Quarterly tax developments

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

September 2019
Tax developments

Legislation enacted in the third quarter

Companies are required to account for the effects of changes in tax laws in the period the legislation is enacted. These changes are included in a company’s estimate of its annual effective tax rate in the first interim period that includes the effective date of the rate change, but not earlier than the period that includes the enactment date. If an interim change is significant, temporary differences may need to be estimated as of the enactment date.

Federal, state and territories

California – On 1 July 2019, California enacted legislation conforming its tax code to certain provisions of the Tax Cuts and Jobs Act (P.L. 115-97) (TCJA). TCJA provisions to which California now conforms include:

- Disallowing deductions for Federal Deposit Insurance Corporation premiums
- Eliminating net operating loss (NOL) carrybacks
- Limiting like-kind exchanges
- Modifying the cap on deductions for “excessive employee remuneration”
- Eliminating the ability to elect to treat a stock purchase as an asset purchase for California tax purpose if the taxpayer has not made the same election for US tax purposes
- Eliminating the technical termination of partnerships

The changes do not affect California’s general date of conformity to the Internal Revenue Code (IRC), which is 1 January 2015. The changes have various effective dates. See the State and Local Tax Weekly for 19 July 2019.

District of Columbia – On 22 July 2019, the District of Columbia enacted legislation, which Congress subsequently approved, reducing the amount of corporate franchise tax credits that qualified high technology companies (QHTCs) may claim. The legislation also replaces the 6% corporate income tax that applied to QHTC income with the general corporate rate of 8.25%. Other changes include limiting the application of the 10-year credit carryforward to credits based on the wages of qualified employees hired before 1 October 2019. The changes are effective 1 January 2020. See the State and Local Tax Weekly for 23 August 2019.

Hawaii – On 2 July 2019, Hawaii enacted legislation taxing out-of-state businesses on income earned in Hawaii if those businesses engage in or solicit 200 or more business transactions with persons in Hawaii or have gross income attributable to Hawaiian sources of $100,000 or more. The change is effective for tax years beginning after 31 December 2019. See the State and Local Tax Weekly for 22 July 2019.

Illinois – On 1 August 2019, Illinois enacted legislation extending the expiration date of the film production services tax credit to tax years ending before 1 January 2027. See the State and Local Tax Weekly for 2 August 2019.

On 2 August 2019, Illinois enacted legislation extending the expiration date of the research and development (R&D) credit five years to tax years ending before 1 January 2027. See the State and Local Tax Weekly for 2 August 2019.

Missouri – On 11 July 2019, Missouri enacted legislation decoupling from the federal limitation on interest expense deductions. The law also requires companies to deduct interest expense paid in the current year but not deducted on the federal return. The changes apply retroactively for tax years beginning on or after 1 January 2018. See the State and Local Tax Weekly for 2 August 2019.

Welcome to our September 2019 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 laws 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 laws 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 26 September 2019.

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.
Other changes include repealing a tax credit that banks previously could claim against their bank tax or corporate income tax liability, based on their outstanding shares and surplus in Missouri. The change is effective 28 August 2019 for tax years beginning on or after 1 January 2020. See the State and Local Tax Weekly for 2 August 2019 and the State and Local Tax Weekly for 9 August 2019.

**New Hampshire** – On 9 September 2019, New Hampshire enacted legislation adopting market-based sourcing rules for apportioning income earned by multistate businesses from sales and services and intangible property. The changes apply to tax years ending on or after 31 December 2021. See the State and Local Tax Weekly for 20 September 2019.

**Oregon** – On 15 July 2019, Oregon enacted legislation allowing companies to claim an 80% dividends-received deduction for global intangible low-taxed income (GILTI) if certain requirements are met. The change applies retroactively to tax years beginning on or after 1 January 2018. See the State and Local Tax Weekly for 19 July 2019.

On 23 July 2019, Oregon* enacted technical corrections to the new corporate activity tax (CAT), which was enacted in May 2019. Some of the changes include:

- Broadening the scope of businesses subject to CAT
- Adding new exclusions for certain business receipts
- Revising the definition of cost inputs

The CAT, including the technical corrections, is effective for tax years beginning on or after 1 January 2020.

**International**

**France** – On 25 July 2019, France enacted legislation retroactively increasing the 2019 corporate income tax rate on taxable income over EUR 500,000 to 33% from 31% for companies with revenue of EUR 250 million or more. The change applies for tax years beginning on 1 January 2019 through 31 December 2019. The rate on the first EUR 500,000 of taxable income remains at 28%. For tax years beginning on or after 1 January 2020, the rate gradually decreases to 25% by 2022, as scheduled. See Tax Alerts 2019-1269, dated 16 July 2019, and 2019-1342, dated 25 July 2019.

**Portugal** – On 9 September 2019, Portugal enacted legislation clarifying the tax treatment of a real estate investment trust (REIT) under the recently enacted REIT regime. The new law maintains the tax exemption for REITs on investment income (e.g., dividends, interest), rental income and capital gains to the extent the property held for the purpose of being rented for three or more years. The changes are effective upon enactment. See Tax Alert 2019-1635, dated 16 September 2019.

**India** – On 1 August 2019, India enacted legislation decreasing the corporate income tax rate to 25% from 30% for the tax year beginning 1 April 2019 and ending 31 March 2020 for Indian companies with gross receipts of INR4 billion (US$57 million) or less in tax year 2017–2018. Other changes include:

- Providing an alternative one-time 18% tax in lieu of requiring companies to repatriate excess funds held outside India that result from a transfer pricing adjustment to a specific transaction
- Allowing certain Indian companies to claim tax-free treatment for split-offs and spin-offs by transferring their assets and liabilities at other-than-book value
- Taxing the difference between the consideration and money paid to nonresidents on or after 5 July 2019
- Exempting from income tax the difference between a share’s issue price and fair market value, provided certain conditions are met
- Permitting Indian companies in financial distress to carry over tax losses, even when there is a substantial change in ownership, provided certain conditions are met

The effective dates of the changes vary. For discussion of further developments in India, see the “Things we have our eyes on” section of this publication.

* A Tax Alert was not published on this development.
Switzerland — On 6 August 2019, Switzerland enacted federal legislation that, among other things, creates a patent box regime in accordance with the standards of the Organisation for Economic Co-operation and Development (OECD). Under the new regime, up to 90% of net profits from domestic and foreign patents and similar rights may be effectively exempt from tax (reduction percentage at cantonal discretion). Before the patent box can be applied for the first time, the corresponding tax-deducted research and development expenditures must be recaptured and taxed. To the extent that the tax reform measures relate to cantonal and communal income tax law changes, the measures will effectively be implemented through modification of the cantonal tax law. Each canton has its own respective tax legislation process, which requires a standalone review on a canton-by-canton basis to conclude the completion of the legislation process. The changes are effective 1 January 2020.

Turkey — On 19 July 2019, Turkey enacted legislation granting eligible electronic vehicle producers either a cash payment or a tax credit, including an income tax credit. The change is effective upon enactment. See Tax Alert 2019-1315, dated 22 July 2019.

Legislation effective in the third quarter

Federal, state and territories

Colorado — Effective 2 August 2019, companies must include affiliated US holding companies with no property or payroll in their Colorado combined returns. The change was enacted 31 May 2019. See Tax Alert 2019-1071, dated 11 June 2019.

Indiana — Effective 1 July 2019, the corporate income tax rate decreases to 5.50% from 5.75%. The change was enacted 25 March 2014. See the State and Local Tax Weekly for 24 March 2014.

West Virginia — Effective 22 September 2019, companies may claim income tax benefits for investments made in a qualified opportunity zone business located in West Virginia, if the business meets certain requirements. The change was enacted 28 June 2019. See the State and Local Tax Weekly for 9 August 2019.

International

Bangladesh — Effective 1 July 2019, the 12% rate on income from ready-made garments (10% for income from garments produced in a building with green certification) applies until 30 June 2020. The 15% rate on income from the textile sector applies until 30 June 2022. Other changes include:

- Granting income tax exemptions to manufacturing sectors, such as agricultural machinery, furniture, plastic recycling, and mobile phone tower or tower-sharing infrastructure
- Extending income tax exemptions for 21 industries and 17 physical infrastructure development sectors (e.g., bridges, gas pipelines, seaports) through 30 June 2024
- Requiring payment of capital gains tax on or before the date a company transfers shares

These changes, among others, were enacted on 30 June 2019. See Tax Alert 2019-1341, dated 25 July 2019.

Uganda — Effective 1 July 2019, only beneficial owners who are natural persons may claim benefits under an income tax treaty between Uganda and another country. Investors may also claim income tax exemptions for 10 years, provided certain requirements are met. Other changes include:

- Allowing financial institutions and insurance companies to fully deduct their interest expense
- Imposing a 6% withholding tax on purchases of a business or a business asset
- Reducing the withholding tax rate on government securities with maturity periods of 10 years or more to 10% from 20%

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.

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<thead>
<tr>
<th>Countries involved</th>
<th>Summary of changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bahrain</td>
<td>Bangladesh</td>
</tr>
<tr>
<td>Jersey</td>
<td>Mauritius</td>
</tr>
<tr>
<td>Pakistan</td>
<td>Switzerland</td>
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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.

Other considerations

Federal, state and territories

Federal – In a revenue procedure, the Government outlined procedures for complying with IRC Section 451 and its proposed regulations on revenue recognition. See Tax Alert 2019-1631, dated 15 September 2019; see the “Things we have our eyes on” section of this publication for discussion on the proposed regulations.

In frequently asked questions published on the IRS website, the Government identified circumstances under which opportunity zone investors may and may not adjust their tax basis in a qualified opportunity fund investment to fair market value. The Government also explained how a qualified opportunity zone business may demonstrate that at least 50% of its gross income comes from business activities in a qualified opportunity zone for each tax year. See Tax Alert 2019-1534, dated 28 August 2019.

The US Court of Appeals for the Ninth Circuit, affirming the US Tax Court, held that the Government overvalued a buy-in payment that a US company received from its foreign subsidiary as part of a cost-sharing agreement for the use of certain intangibles. The Court reasoned that the 1994-1995 transfer pricing regulations, which were in effect at the time of the payment, did not define “intangible” to include residual business assets (e.g., going concern value, goodwill, “growth options”), which the Government had included in its valuation. See Tax Alert 2019-1504, dated 21 August 2019.

Kentucky – The Government finalized regulations establishing methods of computing a corporation’s NOL deduction and carryforward for members included in a combined report. The new rules apply retroactively to corporate NOL computations for tax years beginning on or after 1 January 2018.

Minnesota – In two separate cases, the state Supreme Court held that a company could not claim a refund based on a recalculation of its Minnesota R&D credit. The Court reasoned that Minnesota law required the company to use the federal minimum base amount limitation, which it did not do when it calculated the state R&D credit on its amended return. See the State and Local Weekly for 9 August 2019.

Montana – The state Supreme Court held that a domestic corporation could fully deduct dividends received from its “80/20” subsidiaries (e.g., domestic subsidiaries with less than 20% of their payroll and property in the US). See Tax Alert 2019-1339, dated 25 July 2019.

New York – The New York Tax Appeals Tribunal held that an out-of-state corporation’s income from online litigation support was not subject to tax in New York because the income was derived from licensing a tool. As such, the law in effect for the years at issue required the income to be sourced to the state where it was earned. See Tax Alert 2019-1452, dated 12 August 2019.

State – The following states released TCJA-related guidance for state corporate income tax purposes:

- Florida (NOLs, the IRC Section 163(j) limitation on interest expense deductions, GILTI, foreign-derived intangible income (FDII), base erosion anti-abuse tax (BEAT) and bonus depreciation, among others)
- Georgia (dividends from sources outside the US)
- Louisiana (BEAT)
- Massachusetts (GILTI and repatriation)
- Michigan (IRC Section 965 repatriation, GILTI and FDII)
- Nebraska (IRC Section 965 repatriation)
- New Jersey (GILTI and FDII)

* A Tax Alert was not published on this development.
Tennessee (IRC Section 163(j) limitation on interest expense deductions, GILTI and IRC Section 965 repatriation)

Vermont (IRC Section 163(j) limitation on interest expense deductions, GILTI, FDII, IRC Section 965 repatriation and bonus depreciation, among others)


Texas – In amendments to its franchise tax rules, the Government limited eligibility for the 0.375% franchise tax rate for retailers and wholesalers. See Tax Alert 2019-1576, dated 5 September 2019.

Wisconsin – The Wisconsin Tax Appeals Commission held that a corporation could claim a dividends-received deduction for distributions it received from a foreign limited partnership that it elected to treat as a corporation for tax purposes under US law. The Court reasoned that the foreign partnership qualified as a corporation under Wisconsin law by virtue of the election. See Tax Alert 2019-1535, dated 28 August 2019.

International

Australia – The Full Federal Court held that a coal mining company could claim a research and development-related tax incentive for expenses from a failed pilot project testing the viability of developing an underground coal gasification facility. The Court found that the lower tribunal interpreted the requirements for claiming the incentive too narrowly. See Tax Alert 2019-1369, dated 29 July 2019.

European Union – The European General Court overturned a 2015 determination by the EU Commission that the Netherlands granted illegal state aid to a domestic company when it approved an advanced pricing agreement. The Court noted that the Commission failed to explain how the company’s transfer pricing method produced a result that was too low. See Tax Alert 2019-1699, dated 25 September 2019.

Hong Kong – In a departmental interpretation and practice note, the Government clarified how to apply the arm’s-length principle to determine transfer prices between related companies. The Government also provided guidance on the treatment of service and intangible transactions. See Tax Alert 2019-1425, dated 6 August 2019.

In another departmental interpretation and practice note, the Government outlined how it will interpret the concept of permanent establishment (PE) in Hong Kong and the methodology for attributing profits to Hong Kong PEs. See Tax Alert 2019-1475, dated 15 August 2019.

Israel – In a tax order, the Government broadened the applicability of Israel’s preferential tax regime for income from intellectual property to include income from certain medicines that are approved by an Israeli or foreign regulator but are not patented. The order applies retroactively for the 2019 tax year. See Tax Alert 2019-1234, 10 July 2019.

In a tax circular, the Government outlined the tax and legal treatment of various types of preferred shares. See Tax Alert 2019-1395, dated 1 August 2019.

Kenya – In a legal notice, the Government outlined the requirements companies must meet to deduct 130% of their total electricity costs. See Tax Alert 2019-1498, dated 20 August 2019.

Malaysia – In supplemental guidelines, the Government identified companies to which the limit on interest deductibility does not apply. For companies subject to the limit, the maximum amount of deductible interest in a tax year is 20% of tax earnings before interest, taxes, depreciation and amortization (EBITDA). Non-deductible interest expense may be carried forward indefinitely, but the 20% limitation for each tax year will still apply in carryforward years. See Tax Alert 2019-1304, dated 19 July 2019.

Separately, the Government announced that it will repeal the current withholding tax exemption on certain service fees, licensing fees and interest paid by an approved multimedia super corridor status company. The repeal will be effective 1 January 2020. See Tax Alert 2019-1634, dated 16 September 2019.

* A Tax Alert was not published on this development.
Things we have our eyes on

**Federal, state and territories**


**TJCA guidance** – The Government issued proposed regulations on the following TCJA-related topics:

- Revenue recognition under IRC Section 451
- Bonus depreciation under IRC Section 168(k)


**Cloud computing** – In proposed regulations, the Government addressed how cloud computing transactions are classified for purposes of the international IRC provisions. The regulations would modify the rules for classifying transactions involving computer programs and apply these rules to transfers of digital content. See Tax Alert 2019-1472, dated 14 August 2019.

**Research credit** – US Senators Maggie Hassan (D-NH) and Thom Tillis (R-NC) proposed legislation that would double the refundable research credit and increase the alternative simplified credit rate for new and small businesses. See Tax Alert 2019-1413, dated 5 August 2019.

**California** – In amended draft regulations, the Government proposed changes to the market-based sourcing rules for receipts from sales of services and intangible property.

**New York** – In revised draft regulations, the Government outlined how to source receipts from sales of digital products and services when apportioning income for corporate franchise tax purposes. See Tax Alert 2019-1311, dated 22 July 2019.

In separate draft regulations, the Government outlined how to source general business receipts for New York apportionment purposes. The regulations address general apportionment rules, apportionment on combined reports and apportionment for rents, royalties, interest income, advertising activities and commodities income, among other things. See Tax Alert 2019-1410, dated 2 August 2019.

**International**


**Chile** – The House of Representatives passed a comprehensive tax reform bill. Proposed income tax changes include:

- Reducing, through 30 April 2022, the tax rate on repatriated profits generated before 2017 to overall 30% from 35%
- Replacing the current withholding rates on dividends distributed by Chilean companies to foreign shareholders with a 35% rate, regardless of the shareholder’s country of residence

* A Tax Alert was not published on this development.
• Permitting foreign shareholders to fully credit the corporate tax paid by the Chilean company against the withholding tax applicable to distributed dividends (overall tax rate of 35%)
• Expanding the types of expenses a Chilean company may deduct from its corporate taxable income
• Aligning Chile’s PE definition with OECD criteria
• Simplifying the tax haven country definition
• Prohibiting the reduced withholding tax rate from applying to interest paid to a foreign financial institution under a back-to-back structure


Denmark – The Government proposed implementing the controlled foreign corporation rules in the EU’s anti-tax avoidance directive (ATAD). The Government also proposed aligning Denmark’s PE definition with the latest OECD definition but leaving certain Danish rules in place. Other proposals include allowing Danish companies to deduct losses incurred by their foreign subsidiaries or PEs or losses incurred on real estate. See Tax Alert 2019-1633, dated 16 September 2019.

Germany – The Government proposed income tax incentives to encourage investment in the development of electric and hybrid cars. Other changes include:
• Allowing German shareholders to claim the 95% trade tax exemption for dividends received from a non-EU company (without requiring the distributing non-EU company to pass an activity test, as currently required)
• Limiting the 95% trade tax exemption to shareholders that own at least 15% (versus the current 10%) of a company, beginning 1 January 2020


India – In an ordinance, the Government reduced the base corporate tax rate to 22% from 25%/30% for Indian companies that meet certain conditions. The ordinance also introduced a 15% base for newly formed manufacturing companies (subject to certain specified conditions). Other changes include withdrawing the share buyback tax for listed Indian companies that publicly announced share buybacks before 5 July 2019, but had not completed the buyback by that date. The changes are effective for tax years beginning 1 April 2019, provided that the ordinance is approved by the Indian Parliament in its next session. See Tax Alert 2019-1698, dated 25 September 2019.

Indonesia – The Government proposed reducing the 25% corporate income tax rate to 22% for tax years 2021 and 2022, and to 20% for tax years 2023 and thereafter. For newly listed Indonesian companies, the rates would be 19% for tax years 2021 and 2022, 17% for tax years 2023 through 2027, and 20% for tax years 2028 and thereafter. Other proposals include:
• Exempting from taxation dividends that Indonesian companies receive from domestic or foreign companies and reinvest in Indonesia
• Modifying Indonesia’s PE definition to permit the Government to tax the profits of companies with significant economic presence, but no physical presence, in Indonesia


Luxembourg – The Government proposed broadening the scope of its anti-hybrid mismatch rules, so they apply to hybrid mismatches between EU member countries and countries outside the EU. The proposal would also eliminate certain hybrid mismatches not affected by the current rules. See Tax Alert 2019-1448, dated 9 August 2019.
Mexico – The Government proposed significant tax measures to align Mexican tax law with the OECD’s recommendations for preventing base erosion and profit-shifting (BEPS). Some of the most relevant proposals include:

- Adopting a general anti-avoidance rule
- Limiting transaction-related deductions for taxpayers with an effective tax rate lower than 22.5%
- Adopting anti-hybrid rules and treating transparent entities as corporations for Mexican income tax purposes
- Limiting interest expense deductions to 30% of “adjusted taxable income” (similar to EBITDA) for companies with more than MxP20 million of annual net interest
- Expanding Mexico’s PE definition, among others


Norway – The Government proposed allowing Norwegian companies to transfer taxable income to related foreign group companies, so the foreign group’s losses could be used. The Norwegian company and the foreign loss company would have to satisfy certain conditions for the loss relief to apply. See Tax Alert 2019-1538, dated 28 August 2019.


South Korea – The Government proposed taxing royalties received for patents that are registered outside South Korea and used in domestic manufacturing. Similarly, compensation paid by a South Korean company for infringing on a patent registered outside the country would be subject to a 16.5% withholding tax, which includes the 10% surtax.

Other proposed changes include:

- Taxing capital gains realized by nonresidents on the sale of their shares in a South Korean real property holding company
- Placing the burden of proof on taxpayers to demonstrate that certain transactions have a valid business purpose and were not intended to avoid tax


United Kingdom – The Government proposed limiting the usage of capital loss carryforwards to offset 50% of annual capital gains, beginning in April 2020. The limit would not apply to certain insurance company losses and certain gains would be exempt.

The Government also responded to recent case law by proposing measures to make sure that the UK rules on taxing disposals of assets by a UK company to a “group” company within the European Economic Area are compatible with EU law. The proposal, allowing the corporation tax due to be paid in installments, only applies to corporation tax that becomes payable for accounting periods ending on or after 10 October 2018. Tax for earlier periods will be governed by ongoing case law developments. See Tax Alert 2019-1252, dated 12 July 2019.