External Multistate Tax Alert
January 22, 2018

Multistate Tax Considerations of the Federal Tax Reform International Tax Provisions

Overview

On December 22, 2017, President Trump signed legislation (P.L. 115-97) commonly referred to as "The 2017 Tax Reform Act" ("the Act"), which is the most comprehensive tax reform legislation passed in over thirty years.[1] The Act lowers tax rates on individuals, C corporations, passthrough entities[2] and estates. To offset these costs, a number of deductions, credits and incentives were reduced or eliminated.

The Act's corporate income tax provisions and new deduction for passthrough entities will have broad implications for businesses of all sizes, but many of the far-reaching provisions pertain to the United States ("U.S.") taxation of foreign operations. Certain of these provisions, such as the deemed repatriation tax (commonly referred to as the transition tax), have immediate impacts which must be considered when filing 2017 tax returns. Accordingly, this tax alert highlights some of the most prominent international tax changes created by the Act and the associated multistate tax considerations.

Transition Tax/Deemed Repatriation

The transition tax requires a U.S. shareholder owning at least 10 percent of the vote of a foreign subsidiary (where there is at least one U.S. corporation that is a 10 percent voting shareholder) to add to its subpart F income the shareholder's pro rata share of the foreign subsidiary's net post-1986 historical earnings and profits ("E&P"), as determined as of November 2, 2017, or December 31, 2017, whichever is higher. This income is to be reported as of the foreign subsidiary's last tax year beginning before 2018, and is taxed at one of two rates: (1) 15.5 percent for E&P held as cash or cash equivalents; and (2) 8 percent for all other E&P.

The deemed repatriation raises a number of significant state issues, including whether and how the respective states tax subpart F income. The concept behind the deemed repatriation is that once the federal tax is paid on the deemed repatriation, the actual repatriation of these amounts will be tax-free at the federal level. One key issue for companies to consider is, to the extent a particular state does not tax the deemed repatriation, whether such a state will attempt to tax the funds upon their actual repatriation. Another issue for companies to consider is whether the company has already paid tax on any of this E&P (i.e., by filing a worldwide state income tax return) and, if so, whether a position may exist to exclude the deemed repatriated dividends from income. Another consideration is to what degree the computation of gross income inclusion may differ from the federal computation taking into account combined group composition and/or separate filings.

Further, the potential state tax treatment of this deemed repatriation varies. Some states have a fairly straightforward approach for taxing or exempting the addition to subpart F income. For example, a rolling (automatic) conformity state may conform to the amended IRC Section 965 immediately upon enactment, whereas states which have a static or lagging conformity approach to the IRC may not explicitly conform to section 965, leaving out the addition, or at a minimum, leaving the conclusion in question. Therefore, state conformity to the IRC – or a lack thereof - can result in varying treatment among the states. As a result, it is important for taxpayers to closely monitor a state's conformity status.[3]

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[1] The Tax Reform Act's official name is, "An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018."
[2] The Act effectively reduces the tax burden paid by the owners of passthrough entities (e.g., partnerships, S corporations, etc.) by a) creating a new 20% deduction for "qualified business income" and b) reducing the rates imposed on individuals and C corporations.
[3] A summary of each state's conformity to the IRC as of January 1, 2018 is attached to this Alert as Appendix A.

Other Considerations

The Act also provides that U.S. shareholders of controlled foreign corporations must include in gross income the amount of its global intangible low-taxed income ("GILTI"), but is permitted a deduction equal to 50 percent of the GILTI. U.S. corporations will also be required to include foreign-derived intangible income ("FDII") in gross income, but will then be permitted a deduction on the FDII. As such, each state's tax regime must be examined to determine if the GILTI or FDII (and the related deduction) is included in the state taxable income calculation.

For example, the New York Department of Taxation and Finance recently presented to New York Governor Andrew Cuomo a "Preliminary Report on the Federal Tax Cuts and Jobs Act" (the "Report"), in which it attempted to estimate the impact the Act would have on the tax system and economy of the State of New York.[4] When analyzing the Act's international tax provisions, the Report notes that Subpart F income and dividends paid by foreign affiliates to U.S. corporations are "generally not taxed in New York." With regard to GILTI income, however, the Report states:

> Although this new GILTI income is treated similarly to Subpart F income, it is specifically not characterized as Subpart F income under the IRC and therefore would not qualify as other exempt income. Thus, the income would flow through to New York, be treated as business income, and be subject to tax.[5]

With New York weighing in, it is anticipated other state agencies may follow suit soon.

Taxpayers will also need to consider whether the foreign income under the transition tax, GILTI or FDII will be included in the sales factor numerator and/or denominator for apportionment purposes. If the foreign income is treated as a dividend, states may exclude the dividends altogether from the sales factor or only include a portion of the dividend.

Finally, because the Act allows for the repatriation of funds under beneficial terms, it is anticipated that a portion of those funds may be reinvested in the U.S. economy. This is especially true as the Act modifies the IRC section 168 bonus depreciation rules to allow for full expensing of qualified property placed into service after September 27, 2017 and before January 1, 2023. Accordingly, companies who anticipate repatriating and reinvesting a substantial amount of E&P following the deemed repatriation should consider state and local credits and incentives opportunities for such reinvestment.

State Budgets and Legislative Responses

The Act represents "deficit spending" by the federal government and includes roughly $1.46 trillion in unoffset costs for the 10-year federal budget window covering 2018-2027 according to the Joint Committee on Taxation. State governments, however, cannot engage in deficit spending and generally must run balanced budgets. Each state that imposes income taxes will therefore need to evaluate which provisions of federal tax reform that pertain to the calculation of taxable income to determine if the state can afford to conform to any federal tax provision that would reduce state revenues (or, conversely, if they can afford to disconnect from any revenue-raising provisions included in the Act.)

State conformity to the IRC is generally set by statute, and a summary of each state's current conformity to the IRC as of January 1, 2018, is attached to this Alert as Appendix A.

States typically address conformity to the IRC through legislation, although certain states may seek to address essential details through administrative guidance as well. Legislative responses are expected throughout 2018, depending upon when each state is in session. Included below is a summary of each state's 2018 legislative calendar (based on information currently available).

Jurisdiction	State Legislative Calendar
Alabama	January 9, 2018 - April 24, 2018
Alaska	January 16, 2018 - May 16, 2018 (Alaska Constitution limits regular legislative sessions to 121 consecutive days; may be extended).

[4] *Preliminary Report on the Federal Tax Cuts and Jobs Act*, January 2018). A copy of the Report is available here.
[5] *Preliminary Report* at p. 30.

Arizona	January 8, 2018 - April 17, 2018
Arkansas	February 12, 2018 - Will last for 30 days, with the possibility of three- fifteen day extensions
California	January 3, 2018 - August 31, 2018
Colorado	January 10, 2018 - May 9, 2018
Connecticut	February 7, 2018 - May 9, 2018 (dates for regular sessions in even-numbered years set by Connecticut Constitution; session may adjourn prior to final date)
Delaware	January 9, 2018 - June 30, 2018
District of Columbia	January 2, 2018 – December, 2018 (generally in session year-round)
Florida	January 9, 2018 - March 9, 2018
Georgia	January 8, 2018 - (no more than 40 working days)
Hawaii	January 17, 2018 - May 3, 2018
Idaho	January 8, 2018 - March 27, 2018
Illinois	January 23, 2018 (House) and January 30, 2018 (Senate) - May 31, 2018 (both House and Senate)
Indiana	January 3, 2018 - March 14, 2018
Iowa	January 8, 2018 - April 17, 2018
Kansas	January 8, 2018 - April 6, 2018
Kentucky	January - Late March
Louisiana	March 12, 2018 - adjourn no later than June 4, 2018
Maine	January 3, 2018 - April 18, 2018 (may be extended)
Maryland	January 10, 2018 - April 9, 2018
Massachusetts	January 10, 2018 - June 30, 2018 (may be extended into July)
Michigan	Current session runs through December 2018
Minnesota	February 20, 2018 - May 21, 2018
Mississippi	January - Late March
Missouri	January 3, 2018 - May 18, 2018
Montana	Montana holds legislative sessions on odd-numbered years so there is not a regular session scheduled for 2018. There is a possibility that the governor could call a special session this year to address the changes.
Nebraska	January 3, 2018 - April 18, 2018
Nevada	Legislative regular sessions held biennially in odd-numbered years. Special sessions may be called.
New Hampshire	January 3, 2018 - June 30, 2018
New Jersey	No fixed legislative period - generally in session
New Mexico	January 16, 2018 - February 15, 2018
New York	January 2018 – June 20, 2018

North Carolina	January 10, 2018 - (approximately) June 30, 2018
North Dakota	The next regular session will be from January 3, 2019 - April 26, 2019
Ohio	The legislative schedule is set in six-month increments. The last currently scheduled session for the first half of 2018 is June 27, 2018.
Oklahoma	February 5, 2018 – May 25, 2018, but is currently in a special session
Oregon	February 5, 2018 - March 11, 2018 (date of adjournment sent by Oregon Constitution but may be extended by Legislature)
Pennsylvania	January 22, 2018 - June 29, 2018 (Senate) and June 30, 2018 (House)
Rhode Island	January 2, 2018 - mid-July, 2018 (estimated)
South Carolina	January 9, 2018 - no later than May 10, 2018
South Dakota	January 9, 2018 - March 26, 2018
Tennessee	January 9, 2018 - Late April/Early May
Texas	The next regular session will begin on January 8, 2019
Utah	January 22, 2018 - March 8, 2018
Vermont	January 3, 2018 - May 4, 2018
Virginia	January 10, 2018 - March 10, 2018, with reconvened session to commence on April 18, 2018
Washington	January 8, 2018 – March 8, 2018
West Virginia	January 10, 2018 – March 10, 2018
Wisconsin	January 16, 2018 – March 22, 2018
Wyoming	February 12, 2018 – March 10, 2018

Taxpayer Considerations

While the foregoing is not an exhaustive list of all state tax issues raised by the Act’s international income tax provisions, the summary is intended to provide an overview of the range of state and local tax issues presented. Each taxpayer is encouraged to consider these state and local issues, including the ASC740 implications, when evaluating the impact of the Act on current and prospective tax planning.

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APPENDIX A

State tax conformity to IRC—as of January 1, 2018

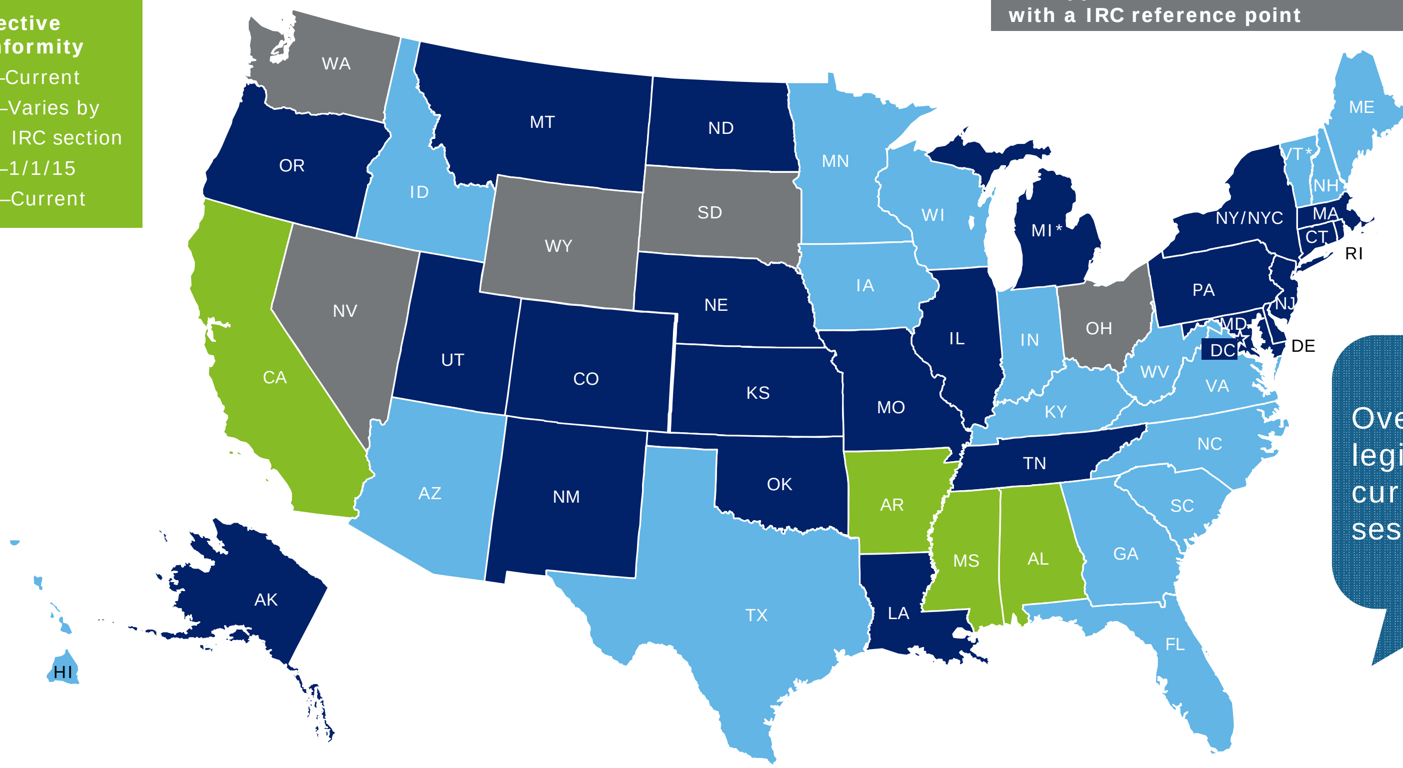
- **Rolling conformity to IRC currently in effect**
- **Conforms to IRC as of a specific date (as noted for each affected state)**
- **Selectively conforms (as noted for each affected state to 'IRC currently in effect', or to 'IRC as of a specific date.')**
- **Not applicable b/c state does not levy an entity level tax with a IRC reference point**

Specific Date Conformity

AZ—1/1/17
FL—1/1/17
GA—1/1/17
HI—12/31/16
ID—1/1/17
IN—1/1/16
IA—1/1/15
KY—12/31/15
ME—12/31/16
MI*—Current or 1/1/12
MN—12/16/16
NH—12/31/16
NC—1/1/17
SC—12/31/16
TX—1/1/07
VT*—IRC in effect for 2016 TY
VA—12/31/16
WV—12/31/16
WI—12/31/16

Selective Conformity

AL—Current
AR—Varies by IRC section
CA—1/1/15
MS—Current



Over 35 state legislatures currently in session

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