PKF O'CONNOR DAVIES
ACCOUNTANTS AND ADVISORS
ESTABLISHED IN 1891

International Tax Insights

December 2018

International Tax Team

Leo Parmegiani, CPA
Partner & Head of International Tax
lparmegiani@pkfod.com | 646.699.2848

Peter D. Baum, CPA
Partner
pbaum@pkfod.com | 914.341.7088

Leonard D. Levin, JD
Partner
llevin@pkfod.com | 914.341.7072

Ralf Ruedenburg
Principal
rruedenburg@pkfod.com | 646.965.7778

David Slemmer
Principal
dslemmer@pkfod.com | 646.965.7781

Tariffs and the Impact on Transfer Pricing Results

By David Slemmer, Principal

Major new tariffs enacted by the United States and any tit-for-tat tariffs enacted by other countries threaten to have an immediate, material impact on the transfer pricing results of multinational companies. Because of a lack of recent experience with strong and escalating trade disputes involving significantly high tariffs, few companies are prepared to deal successfully with the transfer pricing implications.

General Background

A tariff, also referred to as a customs duty, is a tax on a certain class of imported goods. In the U.S., tariffs are levied at the time of import and are paid by the importer of record. The tariff rate varies depending on the product classification, pursuant to the Harmonized Tariff System of the United States and by its country of origin. Companies will typically account for the tariff costs as part of the imported product's cost in its cost of goods sold (COGS).

Impact on Transfer Pricing: Which Related Party Bears the Tariff?

Based on the tariff rules, the importer of record bears initial responsibility for the tariff, and tariff costs would ultimately become part of the COGS of the importer. Unlike anti-dumping rules, no rule prevents the parties from contractually allocating the tariff costs in whole or in part among the parties to the transaction; however, if the parties are related, then the resulting arrangement must be at arm's length.

Effect on Comparability

Depending on the tested party and transfer pricing methodology, tariff treatment could raise comparability issues. For example, if the affiliated U.S. distribution company — the “tested party” for transfer pricing purposes — is exposed to the new tariffs and the comparables are not, some adjustment to the arm's-length range may be appropriate. Such potential adjustments, however, are often difficult to quantify as detailed financial and transactional information on the comparables (e.g., home country of products purchased for resale) is simply not available.

Next Steps for Multinational Companies

The major new tariffs may trigger an immediate, material impact on the transfer pricing results of multinational companies. Many companies may not be prepared to deal effectively with the potentially substantial transfer pricing implications. The solutions to issues created by these tariffs are likely to require both customs and transfer pricing input.

IRS Proposed Regulations: New Interest Limitation Rules and Controlled Foreign Corporations

By Ralf Ruedenburg, Principal

The interest expense limitation rules were modified by the Tax Cuts and Jobs Act (TCJA) in December 2017. On November 26, 2018, the Internal Revenue Service (IRS) released proposed regulations and related guidance.

For multinational companies, it is important to know that the proposed regulations clarify that the changes to the interest expense limitation rules apply to controlled foreign corporations (CFCs) in the same manner they apply to a domestic C corporation. For instance, the new interest limitation rules have to be used when computing subpart F income to be included in the taxable income of the parent company. However, the proposed regulations allude to certain cases where the application of the new interest limitation rules can be modified.

The Treasury Department and the IRS continue to study whether additional modifications to the application should be provided. This could include situations where a CFC is exempt from the application of the new interest limitation rules.

Taxpayers should look out for the publication of the Treasury decision adopting the proposed regulations as final in the Federal Register as the regulations are applicable to tax years ending after the date of the publication. However, taxpayers and their related parties may apply the proposed regulations to tax years ending after December 31, 2017 under certain conditions. Consequently, the proposed regulations would not be retroactive to the date that the TCJA was enacted.

IRS Releases Proposed Foreign Tax Credit Regulations

By Ralf Ruedenburg, Principal

The TCJA made changes to the foreign tax credit rules and related provisions for allocating and apportioning expenses for purposes of determining the foreign tax credit limitation. On November 28, 2018, the IRS issued proposed regulations with guidance on how to determine the foreign tax credit under the new rules. They were published in the Federal Register on December 7, 2018 and comments can be submitted until February 5, 2019.

Among other matters, the following topics are covered by the proposed regulations:

- the allocation and apportionment of deductions,
- adjustments to the foreign tax credit limitation,
- carryover and carryback of unused foreign taxes, and
- the treatment of subsequent reductions in tax.

It has to be noted that there are different applicability dates for portions of the proposed regulations. TCJA related ones apply to tax years beginning after December 22, 2017. Proposed regulations that do not apply to TCJA changes are applicable to tax years ending on or after December 4, 2018. Others have applicability dates dependent on certain circumstances.

Changes to Moving Expense Deduction

By Marco Chang, CPA, Tax Manager

The new Moving Expense Deduction Rules will affect many taxpayers. Prior to the Tax Cuts and Jobs Act (TCJA) of 2017, a taxpayer would generally qualify for moving expense deduction if the new work location meets the distance test from the former home, and the taxpayer works a certain amount of time during the first one or two years in the new location.

However, the TCJA changed the rules. TCJA suspends the Moving Expense Deduction for tax years after December 31, 2017 and before January 1, 2026. One point to note is that if the taxpayer moved in 2017 and the employer reimbursed in 2018, the taxpayer will not be taxed on the reimbursement in 2018.

The only exception set forth by TCJA is for certain members of the Armed Forces. If the taxpayer is a member of the Armed Forces on active duty and the move is because of a permanent change of station, they may qualify for the Moving Expense Deduction.

Companies that plan to send their employees on global assignments may need to take this into consideration when negotiating the assignment package with their employees.

New Voluntary Disclosure Procedures for Post 9-28-2018 Offshore and Domestic Disclosures

By Peter D. Baum, CPA, Partner

On November 29, 2018, the IRS released a memorandum with new procedures for all voluntary disclosures following the end of the Offshore Voluntary Disclosure Program (OVDP) on September 28, 2018. The new Voluntary Disclosure Program (VCP) will now apply to all voluntary disclosures, both domestic and offshore, submitted after September 28, 2018. In addition, the IRS may apply the VCP guidelines to unresolved domestic voluntary disclosures submitted on or before that date.

The new procedures continue to provide taxpayers an ability to come into tax compliance and generally eliminate the risk of criminal prosecution, but there are many changes from the prior OVDP. Some of the changes are logistical changes, such as the timing of submission of the required tax returns and additional documents. Other changes are more substantive including changes to the disclosure period and the penalties imposed.

The VCP covers a six-year disclosure period (shorter than the eight-year OVDP period), but allows a taxpayer to expand the disclosure period if desired. A new feature is that those who cannot reach an agreement on taxes and penalties have the right to appeal the results of the examination with the IRS Office of Appeals. The VCP penalty regime differs from both the OVDP and the longstanding Voluntary Disclosure Program and, although the penalty regime is more uncertain and in most cases potentially more severe than in the OVDP, the IRS makes clear that the VCP is geared toward taxpayers with possible criminal exposure and, for many in that category, that is its primary benefit.

Noncompliant U.S. taxpayers should consult with their tax advisors to calculate their maximum tax, interest, and penalty exposure under the new procedures and determine whether filing a voluntary disclosure is appropriate or other options should be considered.

FinCEN Announces Further Extension of Time for Reporting Signature Authority

By Leo Parmegiani, CPA, Partner

In light of the proposed amendments to the Bank Secrecy Act (BSA) not being finalized, it was recently announced in Notice 2018-1 by the Financial Crimes Enforcement Network (FinCEN) that the filing date for reporting signature authority, Report of Foreign Bank and Financial Accounts (FBAR), is automatically extended to April 15, 2020. This extension applies to the reporting of signature authority held during the 2018 calendar year extended by Notice 2017-1, as well as all reporting deadlines extended by previous related Notices [namely, Notices 2016-1, 2015-1, 2014-1, 2013-1, 2012-1, 2012-2, 2011-1 and 2011-2].

For all other individuals with a FBAR filing obligation, the filing due date remains April 15, 2019.

About PKF O'Connor Davies

PKF O’Connor Davies, LLP is a full-service certified public accounting and advisory firm with a long history of serving clients both domestically and internationally. With roots tracing to 1891, nine offices in New York, New Jersey, Connecticut and Maryland, and more than 700 professionals, the Firm provides a complete range of accounting, auditing, tax and management advisory services.

PKF O’Connor Davies is the lead North American representative in PKF International, a global network of legally independent accounting and advisory firms located in over 400 locations, in 150 countries around the world.

Our Firm provides the information in this e-newsletter for general guidance only, and it does not constitute the provision of legal advice, tax advice, accounting services, or professional consulting of any kind.