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Biden Administration Details Plans for US Tax Reform 2.0

Today, May 28, 2021*, the US Department of the Treasury published the Biden Administration's Green Book, an ambitious 114-page proposal that would fundamentally reshape US tax law for the second time in four years. Formally titled "General Explanations of the Administration's Fiscal Year 2022 Revenue Proposals," the Green Book sets forth President Biden's plans to raise revenues by increasing the corporate income tax rate and rewriting several international tax provisions. A summary of the key elements of the corporate tax reform proposal follows.

Corporate Tax Rate

Raise the Corporate Income Tax Rate to 28% (up from 21%), effective January 1, 2022, pro-rated for non-calendar fiscal years.

GILTI

Revise the Global Intangible Low-Taxed Income (GILTI) regime, effective for fiscal years beginning after December 31, 2021, to:

- Increase effective rate on GILTI to 21% (up from 10.5%);
- Eliminate carve-out of 10% return on Qualified Business Asset Investments (QBAI);
- Calculate GILTI inclusion on a country-by-country basis (currently high and low tax income can be blended across jurisdictions); and
- Eliminate GILTI exemption on foreign oil and gas extraction income.
- Repeal the deduction for Foreign-Derived Intangible Income (FDII) related to US exports, effective for taxable years beginning after December 31, 2021.

BEAT / SHIELD

Replace the Base Erosion Anti-Abuse Tax (BEAT) with the Stopping Harmful Inversions and Ending Low-Tax Developments (SHIELD) rule, applicable to companies with global annual revenues exceeding USD 500 million. The SHIELD regime would disallow deductions for certain payments made by domestic corporations or branches to foreign related parties.

- Unlike BEAT, which is applicable to qualifying outbound payments to all foreign related parties, SHIELD would apply only to payments made to related parties in "low-tax" jurisdictions.
- Low-tax jurisdictions are defined as those that have corporate tax rates below the OECD Pillar Two Global Anti-Base Erosion (GloBE) tax rate, which is currently under consideration by an Inclusive Framework of 139 countries.
- In April 2021, the Biden administration called for a 21% global minimum tax

rate, but has since signaled that it would accept a GloBe rate as low as 15%.

- If SHIELD is in effect before a Pillar Two GloBE tax has been agreed, the "low-tax" threshold will be equal to 21%, in line with the revised US GILTI rate.
- Notably, SHIELD would not be effective until fiscal years beginning after December 31, 2022, providing time for an OECD global minimum tax agreement.

Corporate Inversions

Enact new provisions to broaden the definition of corporate inversions. The following changes would be effective for any transactions that occur after the date of enactment.

- Expand the circumstances under which an inverted foreign corporation is treated as a domestic corporation under Internal Revenue Code (IRC) Section 7874 by (i) replacing the "80% (vote or value) test" with a greater than "50% test," and (ii) eliminating the "60% test" under which an inverted company still be respected as a foreign entity (albeit with certain tax consequences).
- Consider an inversion to have taken place if:
  a) prior to the acquisition, the fair market value (FMV) of the US entity is greater than the FMV of the foreign entity;
  b) the group is primarily managed and controlled in the United States following the transaction; or
  c) post-transaction, the group does not conduct substantial business activities in the country where it is organized.
- Expand the definition of an acquisition under IRC Section 7874 to include a direct or indirect acquisition of substantially all of the assets constituting a trade or business of a domestic corporation or partnership, or substantially all of the US trade or business assets of a foreign partnership.
- Consider a distribution of stock of a foreign corporation by certain domestic corporation or a partnership that represents either substantially all of the assets or substantially all of the assets constituting a trade or business of the distributing corporation or partnership as a direct or indirect acquisition of substantially all of the assets or trade or business assets, respectively, of the distributing corporation or partnership.

Foreign Tax Credits for Sale of Hybrid Entities

Limit foreign tax credits from sales of hybrid entities.

- This provision is intended to address situations in which a taxpayer benefits from the tax attributes of a 338 election, but is not subject to the foreign tax credit restrictions due to the mismatch in the tax treatment of hybrid entities.
- The proposal would apply the principles of IRC Section 338(h)(16) to limit foreign tax credits for the sale of hybrid entities.
- This foreign tax credit limitation would apply to any transactions that occur after the date of enactment.

Excessive Interest Deduction Limitations

Restrict deductions of "Excessive Interest" of financial reporting groups that borrow disproportionately in the United States.

- The proposal provides two options for determining an interest deduction limitation.
    1. "Excessive Interest" is deemed to exist when a US group has a net interest expense to EBITDA ratio that exceeds the global group ratio. Excessive interest expenses are non-deductible in the year in which they are incurred, but may be carried forward and deducted in subsequent years provided that the US group is no longer subject to Excessive Interest limitations.
    2. If the taxpayer fails to substantiate its Excessive Interest calculations, or so elects, under the "10-Percent Alternative," the US taxpayer's interest expense deductions would be limited to the following: US Taxpayer's Interest Income + 10% of US Taxpayer's Adjusted Taxable Income.
- Excessive Interest, IRC Section 163(j), and SHIELD rules may apply to a single intercompany interest payment.
- Where both Excessive Interest and 163(j) are triggered, the lesser disallowance would apply.
- The proposal would not apply to financial services entities or US groups that report less than USD 5 million of net interest.
- Effective for taxable years beginning after December 31, 2021.

Alternative Minimum Tax

Impose a 15% minimum tax on the book earnings of corporations that report more than USD 2 billion of pre-tax net income.

- This provision would serve as an alternative minimum tax (AMT) for companies that report substantial book (but not tax) income.
- Effective for taxable years beginning after December 31, 2021.

Onshoring Incentives / Offshoring Penalties

Provide tax incentives for locating jobs and business activity in the United States and eliminate tax deductions for expatriating jobs and business activity to foreign jurisdictions.

- US taxpayers would receive a 10% tax credit for eligible expenses incurred by a US or foreign group member related to "onshoring" a foreign trade or business.
- "Onshoring" is defined as reducing or eliminating a foreign trade or business and starting up, expanding, or otherwise moving the same trade or business to the United States.
- Conversely, the proposal would disallow deductions for expenses associated with "offshoring" a US trade or business.
- The proposal would be effective for any expenses incurred after the date of enactment.

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