2019 year-end tax considerations for businesses

Legislative changes and other tax concerns that may affect planning

This guide reflects the tax considerations and developments that we believe may create risk or opportunity for businesses in 2019 and beyond. It is not an exhaustive list of all tax issues that may affect your business, but it is designed to help you make informed decisions related to year-end tax planning.

Please see our website for additional information on many of these issues.

October 15, 2019

Introduction

Almost two full years have passed since the Tax Cuts and Jobs Act (TCJA) was signed into law. Over the last two years, the IRS and Treasury have released a considerable amount of guidance in the form of both proposed and final regulations. While some of this guidance has been taxpayer friendly, not all of the proposed regulations yield favorable results. As we approach year-end, taxpayers continue to seek additional clarity about areas where guidance is still pending and assess how any revisions to temporary regulations might affect their business.

Even with the significant amount of TCJA guidance issued, the uncertainty and volume of changes in the law have made it difficult for some taxpayers to take full advantage of the opportunities provided by the TCJA. As it seems unlikely that Congress will pass major tax legislation before year-end, taxpayers should use this time to focus on planning opportunities based on the knowledge gained over the last two years.

We have compiled this guide to help companies make informed decisions related to year-end tax planning. As we continue to receive additional guidance and regulations related to the TCJA, it is important to be aware of how these changes might affect year-end planning and take action when possible.

General considerations

Deduction and revenue planning

For companies looking to reduce taxable income (e.g., to minimize current taxes payable) or accelerate income (e.g., in order to reduce current year net operating losses—NOLs), there are several accounting method approaches that may help accomplish those goals. A few of these include:

- Changing from the cash basis to the accrual basis of accounting, or vice versa
- Conducting inventory planning (e.g., performing a uniform capitalization—UNICAP— review or electing new last-in, first-out—LIFO—sub-methods)
- Accelerating certain deductions or electing to capitalize prepaid expenses for the current year under the 12-month rule

- Electing to recover over 36 months or currently deduct self-developed software costs
- Deferring amounts received from advance payments for goods or services
- Properly using the recurring-item exception for taxes, rebates and refunds
- Shoring up bonus plan requirements to substantiate deducting in the year employees provide the related services
- Accelerating recovery of real property through cost segregation and/or repair studies

Small taxpayer designation

The TCJA increased the threshold for defining a small-business taxpayer to include those with average annual gross receipts of $26 million or less for the three prior tax years, for the tax year beginning after Dec. 31, 2018. This amount is indexed yearly for inflation. Those qualifying under the small business taxpayer designation may be able to use the overall cash method, be exempt from applying certain inventory rules and be exempt from the limitation on interest deductions.

Changes in financial statement treatment for revenue and leases under ASC 606 and ASC 842

As companies begin implementing new audit standards, they often overlook the federal tax implications. To the extent that companies change the timing of an item on their financial statements (such as lease payments or revenue recognition), the company may have to file Form 3115 before the tax treatment can mirror the financial statement change. When reviewing the changes to financial statements, it is also important to consider the impact of the new proposed regulations under section 451(b), which include rules on when to accelerate income recognized on the taxpayer's audited financial statements.

Bonus depreciation

One hundred percent additional first-year (bonus) depreciation is available for qualified property acquired and placed in service after Sept. 27, 2017. The IRS has issued final and re-proposed regulations related to when taxpayers acquire an asset under a written, binding contract. The TCJA expanded bonus depreciation to qualifying used property. The expansion to used property may allow certain business acquisitions to recover a portion of the purchase price immediately through 100% bonus depreciation.

Uniform capitalization regulations

In November 2018, the Treasury and IRS issued new UNICAP regulations providing taxpayers new rules and a new method for capitalizing inventory costs. The new method is one of several that taxpayers can consider when capitalizing costs to inventory and could offer simplicity and tax efficiency in addition to compliance. The final regulations are effective for tax years beginning on or after Nov. 20, 2018; calendar-year taxpayers must apply the new regulations as of their 2019 tax returns. Changes in accounting method (generally automatic) are required to comply with the new regulations. The rules affect both producers and resellers, but affect producers more.

Inventory is often one of the largest assets on the balance sheet of a producer or reseller and historic UNICAP methods are often complicated and out of compliance. Fortunately, the new regulations and the accompanying automatic change procedures offer taxpayers the opportunity to comply with the new regulations while obtaining prior-year audit protection for historic UNICAP methods. Now more than ever, taxpayers should evaluate the impact of these new rules.

Fringe benefits and related issues

The TCJA made changes to the treatment of various fringe benefits that were generally effective for the 2018 tax year. As the end of 2019 approaches and with a tax filing season under these new rules completed, companies need to make sure that any changes in treatment that required changes in the company's record-keeping processes are adjusted for 2019 to ease the compliance burden. Changes may include the following:

- **Loss of the tax exclusion for employer payment of employee moving expenses under section 132(g):** In case you did not have moving expenses in 2018 and your system has not been updated, remember to make sure all employee moving expenses incurred in 2019, paid or reimbursed by an employer, are reported as taxable compensation, subject to FICA/Medicare and federal income tax withholding, by year-end. Once included in employee income, the amounts are deductible as compensation.
- **Loss of the employer tax deduction on most entertainment expenses:** Verify that time and business expense systems are properly collecting and marking entertainment expenses separately from meals expenses, employee recreational expenses and other business expenses, and recorded in separate general ledger accounts. Exceptions to the entertainment expense disallowance may include:

- Sporting event tickets, concerts, golf tournament amounts that are actual charitable contributions or specific advertising expenses, etc.
- Expenses for employee events that are nondiscriminatory, broad-based employee social and recreational events that may have an entertainment element.

- **Reduction of the tax deduction for almost all de minimis fringe benefit food and beverage expenses to 50%:** Confirm meals and business expense systems are properly collecting all de minimis fringe benefit food and beverage costs and separating them from other business costs (such as invoices that bill for both office supplies and coffee and snacks for an office pantry or break room).
- **Loss of the tax deductions for employer-provided parking and transit benefits under section 132(f):** This rule proved very burdensome for many during the 2018 compliance cycle. For 2019, consider separately tracking direct expenses for parking areas or carefully documenting estimates for leased parking areas. The following items should be reviewed to ensure proper treatment:
  - Free parking for employees. The expense disallowance is based on expenses to the employer, not the value to the employee.
  - Pre-tax employee elections to pay for parking or mass transit.
  - Free bus or van service for employees commuting to and from home (unless specifically for safety reasons).
- **Loss of the deduction for employee commuting expenses (except where necessary for ensuring safety of the employee):** Confirm that any expenses incurred to cover or reimburse employee commuting costs are accounted for. This analysis requires an understanding of the definition of business travel for tax purposes; some employee arrangements that appear to be travel may actually be commuting costs. Also, remember that this provision disallows the deduction regardless of whether the benefit is included in income, unlike the transportation disallowance above.

Health reimbursement arrangements

During 2019, the federal departments of the Treasury, Labor, and Health and Human Services jointly published final regulations regarding health reimbursement arrangements (HRAs). HRAs are account-based health plans that employers can use to reimburse employees for their medical care expenses. The goal of these regulations is to give employers more options for providing health benefits to their employees on a tax-advantaged basis. The regulations create two new types of HRAs starting Jan. 1, 2020: Individual Coverage HRAs and Excepted Benefit HRAs. Small and midsize employers may want to add these features to their plans by Jan. 1 to help employees pay for health insurance premiums and other medical costs on a tax-advantaged basis.

Like-kind exchange changes

As a result of the TCJA, deferral of gain under section 1031 is now limited to real property transactions as of Jan. 1, 2018. Real estate exchanges are subject to the same rules and regulations as under pre-TCJA law. In the Conference Committee report on TCJA, footnote 726 clarifies that real property eligible for like-kind exchange treatment under pre-TCJA rules is intended to remain eligible; meaning the definition of real property has not changed.

For tangible personal property, the full expensing election may provide relief for those taxpayers affected by this change. Although the gain from the sale of personal property may no longer be deferred in a like-kind exchange, the full expensing deduction may be used to offset the gain triggered.

Affordable Care Act update

Although the TCJA eliminated the penalty on individuals without health insurance starting in 2019, the TCJA did not repeal the employer penalty. Therefore, applicable large employers (ALEs) that fail to offer employee health insurance that meets Affordable Care Act (ACA) standards may be assessed a shared responsibility payment by the IRS. A company is an ALE if it averaged at least 50 full-time employees (including full-time equivalents) during the preceding calendar year, or was in a group of related companies that met the large employer criteria.

In order to avoid this penalty, a large employer must offer minimum essential health coverage to substantially all (95%) of its employees and their dependents. This coverage must be affordable and provide minimum value (by covering a certain percentage of all medical expenses incurred by employees).

To determine which employers owe the penalty, the IRS requires ALEs to file Forms 1095-C and 1094-C to report workforce and health plan information. For 2019, the due date to provide employees with Form 1095-C is Jan. 31, 2020 (just like Form W-2), and an employer must file Form 1095-C and the related Form 1094-C to the IRS by Feb. 28, 2020, if filing on paper (or April 1, 2020, if filing electronically).

The IRS is currently assessing penalties on ALEs that did not offer ACA-compliant coverage to their employees starting in 2015. In addition, the IRS is pursuing ALEs who failed to file Forms 1095-C and 1094-C in prior years. Since the penalties can be substantial, companies subject to these ACA requirements should review their compliance efforts and understand any potential risk for noncompliance.

Research and development tax credit

The research and development (R&D) tax credit is repeatedly one of the most popular incentives in the tax code. The repeal of the alternative minimum tax as part of the TCJA is making it easier to utilize the R&D tax credit to reduce current tax liabilities.

A small business start-up may claim the credit, up to $250,000, against its FICA payroll tax liability if it had less than $5 million in gross receipts for the current taxable year and no gross receipts for any taxable year prior to the five-taxable-year period ending with the current taxable year. If you wish to make this election and are using an outside payroll provider, it is important to discuss this with them as soon as possible, as the payroll provider must file certain forms on your company's behalf.

In addition, the alternative simplified credit (ASC) continues to be the preferred method elected by many taxpayers, because it relies only upon the prior three years' qualified research expenses to compute the base amount, where the regular credit method requires a much more complex base amount computation that can be difficult to document. The ASC election should be made by completing section B on Form 6765 on the original tax return.

The IRS is asking for more detailed information and documentation during R&D credit examinations. It is critical that taxpayers document R&D project activities and differentiate R&D project costs in their accounting records.

Work opportunity tax credit

The WOTC program was designed to encourage employers to hire and retain individuals from specific target groups with employment barriers and is available through 2019. The program now also applies to employers that hire qualified long-term (27 weeks or more) unemployed individuals on or after Jan. 1, 2016.

The WOTC equals 40% of the first $6,000 of wages, with higher wage limits for long-term family assistance recipients and qualified veterans for the first tax year an employee is hired. The credit is reduced to 25% for individuals who work at least 120 hours, but fewer than 400 hours, during the one-year period beginning on the employment date.

There is no credit for individuals who work fewer than 120 hours in their first year of employment. The WOTC also includes 50% of second-year wages for the tax year for wages paid to long-term family assistance recipients.

Employer credit for paid family and medical leave

This tax credit was enacted as part of the TCJA and provides a tax credit of between 12.5% and 25% for wages paid to qualifying employees on family or medical leave in calendar years 2018 or 2019. To qualify, employers must maintain a written family and medical leave policy providing qualifying employees at least two weeks of paid family and medical leave and paying at least 50% of the normal wage rate during the leave period. There are special rules regarding part-time employees and payments to employees earning above a certain amount are not eligible.

Business taxpayers should review their family and medical leave policies and determine if they qualify. This is only a two-year tax credit program and it is uncertain whether Congress will extend this credit for additional years.

Energy credits

Tax credits for many types of renewable energy were retroactively reinstated by the Bipartisan Budget Act of 2018. The residential energy efficient property credit was extended with certain reduced-rate modifications through 2021. The business energy investment credit was further extended for solar and extended with a phase-out for other renewables as follows:

- The 30% investment tax credit for qualified solar property is available through 2019, with a 26% credit available in 2020 and a 22% credit available in 2021. After 2023, the credit is reduced to 10%.
- The 30% investment tax credit for fiber-optic solar lighting, qualified fuel cell property and qualified small wind property is available through 2019, with a 26% credit available if construction begins in 2020, a 22% credit available if construction begins in 2021 and no credit if placed in service after 2023.
- The 10% investment tax credit for qualified microturbine property and combined heat and power system property (with certain rate modifications) is available if construction begins before 2022.
- The credit remains at 10% for geothermal equipment with no expiration.

The renewable electricity production tax credit (PTC) for large wind projects is at a rate of one cent per kilowatt-hour of electricity sold each year for 10 years. If the taxpayer makes an election to claim the investment tax credit related to qualified wind property in lieu of the PTC, the credit rate is 12% if construction begins in 2019. Taxpayers who wish to take advantage of the PTC when the property is placed in service should either plan to spend more than 5% of the eligible wind farm construction costs by the end of 2019 or take steps to begin physical work of a significant nature on the facility.

Tax credits that expired at the end of 2017

The determination as to whether or not any expired tax credits will be retroactively extended is predicated on what happens with any year-end tax legislation. At this time, it is uncertain whether Congress can agree on an extenders package that would pass before the end of the year. However, refund opportunities may still exist for certain unclaimed $0.50 per gallon alternative fuel credit or $1 per gallon biodiesel and renewable diesel credit for prior years.

There is still an opportunity for qualified sellers or users to register as alternative fuelers by filing Form 637 and then filing refund claims for open years for an elective income tax credit in lieu of the standard excise tax credit or payment.

IRS account transcripts

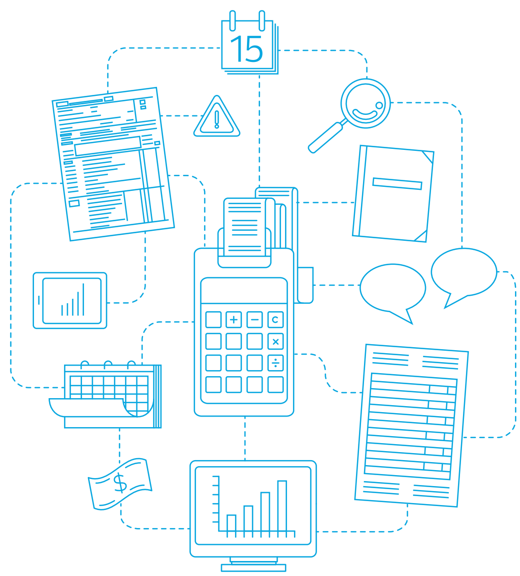
A company's IRS account transcript contains useful information, including the information necessary to confirm estimated payments or credit elects applied to the 2019 tax year before preparing an extension or filing the return. For prior years, the account transcript can identify items of which the company may be unaware, such as penalty or interest assessments, math error adjustments or examination indicators. Thus, companies should consider ordering an account transcript in January 2020 for 2019 and earlier years. Beginning June 28, 2019, the IRS stopped transmitting transcripts to requesting companies via fax. Instead, the IRS will mail the transcript to the company's address of record. The transcript can take up to two weeks to be transmitted by mail. For this reason, we recommend that you make the request by Jan. 15, 2020, to ensure it is received timely. To order a transcript to be mailed, call the IRS business line at +1 800 829 4933.

Tax return due date reminders

For tax years beginning after Dec. 31, 2015, tax return due dates changed. Calendar year C corporation returns and most fiscal year returns are due on the 15th day of the fourth month following the end of the fiscal year, and S corporation and partnership returns are due on the 15th day of the third month following the end of the fiscal year. Form 7004 provides for an automatic extension of six months after the regular due date.

For C corporations with a fiscal year ending on June 30, the effective date change is delayed until the first tax year beginning after Dec. 31, 2025. Accordingly, those returns are due Sept. 15.

The deadline for filing Forms W-2, W-3 and 1099-MISC (Box 7) reports with the Social Security Administration is Jan. 31 for paper or electronic filing.



Accounting for income taxes under ASC 740

In preparation for year-end, companies should continue to assess the impact of the TCJA on their provision for income taxes. Several areas may require additional attention in the current year and companies may want to begin evaluating these items with preliminary data prior to year-end. These areas include items that may be permanent in nature, primarily, section 162(m) limitations, foreign-derived intangible income (FDII) and the global intangible low-taxed income (GILTI) provision. Additionally, where companies are using the reversal of deferred tax liabilities to support the realization of deferred tax assets (specifically, interest expense and NOLs), companies should begin scheduling these reversals to ensure that the expected timing of these reversals supports the realization of deferred tax assets.

Companies should also pay careful attention to the release of any final regulations between now and year-end and make adjustments as necessary. Companies that did not follow sets of proposed regulations during 2018 should evaluate whether a reserve for uncertain tax positions is required. If a company believes it will benefit from the GILTI high-tax exclusion, companies should be aware that the effect of these regulations should not be reflected in a company's provision until these regulations are final.

Finally, companies should review their state tax filings for the many state tax changes since the passage of the TCJA. This review should consider where state tax law has or has not conformed to the federal changes.

Corporate and transactional considerations

File Form 4466 in January to obtain a quick refund

Corporations can receive a quick refund (generally in less than 45 days) of federal estimated tax payments in excess of the company's estimate of its tax liability for the year. The company must file Form 4466 after the close of its tax year but before the un-extended due date of its Form 1120 to receive this quick refund. The company can designate that the excess amount be credited to another IRS liability. Penalties may apply if the requested refund (or credit to another liability) leaves the corporation underpaid for estimated tax purposes.

Consider filing an automatic extension even if the return will be filed on time

The timely filing of Form 7004, *Application for Automatic Extension of Time to File Certain Business Income Tax, Information, and Other Returns*, will provide an automatic six-month extension of time to file a Form 1120 corporate income tax return for calendar-year corporations.

Filing the extension may be beneficial even if the corporation files the return the next day. A valid automatic extension request extends the time for a calendar-year corporation to file its return for six months from the original due date of the return. Note that for calendar-year corporations, the original due date for Form 1120 is April 15, 2020.

The extension period allows companies time to make corrections to the return, up to the extended due date, without penalty—including making timely tax elections or applying automatic accounting method changes if omitted from the initial filing. A subsequently filed return containing these items filed before the extended due date would supersede the previously filed return that omitted them. The superseding return becomes the official return and the statute of limitations on assessment will expire (under normal circumstances) three years from the date the taxpayer files the return.

Accelerating subsidiary stock losses

For consolidated taxpayers, two planning opportunities may be available to accelerate and recognize losses in the current year. Consolidated groups with an insolvent subsidiary should evaluate whether it makes sense to claim a worthless stock deduction. Claiming the deduction may require liquidating the insolvent subsidiary or converting it into a limited liability company (LLC). Alternatively, a disposition of the subsidiary stock could accelerate the recognition of the loss.

Accelerating section 481 adjustments in the year of an M&A transaction

Taxpayers have the ability to accelerate income into the year of certain mergers and acquisitions (M&A) transactions and possibly the year prior under rules provided by the IRS. These rules can provide tax advantages in situations where section 382 limitations would limit the ability to offset such income post-transaction. For certain accounting method changes, a taxpayer must file the method change request prior to the end of the tax year in order to obtain this treatment.

Identifying unamortized debt issuance costs

Companies that have refinanced debt or taken out new debt during the tax year should evaluate whether any previously unamortized debt issuance costs are eligible for accelerated tax deduction during the current year. In addition, companies should also assess whether certain fees paid to lenders as part of the refinancing or issuance of new debt may qualify as original issue discount (OID). Any amounts treated as OID must be amortized over the life of the debt and may be subject to the business interest limitation under section 163(j).

Federal income tax mulligan

While not a new ruling, Rev. Rul. 80-58 allows taxpayers to rescind a transaction. While this is difficult to accomplish and little guidance exists in this area, this ruling does provide an avenue for rescission. However, to successfully complete a rescission, it must occur within the same tax year as the transaction. As a result, this item warrants consideration during year-end planning.

Section 382 closing of the books election

Corporations should carefully monitor changes in stock holdings and stock issuances that occur during the year in order to identify whether the company has undergone a section 382 ownership change. Corporations undergoing a section 382 ownership change may make a closing-of-the-books election. Addressing whether or not the corporation will make the election may result in significant tax benefits.

The corporation may prefer to maximize the amount of its income for the taxable year treated as accruing prior to the ownership change to maximize use of NOL deductions (or certain other deductions). If it files a closing-of-the-books election with its timely filed tax return, the corporation closes its books at the date of change for section 382 purposes, thereby specifically measuring income and deductions pre- and post-change. Without the election, under the default rule, the corporation applies daily proration of the entire year's items of income and deductions.

Addressing the closing-of-the-books election decision before the end of the year can assist with year-end tax planning, since it helps position the company to determine whether acceleration of income or deduction items would be advantageous.

Accelerating an ownership change

On Sept. 10, 2019, the IRS and Treasury proposed new regulations under section 382, which provides a limitation of certain tax attributes (e.g., NOLs) where a corporation undergoes an ownership change. One major departure from the current rules is the proposed removal of one of the two safe harbors for calculating the recognition of built-in gain (or loss), the section 338 approach. The section 338 approach is generally more favorable for companies in built-in gain positions. Companies in a built-in gain position tend to be those that derive most of their value from self-created intangibles with no tax basis. It is expected that life science and technology companies would be particularly affected by the removal of the section 338 approach.

Companies that are contemplating an ownership change in the near future (e.g., a stock offering) should consider accelerating the ownership change to take advantage of the section 338 approach before the IRS and Treasury finalize the regulations as proposed.

Projecting earnings and profits

During year-end planning, it may be important for a corporation to project the remaining current-year earnings and expected 2020 earnings along with cumulative earnings and profits. These projections can aid companies planning to distribute cash (or other property) to shareholders in deciding the tax year in which to make the distribution.

Form 8937, *Report of Organizational Actions Affecting Basis of Securities*

C and S corporations that take organizational actions that affect the basis of securities in the hands of stockholders generally must file Form 8937 within 45 days of the transaction date, or by Jan. 15 of the year following any such actions that take place in December.

Organizational actions include stock splits, stock dividends and distributions that are fully or partially nontaxable, and some reorganizations. S corporations may report the required Form 8937 information on Schedule K-1 instead of Form 8937, and a company may meet Form 8937 filing requirements through appropriate postings on the company's website.

Corporations should analyze their transactions to ensure that they timely meet the filing requirements under Form 8937.

Realizing maximum benefits through a transaction cost analysis

When a company engages in a transaction such as a merger, sale of an entity, acquisition of an entity or business combination (either on the buy-side or the sell-side), the IRS requires costs incurred to facilitate the transaction to be capitalized. With stock transactions, these costs generally are capitalized into stock basis and are not recoverable until such stock is sold. Alternatively, with asset transactions, these costs generally are capitalized and amortized over a period of time, typically over 15 years on a straight-line basis. In contrast, costs that do not facilitate a transaction can generally either be deducted as incurred or amortized over 15 years.

Performing a TCA allows a company to identify nonfacilitative costs and maximize tax deductions. A TCA involves a thorough analysis of activities performed and expenses incurred in connection with exploring and entering into a merger or acquisition transaction. The study results in the determination and proper documentation of the appropriate federal income tax treatment of transaction costs. Without proper documentation, all transaction costs generally must be capitalized, rather than deducted during the year paid or incurred.

Section 163(j)

The new section 163(j) enacted under the TCJA generally limits the deduction of business interest to the sum of the taxpayer's business interest income for the year and 30% of the taxpayer's adjusted taxable income for the year. Prior to the end of the tax year, taxpayers should consider converting debt to equity or refinancing debt in order to reduce the amount of interest subject to section 163(j) for the remainder of the year.

Section 162(m)

The TCJA affected public companies by significantly changing the rules of section 162(m) for the $1 million limitation on executive compensation. Under the changes, performance-based compensation (other than under limited transition relief) is no longer exempt; a broader group of companies are subject to section 162(m) limitations; and the list of "covered employees" whose compensation is subject to the limitation is expanded. Under the new covered employee definition, once a person is a covered employee in any year after 2017, the employee is always a covered employee, and the company is subject to the limitation on tax deductions for compensation paid to that individual over $1 million, even if the amounts are paid at retirement or death. To the extent some of the section 162(m) changes did not have a tax impact during 2018, this may have not been a priority item to address. However, a list of covered employees should be started as soon as possible as contemporaneous records will be helpful in tracking covered employees.

International tax considerations

Foreign-derived intangible income planning

The FDII rules are an incentive for U.S. companies to sell goods and provide services to foreign customers. By using the new FDII regime, as well as the decreased federal corporate income tax rate, foreign-owned U.S. corporations may be able to significantly reduce the group's overall tax burden where eligible functions such as R&D or certain services are relocated to the United States.

Further guidance is expected from the IRS to explain the operations of this new regime.

Global intangible low-taxed income planning

The TCJA enacted a new rule that requires certain shareholders of foreign corporations to include into current income their share of GILTI. GILTI can apply to a broad swath of taxpayers in any industry, so U.S. shareholders need to assess whether they may have exposure to this new income inclusion. Planning opportunities to limit a taxpayer's exposure to GILTI are available and should be considered in order to minimize the impact of this new tax scheme.

Base erosion and anti-abuse tax planning

The TCJA introduced the BEAT, an additional tax designed to ensure that corporations with significant base erosion payments made to related foreign parties pay a certain amount of U.S. federal income tax. This tax is in addition to a corporation's regular income tax liability. Taxpayers with more than $500 million of average annual gross receipts and deductible payments to foreign related parties should carefully consider the impact of tax credits (such as the R&D credit) and NOLs on the likelihood of paying the BEAT.

Foreign tax credit planning

The TCJA also introduced significant changes to the system of international taxation. In late 2018, the Treasury and IRS issued proposed FTC regulations setting forth several transition rules and elections that may limit taxpayers' ability to use excess FTCs going forward. Taxpayers with significant pre-TCJA carryforward or post-TCJA carryback credits should carefully consider how their unused FTCs may be limited and which election may be available to allow for an efficient utilization of FTCs.

Base erosion and profit shifting and country-by-country compliance

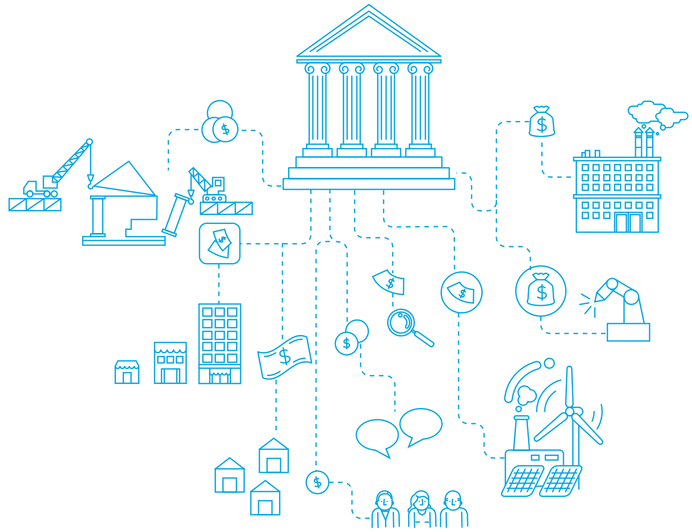
In line with the Organisation for Economic Co-operation and Development's BEPS project, the IRS issued final regulations in 2016 requiring annual country-by-country reporting (CbCR) by U.S. taxpayers that are the ultimate parent of a multinational enterprise group. This tax filing requirement applies to companies with $850 million or more in global group revenues.

Taxpayers who wish to avoid filing in non-U.S. countries should consider filing Form 8975, *Tax Jurisdiction and Constituent Entity Information, with the IRS*, because filing this form in the United States will satisfy any filing requirements in other countries.

This reporting requirement is still relatively new and may have required taxpayers to significantly change their information reporting processes. Accordingly, affected taxpayers should carefully review the financial and administrative impact CbCR may have had on their compliance function and reevaluate if necessary.

Transfer pricing planning

In addition to considering whether to file Form 8975, taxpayers should consider a variety of important transfer pricing issues before year-end. For example, taxpayers should ensure that year-end true-ups are performed with respect to any cost allocations and should reconcile financial statement results to those required by any relevant transfer pricing documentation that is in place.



Taxpayers should ensure that intercompany transactions are supported by an appropriate agreement. Moreover, taxpayers should conduct a high-level risk assessment of global intercompany activity and consider whether to update any existing transfer pricing documentation, either because of a change in facts or because the documentation is out-of-date.

Planning for payments between foreign subsidiaries

U.S. taxpayers generally pay tax on foreign income earned by a non-U.S. subsidiary when the subsidiary makes a distribution of income to the U.S. shareholder. However, payments made between offshore subsidiaries often trigger income inclusions to a U.S. shareholder, even if the U.S. shareholder receives no money.

The TCJA did not make permanent an exception to the law that allows a foreign subsidiary to pay another foreign subsidiary without triggering income to U.S. shareholders. As a result, the exception is scheduled to expire for taxpayers with tax years starting on or after Jan. 1, 2020. It is unclear whether Congress will make this exception permanent as part of a possible extenders package.

In the absence of a permanent exception, taxpayers should consider their planning alternatives in order to mitigate potential income inclusions arising from payments between foreign subsidiaries.

Intercompany loan planning

Under current law, a loan or equity investment in a U.S. company by a related foreign subsidiary can result in an income inclusion to a U.S. shareholder of the foreign subsidiary. Even a guarantee by a foreign subsidiary can trigger an income inclusion.

Many taxpayers are unaware of this rule and may have such U.S. investments in place at any given time. However, taxpayers can minimize the adverse impact of this rule by reducing or eliminating U.S. investments or guarantees by foreign subsidiaries before the end of the year.

The changes to the anti-deferral rules under the TCJA should result in fewer taxpayers having exposure to this rule; however, taxpayers using a CFC or its assets as collateral for borrowing should remain aware that certain traps remain.

Review cost-sharing agreements

The story of *Altera v. Commissioner* is a long one. By all accounts, it only looks to get longer. In July 2018, the U.S. 9th Circuit Court of Appeals overturned the U.S. Tax Court's unanimous 2015 decision in *Altera v. Commissioner*, which had effectively invalidated the IRS cost sharing regulations. In July 2019, a 9th Circuit panel of three judges confirmed the 2018 decision. However, in August 2019, Altera filed a petition for an en banc review by the entire 9th Circuit Court. As it currently stands, the 9th Circuit Court decision reverses the U.S. Tax Court's decision on this issue, holding that the Treasury's rule was not arbitrary and capricious, because the Treasury provided a sufficient basis for its decision-making. Many taxpayers have taken positions for financial accounting purposes and in protective tax returns claiming a benefit under the decision of the Tax Court. These taxpayers should immediately evaluate the impact of this appellate decision, because it is unlikely the Supreme Court will entertain an appeal of this decision. Taxpayers should evaluate whether to adjust their ASC 740 reserves and whether this decision will affect interim tax provisions as a potential change in law.

For further information, see [Altera saga continues as taxpayer seeks revisit of IRS victory](#).

Exporters should consider a domestic international sales corporation

The U.S. provides incentives to boost exports of some domestic goods. Taxpayers may exclude tax commissions paid to a domestic international sales corporation for supporting overseas sales. When ultimately paid to individual DISC shareholders, DISC commissions are taxable at a 20% rate instead of the higher corporate or individual rates that apply to ordinary business income.

DISCs involve little cost, but a new legal entity must be established, which requires a separate tax return, and all shareholders must elect DISC status before the tax year begins. Thus, interested taxpayers should make a DISC election for 2020 before Jan. 1, 2020.

Key global information reporting action points

Prepare for renewed focus on nonresident aliens and Foreign Account Tax Compliance Act exams

Post TCJA, the IRS' Large Business and International (LB&I) division announced several new compliance campaigns in 2019 focused on enforcement of withholding, deposit and reporting requirements for payments made to U.S. nonresident aliens. The campaigns will be enforced through a variety of mechanisms including examinations and penalty assessments. The IRS also announced the launch of a campaign focused on identifying U.S. and foreign financial institutions that have failed to file FATCA reports. Examinations are expected to commence in 2020, which means that companies have a very narrow window of opportunity to become compliant.

Companies should plan to spend the close of the year identifying and remediating any gaps in processes, submitting any unfiled returns, and implementing policies and procedures for ongoing compliance with these rules. The IRS has indicated that it will accept voluntary disclosures regarding noncompliance before institutions receive notices. However, penalty abatement will not be an option once a notice has been received, so take action now!

Reevaluate the FATCA and CRS status of entities in the group

To the extent that companies have acquired or created new legal entities, restructured the group this year, moved into jurisdictions that have adopted the Common Reporting Standard (CRS), or entered into an intergovernmental agreement (IGA) under FATCA, the company should plan to reevaluate or confirm the FATCA and CRS status of legal entities in the group. Entities that accept deposits, have custody of assets, perform investment activities, or serve as captive insurance companies or certain holding companies may be considered foreign financial institutions and may have FATCA and CRS reporting obligations.

Monitor and implement changes to information returns for the TCJA

Withholding agents should carefully monitor changes in new versions of information returns that have been published post-TCJA and should update their systems and any substitute forms or instructions as required. A new draft 2019 Form 8966, *FATCA Report*, has been published for example, along with a draft 1099-NEC that the IRS proposes will be used to report nonemployee compensation (NEC) starting for tax year 2020. Changes to these forms will have significant cost and procedural implications. Therefore, companies should begin discussions with their tax operations, technology and legal teams now to plan for these changes and should update their systems and withholding processes for changes as soon as possible. Additionally, to the extent that substitute forms are used, withholding agents will need to build in sufficient lead time for budget approvals, drafting and revising recipient guides, and design of new forms, as needed.

Prepare to begin collecting new W-8s

Companies should begin requesting new Forms W-8 and CRS self-certifications from new investors, customers opening new accounts, or those with forms that will expire after Dec. 31, 2019. Note, however, that valid unexpired Forms W-8 can still be relied on and do not need to be replaced until they expire (generally within three years) unless there is a change in circumstances that mandates collection of a new form.

Prepare to start section 6050Y reporting of life insurance contracts

The TCJA introduced section 6050Y, which imposes new information reporting requirements for certain life insurance contracts with reportable death benefits paid and reportable policy sales made after Dec. 31, 2017. The IRS has delayed any reporting under section 6050Y until final regulations are issued, but has issued transitional guidance to assist companies preparing to satisfy these requirements once final regulations are issued. Companies should begin assessing the impact of these reporting requirements on their operations and should be prepared to start reporting once final regulations are issued.

According to the rules, section 6050Y reporting will be required by (1) anyone who acquires a life insurance contract, or any interest in a life insurance contract, in a reportable policy sale; (2) an issuer of a life insurance contract upon notice of a transaction required to be reported above or upon any notice of a transfer of a life insurance contract, or any interest in a life insurance contract, to a foreign person; and (3) any payor of reportable death benefits.

For purposes of these rules, reportable death benefits are defined as the amount paid at the death of the insured under a life insurance contract that was transferred in a reportable policy sale. Likewise, a reportable policy sale is defined generally as the acquisition of an interest in a life insurance contract, directly or indirectly, if the acquirer has no substantial family, business or financial relationship to the insured.

Companies should evaluate their assets and business activities to ascertain whether they have a section 6050Y reporting obligation and should implement systems and procedures for complying with this requirement going forward as needed.

Pass-through entity considerations

Consider application of the section 199A deduction

Section 199A allows for a deduction of up to 20% of a taxpayer's "qualified business income" (QBI). QBI generally includes most "trade or business" income reportable on an individual's income tax return, often attributable to the individual's share of income from pass-through entities. However, certain exceptions do apply. Notably, foreign source income, investment income, and income from certain listed "specified service trades or businesses," among other items, generally will not constitute QBI and would thus not be eligible for the deduction. For income that does constitute QBI, this deduction effectively reduces the top income tax rate applicable to that income from 37% to 29.6%. The deduction does not apply to self-employment or net investment income taxes. However, the deduction is applicable in computing alternative minimum taxable income.

Pass-through owners whose taxable income exceeds $160,700 (or $321,400 for a joint return) are subject to limitations on the deduction. These taxpayers may see the deduction reduced or fully eliminated if the business does not pay sufficient wages to its employees; does not employ sufficient amounts of tangible, depreciable assets in the business; or conducts business activities considered in whole or part to be a "specified service" business described in the law.

While beneficial to many, this new deduction has brought with it new reporting requirements and complexities for pass-through entities and their owners. The proposed regulations issued in 2018 addressed many areas of uncertainty and have since been replaced by final regulations. The final regulations largely follow the proposed regulations and clarify some of the uncertainty left in the wake of the proposed regulations. For tax years 2019 and forward, taxpayers may no longer rely on the proposed regulations and instead will be subject to the rules outlined in the final regulations.

Uncertainty still exists in several areas, particularly whether certain business activities involve the performance of services in certain nonqualifying "specified service" business fields—such as consulting and health care. Additionally, new guidance from the IRS has made the reporting requirements associated with entity-level aggregation of businesses for purposes of calculating the deduction much more complex than originally anticipated.

Given the complexity, pass-through business owners should consult with their tax advisors when evaluating their eligibility for the 20% deduction, evaluating compliance with the final regulations and considering whether changes to their business could enhance the benefit.

Bonus depreciation available for certain "step-up" transactions

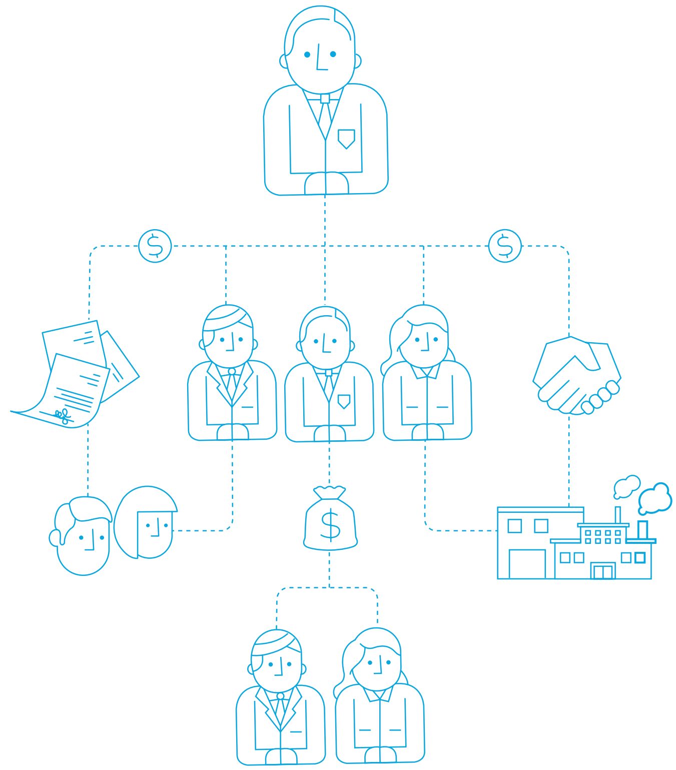
Historically, purchasers of partnership interests were able to generate additional depreciation deductions through step-up elections; however, these step-ups were not eligible for bonus deprecation, as they generally represented the indirect purchase of a used asset. As noted above, the TCJA changed this rule to allow bonus depreciation for purchases of used assets.

Final regulations regarding bonus deprecation issued in 2019 closely follow the proposed regulations issued in 2018. The final regulations clarify how the rule changes affect step-up depreciation generated by the acquisition of an interest in an existing partnership and similar transactions. In many cases, but not all, the purchaser will benefit from this immediate deduction to the extent its share of the step-up is allocable to qualified assets. Although the final regulations provide clarity on the application of the bonus depreciation rules to certain step-up transactions, there is still uncertainty surrounding the availability of bonus depreciation for certain transaction structures—such as those involving the purchase of all interests in a partnership by an existing partner or the contribution of assets to a partnership in exchange for both equity and money.

Taxpayers considering transactions that may generate a step-up, or in transactions that could be restructured to generate such a step-up, should pay particular attention to these final regulations. Prior to finalizing the structure of a transaction, each transaction should be analyzed to determine whether, and to what extent, expensing is available, as well as the corresponding tax consequences to the seller. In addition, some transactions that have already closed, but are subject to the new bonus depreciation rules, should be reviewed to ensure that the optimum allowable tax treatment is obtained.

Passive loss and net investment income tax planning

Individuals, closely held C corporations and personal service corporations are generally restricted in their ability to deduct losses from passive activities. Passive losses include losses from rental activities and other business activities in which the taxpayer is not actively involved. However, taxpayers who can demonstrate the necessary level of participation may be able to generate a current deduction for these losses and generate significant income tax savings.



The keys to doing so are: (1) understanding how much participation is necessary, and (2) ensuring that the participation can be substantiated. In most cases, a taxpayer must devote at least 500 hours to an activity in order to avoid the limitations on passive losses. However, in some cases, a taxpayer may only need to participate for 101 hours in an activity in order to deduct these losses. Thus, taking action now to increase one's participation can, in some instances, provide a valuable tax deduction.

In situations where the business activity generates a net profit, participation is also relevant when trying to minimize exposure to the 3.8% net investment income tax under section 1411. Owners of pass-through entities usually can avoid the tax on their distributive share of income if they participate in the business for at least 101 hours during the year.

In sum, finding ways to help owners meaningfully participate in a business can have the added benefit of significantly reducing their tax burden.

Reconsidering entity choice

Most pass-through businesses consider their entity structure only once, at the time of formation. However, the TCJA has taken the traditional rules and turned them upside down, leading many partnerships, LLCs and S corporations to reconsider their choice of entity. Under the TCJA, corporate tax rates were reduced from 35% to 21%, while pass-through businesses, such as S corporations and partnerships, may now qualify for a pass-through deduction that effectively cut their tax rates from 39.6% to 29.6%.

This has led many businesses to analyze whether their current tax structure is still efficient. Important issues to consider when reevaluating entity choice include:

- Why should I remain an S corporation, effectively paying a 29.6% or 37% tax rate, if I can get a 21% tax rate as a C corporation?
- Can my partnership convert to C corporation status and enjoy the lower corporate tax rate?
- Are there issues beyond the annual tax savings I should be considering?
- Are there self-employment tax implications? What about changes to how the owners are currently compensated?
- What role do state and international considerations play in this decision?
- What is the future exit strategy?

Analyzing the interplay of these potentially competing factors is complex, but understanding the implications of entity type on a business's overall tax burden is critical in light of these tax rate changes.

IRS compliance campaign affecting S corporations

The IRS LB&I division has identified and selected specific issues on which to focus its compliance efforts through a campaign approach. One of those campaigns focuses on S corporation shareholders who may have claimed losses in excess of their basis in the entity and shareholders' obligation to track (and report) their stock and debt basis when reporting flow-through losses from the S corporation.

S corporation shareholders can take action in anticipation of this campaign, both to ensure that they have adequate records to support their basis calculations and to potentially generate basis before year-end in order to utilize previously suspended losses.

New loss limitations

The 2017 tax law includes a new provision that limits an owner's ability to deduct active business losses against nonbusiness income. Previously, active losses could be offset against all income, with no limitation on deductibility. Under the new law, "excess business loss" deductions are limited to income plus a threshold amount of $250,000 ($500,000 for married filing joint filers). Any losses that are limited under this new provision are carried over and become NOLs in subsequent years. This generally results in a one-year deferral of the excess loss. However, the new tax law also limits the utilization of NOLs to 80% of taxable income in any given year. Accordingly, NOLs generated as a result of this new active business loss limitation will likewise be subject to additional restrictions.

Taxpayers should review their active business income and losses to evaluate whether any losses would be fully offset against active business income or whether they may be subject to this new loss limitation.

Planning for the new partnership audit rules

All entities organized as partnerships for federal tax purposes will be affected by the new partnership audit rules enacted in late 2015 and effective for partnership tax years beginning on or after Jan. 1, 2018. These rules, among other issues, raise the specter of a required entity-level payment of tax on any audit adjustments. Partnerships subject to these rules will need to designate a partnership representative whose powers to bind the partnership will go well beyond the tax matters partner of prior law. As a result, these new audit rules may create significant new business conflicts among current partners, as well as former partners and managers.

Since enactment, additional regulatory guidance, as well as technical corrections to the statute itself, have become effective. Most critically, both the regulations and technical corrections clarify that the "push-out" mechanism, by which partnerships can place the burden of examination-related tax adjustments on their partners—the partners in the year being examined—by issuing them statements showing their share of any adjustments, will be operable through tiered partnership structures.

Although audits subject to this new regime may not begin until 2020, potential conflicts and risks could exist now, particularly when transactions involving uncertain tax positions may be subject to audit under the new regime. Therefore, we recommend that partnerships act immediately to ensure that appropriate governance and operating provisions are in place in the partnership's governing documents to adequately protect the interests of current partners, former partners and management.

Additionally, partnerships subject to the new partnership audit rules (i.e., partnerships that are not eligible to elect out of the new rules) may no longer file an amended return, and must instead file an administrative adjustment request to correct items on a previously filed tax return. Consequently, partnerships may wish to consider extending their federal tax returns regardless of when the tax return will actually be filed. In the event the partnership identifies an incorrect item after the return is filed, but before the extended due date of the tax return, the partnership would be permitted to file a superseding return to correct the item by the extended due date. Partnerships that identify errors after filing, but that have no such extension in place, would need to file an administrative adjustment request to deal with such an error.

Self-employment tax considerations for partners

Several tax court decisions, in conjunction with other forms of guidance including long-standing and controversial proposed regulations, have created an unclear picture as to the treatment of members of LLCs and limited liability partnerships (LLPs) under the self-employment tax rules.

The IRS has taken aggressive positions in this area. Recent decisions indicate that in certain cases LLCs may want to consider modifications to their governance rules, substantiating the fact that certain portions of income are exclusively a return of capital (and not compensation for personal services), or adopting a limited partnership structure. These changes may provide greater confidence regarding the application of the self-employment tax to members of LLCs and LLPs.

Partners as employees

Partnerships or LLCs may find treating partners as employees provides several benefits, including state tax benefits and overall simplification of reporting wages via Form W-2 instead of Schedule K-1. Several recent developments in the law, both favorable and unfavorable, affect when this practice may be permissible. This includes unfavorable regulations denying employee treatment under structures in which the partners of a tax partnership are employees of a single-member LLC owned by the tax partnership. The regulations also clarify that using a professional employer organization does not achieve employee status for partners in the partnership.

A partnership or LLC considering taking or maintaining a position that some of its direct or indirect partners are direct or indirect employees may want to consider adopting a tiered structure so that employees are partners in a holding company rather than the tax partnership that is their actual employer. Additionally, partnerships or LLCs considering taking this position will also want to analyze the impact such a decision may have on their partners' ability to utilize the new pass-through deduction afforded by section 199A. Specifically, W-2 wages paid to direct or indirect partners will not be considered qualified business income and, thus, are not eligible for the new deduction.

Planning in this area can generally produce the desired result with minimal hurdles.

New carried interest legislation

The TCJA added a new provision affecting the treatment of so-called "carried interests," defined generally as partnership interests received in exchange for services in certain specified businesses in the investment and real estate industries. This provision has the practical impact of converting capital gain income into ordinary income in certain circumstances.

Many exceptions and nuances apply to this new recharacterization rule. We recommend that taxpayers expecting a large carried interest realization event consider the applicability of this new provision and discuss potential mitigation strategies with their tax advisors.

Taxpayers should also be aware that this carried interest information might be reported to all partners via Schedule K-1 footnotes, even when the carried interest rules may not be applicable to the individual partner. Taxpayers should consult their tax advisors to determine whether the carried interest recharacterization rules apply to their individual circumstances.

New pass-through basis reporting requirements

In late 2018, the IRS changed the instructions to Forms 1065 and 1040 and included new and expanded reporting requirements. S corporation shareholders are now required to include a basis schedule with their tax return when a shareholder receives a distribution, sells stock, recognizes a loss or receives a loan payment. Partnerships are now required to report the beginning and ending tax basis capital for each partner, if either amount is negative.

While these changes were made only to the relevant forms and instructions listed above, it is key to note that forms and instructions may have the same force and effect as an actual Treasury regulation, and thus must be carefully followed. For the 2018 tax year, the IRS and Treasury have provided penalty relief for late filing of partners' negative tax basis capital information. Any negative tax basis capital information for the 2018 tax year must be filed by March 15, 2020, for calendar-year partnerships in order to receive penalty relief for late filing.

These reporting requirements are mandatory and we recommend that pass-through entities consult with their tax advisors immediately, especially in cases where shareholders' or partners' historical tax basis information has not been tracked.

State and local tax considerations

Nexus review

Nexus is most often addressed in the context of analyzing what a company does and determining where the company could arguably have established sufficient contacts to be required to file state income and franchise tax returns. However, the question of where a company has to file only scratches the surface of the importance of determining nexus.

More than ever, businesses should consider whether nexus has been established among all state tax types. State revenue departments are increasingly scrutinizing the in-state activities of remote businesses, especially in the context of economic nexus. For sales tax, the U.S. Supreme Court issued its decision in *South Dakota v. Wayfair*, overturning the long-standing physical presence nexus standard established through *Quill v. North Dakota* in 1992.

With the *Wayfair* decision, the Court has opened up the possibility for states to impose sales and use tax collection and remittance responsibilities on remote sellers based solely upon their economic presence in a state. Almost all of the states imposing a sales and use tax now require out-of-state vendors to collect and remit sales tax provided they meet certain transaction and sales thresholds.

Most states have long taken the position that companies are subject to income and franchise taxes even without maintaining a physical presence in their jurisdictions. But in a post-*Wayfair* era, states have become more focused on activities that produce economic nexus for income and franchise tax purposes. Businesses need to be aware of laws and regulations that can minimize their exposure to taxes such as Public Law 86-272, nonbusiness income allocation, and factor presence standards.

Additionally, it is important to understand whether a company has any opportunities to restructure legal entities or business operations to generate benefits from establishing or eliminating nexus. For example, a company in a loss year with an expectation of generating income in future years may be well-advised to establish nexus now in states it has targeted for expansion in order to protect a NOL. In some cases, this can be as easy as hiring or moving an employee earlier than originally planned; however, regardless of the necessary steps, any nexus-establishing activities must be done by year-end.

Gross receipts taxes review

Through mid-2019, six states have adopted some form of gross receipts taxes (Delaware, Nevada, Ohio, Oregon, Texas and Washington). These taxes are imposed on the gross receipts of a business without regard to profit or loss. In some states, the gross receipts tax is imposed in addition to corporate income and franchise taxes. The tax generally applies to receipts generated from sales within the state. Out-of-state businesses are often unaware that they are incurring gross receipts tax liabilities. In the coming year, a number of states will consider adopting a gross receipts tax. At the local level, cities in California, Washington and many other states, also impose gross receipts taxes and more are considering these taxes every year.

In addition to the increased tax burden, gross receipts taxes often require new reporting and compliance obligations. Businesses should assess whether states in which they are doing business impose a gross receipts tax or are considering imposing such a tax in the coming year.

Market-based sourcing review

By 2019, over two-dozen states have adopted market-based sourcing rules for services, replacing the traditional cost of performance sourcing rules. Market-based sourcing looks to the location of the customer. However, the states take different approaches to determining the market, including considering where the services are delivered, received, and billed. Companies that do not analyze these different approaches often overstate or understate their sales factors.

Apportionment review

State revenue departments are scrutinizing business apportionment methods more closely than ever before. For multistate companies, particularly those with more than one business line, complying with myriad different apportionment rules can be a complex administrative burden. Correctly identifying the required apportionment method and the income subject to apportionment and allocation could save substantial amounts of income and franchise taxes.

Before year-end, it is important to extrapolate estimated apportionment data from the first through third quarters of the current year and the fourth quarter of the prior year to identify key positions for which the company will need specific, highly detailed data for its returns. Additionally, by analyzing this data, the company can determine whether more favorable apportionment can be obtained via restructuring of its legal entity structure or business operations or through requesting to use an alternative apportionment formula.

Attribute maximization review

State attribute regimes, such as state NOL calculation and usage rules, can vary significantly from the federal rules. Companies can take advantage of various planning opportunities to address attributes generated before establishing nexus, becoming a member of a combined or consolidated group and acquiring, merging or liquidating an entity. For example, If a company has substantial tax attributes trapped in a perennially underperforming or newly acquired entity and has another entity that could fully utilize those attributes, it may be beneficial to merge those entities or, in some cases, to elect or request to file on a combined or consolidated basis.

Deduction maximization review

If a company has multiple entities in its structure, it may be beneficial to examine projections of current-year income and deductions to identify isolated current-year loss entities. It may be possible to fully utilize the deductions creating those projected losses through expense allocation, transferring payroll or property, restructuring, or electing or requesting to file on a combined or consolidated basis.

Unitary review

Depending on the circumstances, filing state income tax returns on a mandatory combined basis can provide substantial benefits or detriments to taxpayers. It is important to determine whether the business has the requisite control, integration and flow of value to establish unity and to model state income taxes on a separate and combined basis. Where sufficient value exists, it may be advisable to take steps to break or create unity. This analysis is particularly important if the company has completed, or is going to complete, a major acquisition or disposition of entities or assets during the tax year.

Credits and incentives compliance review

Many state tax credits and incentives programs have regular reporting requirements, often annually, that must be completed to retain benefits and avoid penalties and clawbacks. It is important for a company benefitting from state credits and incentives to understand its continuing compliance responsibilities, ensure that it meets commitments (such as those associated with new hiring, job retention and investment) by agreed-upon deadlines, and file all required forms and data in a timely manner.

By reviewing active state credit and incentive agreements and applicable statutory and regulatory requirements, as well as taking the right steps now to keep in compliance for this year, a company can avoid having to go through the arduous process of renegotiating these agreements or the outright loss of prior, current and future benefits.

State tax reform review

Even though most states have had two legislative sessions to address state tax reform since the passage of the federal tax changes, the full impact of reform on state budgets and tax regimes remains unclear. Both business and personal income taxpayers will need to consider how the federal changes will affect state law. Currently, state conformity must be observed on a state-by-state basis. While some states and localities automatically conform to changes to the Internal Revenue Code for income tax purposes (so-called "rolling conformity" states), many others have fixed-date conformity or only conform to specifically enumerated provisions.

The states are likely to focus on international issues such as GILTI and FDII. However, other areas of tax reform will continue to result in a complex landscape of conformity, including section 163(j). It is important for businesses to be aware of the vast differences among the state approaches to reform and be prepared to address those differences on relatively short notice.

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