the Government explained how taxpayers may determine whether they can reasonably expect their PPP loans to be forgiven. Taxpayers that reasonably expect their PPP loans to be forgiven may **not** deduct expenses paid with those loans for Hawaii income tax purposes. See the [State and Local Tax Weekly for 16 July 2021](#).

State – The following states have ended the temporary nexus relief they provided to out-of-state businesses whose employees were working remotely in the state due to COVID-19. Consequently, these states could consider out-of-state businesses with remote workers in the state as having nexus for corporate income tax purposes:

- ▶ California
- ▶ Maine
- ▶ New Jersey
- ▶ Pennsylvania

See the [State and Local Tax Weekly for 16 July 2021](#), the [State and Local Tax Weekly for 23 July 2021](#), [Tax Alert 2021-1495](#), dated 10 August 2021, and [Tax Alert 2021-1505](#), dated 12 August 2021.

South Carolina – The Government said it will continue, through 31 December 2021, to disregard the locations of employees who are temporarily working in South Carolina due to COVID-19 for purposes of determining a business's nexus with the state or altering its income apportionment. See the [State and Local Tax Weekly for 31 August 2021](#).

International

Chile – In a ruling, the Government identified the factors to consider when determining whether an insurance PE in the UK existed in Chile under the Chile-UK income tax treaty. The ruling stemmed from payments made by a UK insurance company to a Chilean resident. See [Tax Alert 2021-1633](#), dated 9 September 2021.

Colombia – The Council of State (the highest tax court) annulled an opinion by the Colombian Tax Authority that denied income tax deductions for interest on loans used to acquire shares in a company, regardless of the circumstances. The Council reasoned that the taxpayer might satisfy Colombia's general requirements for expense deductions depending on its facts and circumstances, particularly the reasons for the share acquisition and how that acquisition related to the taxpayer's business. See [Tax Alert 2021-1512](#), dated 13 August 2021.

Hong Kong – In new guidance, the Government indicated employees working from home in Hong Kong temporarily due to COVID-19 will not create a PE for their foreign employer. Similarly, employees or agents who temporarily conclude contracts from their home offices will not create a PE for their foreign employers unless they were concluding contracts before the COVID-19 pandemic. These conclusions could change, however, when public health measures adopted during the pandemic are removed. See [Tax Alert 2021-1496](#), dated 13 August 2021.

India – The Income Tax Appellate Tribunal of Delhi held that a Norwegian service provider had established a service PE in India based on the services that its employees performed in India for a domestic company. The Tribunal reasoned that the activities performed by the service provider were too interconnected to be considered separate projects, as the provider asserted. The common billing and receipt of income also indicated the activities related to the same project, which led to the conclusion that the business service agreement was a single contract. Accordingly, the Tribunal combined the days spent in India by the provider's employees into one total that met the threshold for service PEs. See [Tax Alert 2021-1633](#), dated 9 September 2021.

Mexico – The Government published another list of expected effective tax rates for large taxpayers engaged in various economic activities or industries during tax years 2016 through 2019. If a corporation's effective tax rate is lower than the listed rate, among other things, the Government could assert that the transfer pricing is incorrect. See [Tax Alert 2021-1463](#), dated 3 August 2021.



Russia – In letter guidance, the Ministry of Finance clarified that Russian withholding tax did not apply to interest paid by a Russian PE of a foreign company to a foreign lender with no Russian presence. The Ministry of Finance noted, however, that the withholding tax would generally apply in this situation beginning 1 January 2022. See [Tax Alert 2021-1633](#), dated 9 September 2021.

Switzerland – The Swiss competent authorities announced that a 5%, rather than 10%, withholding rate applies to dividends under the India-Switzerland income tax treaty, as of the date that Lithuania joined the Organisation for Economic Co-operation and Development (OECD), i.e., 5 July 2018. The authorities concluded that the treaty's most-favored-nation clause dictated application of the 5% rate, which appeared in treaties that India negotiated with Lithuania after the India-Switzerland treaty. Because Lithuania was not an OECD member when it executed its treaty with India, the 5% did not become effective under India-Switzerland treaty until the date it became a member. See [Tax Alert 2021-1570](#), dated 26 August 2021.

Taiwan – The Government amended its regulations on bilateral tax treaties to tighten the rules for determining when a PE exists. Other changes include explaining how to determine whether a taxpayer has met the time threshold for a construction PE and refining the definition of preparatory or auxiliary activities. See [Tax Alert 2021-1633](#), dated 9 September 2021.

Uruguay – In a decree, the Government introduced an income tax exemption for eligible corporations that invest in aeronautical infrastructure projects. The exempted amount will depend on how the government rates the project but could be as high as 90%. See [Tax Alert 2021-1543](#), dated 23 August 2021.

Things we have our eyes on

National, state and local governments continue to seek to increase their revenues. Companies should continue to monitor developments in this area. Some of these potential tax law changes are summarized here.

Federal, state and territories

Tax reform – The House Ways and Means Committee approved the tax portion of a budget reconciliation bill that would significantly revise US income tax rules. Proposals in the bill would:

- ▶ Increase the corporate rate to 26.5% from 21%
- ▶ Lower the IRC Section 250 deduction percentage for global intangible low-taxed income (GILTI) to 37.5% from 50% and the IRC Section 250 deduction percentage for foreign-derived intangible income (FDII) to 21.875% from 37.5%
- ▶ Allow the IRC Section 250 deduction to increase NOLs
- ▶ Require US shareholders to compute their GILTI inclusion on a country-by-country basis
- ▶ Make other notable changes to the GILTI computation, such as adding foreign oil and gas extraction income into GILTI tested income and allowing tested losses to be carried forward
- ▶ Determine a US shareholder's foreign tax credit (FTC) limitation for all baskets on a country-by-country basis so companies could not credit excess FTCs from high-tax jurisdictions against income from low-tax jurisdictions
- ▶ Eliminate the separate foreign branch basket for FTC limitation purposes
- ▶ Allow foreign tax credits in all baskets to be carried forward five years but not carried back
- ▶ Tax certain foreign base company sales and services income as GILTI tested income unless the transaction involves a US resident, directly or through a branch or pass-through entity
- ▶ Limit the interest expense of a multinational group's US operations to its proportionate share of the group's overall interest expense
- ▶ Limit the carry forward period for disallowed interest expense to five years
- ▶ Significantly modify the base erosion and anti-abuse tax (BEAT) while retaining its general framework
- ▶ Treat certain payments as a dividend equivalents subject to withholding tax
- ▶ Expand the scope of the wash sale rules under IRC Section 1091
- ▶ Broaden the scope of the constructive sales rules under IRC Section 1259 to apply to digital assets
- ▶ Delaying the effective date of mandatory capitalization of research and experimental expenditures to tax years beginning after 31 December 2025

See Tax Alerts [2021-9019](#), 13 September 2021; [2021-1678](#), dated 15 September 2021; [2021-1697](#), dated 17 September 2021; [2021-9023](#), dated 17 September 2021.

International taxation – In a discussion draft of legislative text, Senate Finance Committee Chairman Ron Wyden (D-Oregon) and Senators Sherrod Brown (D-Ohio) and Mark Warner (D-Virginia) proposed changes to the current rules for GILTI, FDII and BEAT. The proposed changes would:

- ▶ Repeal the GILTI and FDII exemptions for qualified business asset investment
- ▶ Increase the GILTI rate by an unspecified amount
- ▶ Establish a mandatory country-by-country high-tax exclusion system for GILTI, subpart F and foreign branch income
- ▶ Replace FDII's "deemed intangible income" with a new metric, "domestic innovation income," which would be expenses for R&D and worker training

- ▶ Equalize the yet-to-be-determined FDII and GILTI rates
- ▶ Give domestic business credits under IRC Section 38 their full value for BEAT purposes
- ▶ Establish a second-rate bracket for “base erosion income,” which would be the amount of income added to taxable income under IRC Section 59A(c)(1) to determine the modified taxable income

See Tax Alerts [2021-1563](#), dated 25 August 2021, and [2021-1580](#), dated 29 August 2021.

Partnerships – In another discussion draft of legislative text, Sen. Wyden proposed revising sections of the tax code governing partnerships. If enacted, the proposals, among other changes, would:

- ▶ Mandate basis adjustments under IRC Sections 734 and 743 for partnership distributions and partnership interest sales
- ▶ Amend IRC Section 163(j)(4) so that partners may not use the partnership’s excess business interest income and excess taxable income to deduct interest expense from other sources
- ▶ Require all partnerships to use the remedial method for IRC Section 704(c) allocations
- ▶ Require partnerships to apply the partners’-interest-in-the-partnership standard when determining partnership allocations, unless the proposed “consistent percentage method” applies
- ▶ Generally require partnership liabilities to be allocated based on the partners’ share of partnership profits

See [Tax Alert 2021-9016](#), dated 10 September 2021.

Derivatives – Sen. Wyden introduced a bill that would change the US tax treatment of financial derivative transactions. The bill would replace many of the current statutes and regulations governing the taxation of specific derivatives with a new regime that uses one timing rule, one characterization rule and one sourcing rule for all transactions. It also defines derivatives to include many contracts not traditionally considered to be financial derivative transactions.

Proposals included in the bill would:

- ▶ Require annual mark-to-market accounting for all transactions
- ▶ Treat all gains or losses from derivatives and certain related assets as ordinary
- ▶ Determine the source of tax items based on the taxpayer's country of residence, incorporation or organization
- ▶ Introduce the Investment Hedging Units concept

See [Tax Alert 2021-1504](#), dated 12 August 2021.

Louisiana – In a statewide election on 9 October 2021, Louisiana voters will decide whether to amend the state’s Constitution to eliminate the state deduction for federal income tax paid by corporations and reduce corporate income tax rates. The amendments, which have already been approved by the State Legislature, would also reduce the number of corporate income tax brackets from four to three. Rates would range from 3.5% on the first \$50,000 of net income up to 7.5% on net income over \$150,000 (rather than 4% on the first \$25,000 of net income to 8% on net income over \$200,000). The changes would apply to tax periods beginning on or after 1 January 2022. See the [State and Local Tax Weekly for 16 July 2021](#).

Multistate Tax Commission – In a fourth revision of its “Statement of Information concerning practices of the MTC and supporting states under P.L. 86-272,” the Multistate Tax Commission (MTC) outlined the internet-related activities in which out-of-state businesses may engage without establishing nexus for corporate income tax purposes. It also identified internet-related activities that would fall outside the protections of federal law and subject an out-of-state seller to corporate income tax. To become effective, the revised statement would need to be adopted by member states through statutory, regulatory or administrative action. See [Tax Alert 2021-1608](#), dated 2 September 2021.

International

Brazil – The House of Deputies approved a bill that would reduce the corporate income tax rate to a combined rate of 27% from 34%. The combined rate could drop to 26% if certain budgetary targets are met. The bill would also introduce a 15% withholding tax on dividends as part of a comprehensive reform of the Brazilian tax system. Other proposals include:

- ▶ Eliminating interest on net equity (i.e., similar to a dividend payment that is deductible in Brazil)
- ▶ Requiring taxpayers to carry out capital reductions at fair market value (instead of at book value as currently allowed)
- ▶ Strengthening the rules on disguised distributions of profits by requiring, among other things, domestic transactions between related parties to be at arm's length
- ▶ Changing the taxation on certain types of investment funds

The bill will be sent to the Senate; if the Senate approves it, it will be sent to the President, who can then sanction or veto it, in total or in part. See [Tax Alert 2021-1600](#), dated 2 September 2021.

Cyprus – As part of its National Recovery and Resilience Plan, the Government proposed applying withholding tax to interest, dividends and royalties paid to entities in low-tax jurisdictions and certain jurisdictions on the EU's list of noncooperative jurisdictions on tax matters. It also proposed incentives to promote investment in research and innovation. See [Tax Alert 2021-1469](#), dated 5 August 2021.

Israel – The Government proposed relaxing some of the requirements that eligible corporations must meet to deduct the cost of acquiring startup companies. Additionally, the Government proposed allowing eligible Israeli companies to deduct the cost of acquiring non-Israeli companies, provided they acquire the target company's intellectual property and satisfy other conditions. Other proposals include:

- ▶ Exempting interest income from loans made by foreign financial institutions to certain Israeli startup companies from Israeli withholding tax, provided certain conditions are met
- ▶ Reducing the corporate income tax rate on undistributed retained earnings (e.g., "trapped" earnings that were previously tax-exempt) by up to 40%, to a minimum rate of 6%, for companies that distribute those all or part of those earnings during 2022

See [Tax Alert 2021-1460](#), dated 3 August 2021.

Korea – The Government proposed modifying the ordering rules used to calculate the limit on deductions for interest expense. The Government also proposed modifying its beneficial owner rules to clarify when an overseas investment vehicle (e.g., a foreign investment fund) is deemed to be the beneficial owner of Korean-sourced income. Other proposals include amending the transfer pricing rules to allow for consideration of special circumstances (e.g., COVID-19 pandemic, natural disaster) when evaluating a taxpayer's transfer pricing method. See [Tax Alert 2021-1497](#), dated 11 August 2021.

Mexico – The Government proposed eliminating certain benefits for non-regulated Special Purpose Financial Institutions (SOFOMs) and modifying the thin capitalization rules to require taxpayers to include net operating losses pending to be offset, in addition to paid-in capital and previously taxed earnings, when using the tax-equity option to calculate their limitation on interest deductions. Other proposals include:

- ▶ Requiring restructurings, spin-offs and mergers to have a valid business purpose and meet other requirements to qualify as tax-free or to be able to defer the capital gains tax, respectively
- ▶ Expanding the definition of back-to-back loans to include financing arrangements that lack business purpose (i.e., lack economic substance)
- ▶ Modifying the requirements nonresidents must satisfy when appointing a legal representative in Mexico to elect to be taxed on a net basis when transferring shares

See Tax Alerts [2021-1643](#), dated 10 September 2021, and [2021-1688](#), dated 17 September 2021.

OECD – In a 1 July 2021 statement, the Inclusive Framework of the Base Erosion and Profit Shifting project outlined areas of agreement among 130 member jurisdictions on revised rules for nexus and profit allocation, as well as new rules for a global minimum tax. The framework also outlined the remaining issues to be addressed. A detailed implementation plan is expected by October 2021.

Nine members – Barbados, Estonia, Hungary, Ireland, Kenya, Nigeria, Peru, Saint Vincent and the Grenadines, and Sri Lanka – did not join the statement. In a 10 July 2021 communiqué, the G20 Finance Ministers and Central Bank Governors endorsed the agreement outlined by the framework and invited the outstanding members to join it. As of 12 August, three jurisdictions have changed their position and decided to join the statement, bringing the **total number** to 133.

In a 1 July 2021 press release, Ireland outlined its broad support for the agreement but expressed reservations, particularly in relation to the proposed global minimum effective tax rate of “at least 15%.” Ireland later announced a public consultation period through 10 September 2021 on the BEPS 2.0 measures being proposed to make sure that Ireland’s tax policy can continue to support economic growth and prosperity.

See Tax Alerts [2021-1308](#), dated 2 July 2021; [2021-1319](#), dated 5 July 2021; [2021-1324](#), dated 12 July 2021; and [2021-1397](#), dated 21 July 2021.

Poland – The Government proposed legislation that would significantly reform Poland’s corporate income tax, among other things. Proposed changes include:

- ▶ Simplifying the requirements that Polish companies must satisfy to consolidate for income tax purposes under a so-called Tax Capital Group regime
- ▶ Changing the calculation of the limit on deductions for financing costs (e.g., interest expense), which could reduce deductions and increase the tax base
- ▶ Limiting deductions for certain costs, including intra-group debt financing share acquisitions or costs of certain services provided by shareholders and board members
- ▶ Taxing so-called shifted profits (also known as taxing undertaxed payments), which would apply a 19% corporate income tax rate in Poland on certain qualified payments made directly or indirectly to related entities, if effective taxation is lower by at least 25% of the 19% rate (i.e., lower than hypothetical 14.25% corporate income tax); additional tests and exceptions could apply
- ▶ Limiting tax depreciation of real property to book depreciation
- ▶ Introducing new tax exemptions for Polish holding companies, including an income tax exemption for 95% of dividends received from qualified subsidiaries and a capital gains tax exemption for sales of stock in qualified subsidiaries, provided certain requirements are met
- ▶ Redefining “place of effective management” to prevent Polish companies from claiming to be headquartered in a foreign jurisdiction where they do not engage in actual business operations (strict criteria might result in having a place of effective management in Poland merely due to, for example, Polish residents holding positions at an entity’s managing or supervisory bodies)
- ▶ Changing the rules for CFCs

See Tax Alerts [2021-1432](#), dated 29 July 2021; [2021-1462](#), dated 4 August 2021; and [2021-1692](#), dated 20 September 2021.

United Kingdom – The Government proposed a new tax regime for UK asset holding companies. Under the proposed regime, a qualifying asset holding company (QAHC) may receive the following tax benefits for income from “qualifying activities:”

- ▶ Exemption from tax on gains from the disposal of certain shares and overseas property
- ▶ Exemption from tax on profits from its overseas property business, provided the profits are subject to tax in another jurisdiction
- ▶ Deductions for certain interest payments that would usually be disallowed as distributions

- ▶ Suspension, in some situations, of the late-paid interest rules so it may deduct interest when accrued, rather than paid
- ▶ Treatment of premiums paid on repurchases of shares as capital, rather than as an income distribution

Other proposals include treating certain transparent entities as partnerships for purposes of the UK hybrid mismatch rules. See [Tax Alert 2021-1404](#), dated 23 July 2021.

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