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January 8, 2018

VIA E-mail (smcosper@fasb.org)
Susan M. Cosper
Technical Director and Chairman of the Emerging Issues Task Force
Financial Accounting Standards Board
401 Merritt 7
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RE: Request for Interpretation of Accounting Standards Codification 740 – Income Taxes Relating to U.S. Tax Reform

Dear Ms. Cosper:

Tax reform legislation enacted on December 22, 2017, formerly known as the Tax Cuts and Jobs Act (the Act),[1] significantly alters the U.S. international tax system and, in doing so, raises a number of significant financial statement disclosure issues that must be addressed in a very compressed timeframe. Tax Executives Institute, Inc. (TEI or the Institute) is providing our members' views on how the disclosure requirements under Accounting Standards Codification, Topic Number 740 – Income Taxes ("ASC 740") should be applied to two new regimes that will have widespread impact on U.S. business taxpayers with significant foreign operations, the "Base Erosion Anti-Abuse Tax," provided under new section 59A (the BEAT), and the "Global Intangible Low-Taxed Income" (GILTI) regime, provided under new section 951A.[2]

We understand the FASB recently met with representatives of the "Big 4" accounting firms to discuss issues arising from the Act, including the BEAT and the GILTI regime. To date, three of the Big 4 firms have published commentary expressing their respective views on how the financial impacts of the BEAT and the GILTI regime should be disclosed in financial

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[1] The Act was subsequently renamed, An Act to Provide for Reconciliation Pursuant to Titles II and V of the Concurrent Resolution on the Budget for Fiscal Year 2018, Pub. Law No. 115-97, 131 Stat. ____.
[2] Unless otherwise noted, all references to "section" are to the Internal Revenue Code of 1986, as amended (the Code).

statements. The tax and accounting issues at play are complex, and the Big 4 views diverge. We appreciate this opportunity to provide the views of our membership, which is comprised solely of in-house tax and tax accounting professionals who will be charged with evaluating the financial impacts of the Act and preparing associated financial statement disclosures, especially given the divergent views expressed by the Big 4.

TEI Background

TEI is the preeminent association of in-house tax professionals worldwide. Our approximately 7,000 members represent more than 2,800 of the leading corporations in North and South America, Europe, and Asia. TEI represents a cross-section of the business community and is dedicated to developing and effectively implementing sound tax policy, promoting the uniform and equitable enforcement of the tax laws, and reducing the cost and burden of tax administration and compliance to the benefit of taxpayers and governments alike. TEI is firmly committed to maintaining a tax system that works—one that is administrable and with which taxpayers can comply in a cost-efficient and predictable manner.

TEI, as a professional association of in-house tax executives, offers a unique perspective. Members of TEI manage the tax affairs of their companies and must contend daily with provisions of the tax law impacting business enterprises, including the financial accounting for income taxes. Our members work for companies involved in a wide variety of industries. Their collective perspectives are broad-based and not tied to any particular special interest group. The background, diversity, and professional training of TEI's members place the organization in a unique position to comment on the application of ASC 740 to the new BEAT and GILTI regimes.

I. Overview of Requested Guidance

A. The BEAT

The BEAT is a new corporate minimum tax intended to address the base erosion problem posed by outbound, deductible payments made to foreign affiliates—*i.e.*, the mismatch created by reductions to U.S. taxable income via outbound, related-party payments and the recognition (or nonrecognition) of foreign income attributable to those payments that is never subject to U.S. tax. The new regime starts with a taxpayer's "regular" taxable income, adds back deductions taken for targeted base eroding payments, and applies a prescribed tax rate that varies by year to the alternative tax base.[3] The BEAT liability is the excess of the alternative tax over the taxpayer's regular tax liability less certain tax credits. We believe the BEAT is analogous to the now repealed corporate Alternative Minimum Tax (AMT), and we urge the FASB to issue

[3] For base erosion payments paid or accrued in taxable years beginning after December 31, 2017, for one year, the BEAT rate is 5 percent. That rate increases to 10 percent for taxable years beginning after December 31, 2018, and then to 12.5 percent for taxable years beginning after December 31, 2025. These rate changes further complicate matters discussed herein. For simplicity, we will assume the BEAT rate is 10 percent.

guidance adopting disclosure rules for the BEAT that are similar to those applicable to the AMT—specifically, guidance treating taxes owed under section 59A as permanent tax expense adjustments in the year incurred (referred to herein as the AMT Approach). To date, one Big 4 firm has published commentary aligning with this view.

Two Big 4 firms have published commentary expressing a different view. Those firms contend the BEAT should be accounted for as a parallel tax system, requiring entities to forecast whether they will be subject to the BEAT and, if so, to value deferred tax assets and liabilities according to the applicable statutory rate of section 59A instead of the new U.S. corporate income tax rate of 21 percent. This position is largely based on a belief that the BEAT is comparable to the Mexican *Impuesto Empresarial a Tasa Unica* regime (IETU) and should be disclosed in a manner similar to the method these accountings firms adopted for the IETU in 2008 (referred to herein as the IETU Approach). We respectfully disagree with the fundamental notion that the BEAT is comparable to the IETU, as well as the merits of applying the IETU Approach to the BEAT.

Below, in Part II of this letter, we provide insights into the significant financial statement risks, volatility, and investor confusion that would result if the BEAT is treated as a parallel tax system and reported using the IETU Approach. Indeed, the FASB identified many of these same adverse consequences as a basis for adopting the reporting method for the now repealed AMT. The AMT Approach would provide investors with accurate and intuitive disclosures and eliminate the balance sheet volatility and financial statement risk associated with the proposed IETU Approach.

B. The GILTI Regime

Under new section 951A, a U.S. shareholder of any controlled foreign corporation (CFC) must include in gross income for a taxable year its GILTI in a manner generally similar to inclusions of Subpart F income. The GILTI inclusion is a new anti-base erosion measure aimed at foreign income subject to low effective tax rates. The regime generally ensures a global minimum effective tax rate on GILTI in the range of 10.5 to 13.125 percent through the imposition of a residual U.S. tax.

Like Subpart F, the GILTI regime presents significant ASC 740 complications. We believe these complexities warrant a flexible reporting approach that acknowledges certain facts and circumstances may warrant recording GILTI deferred taxes, but other facts and circumstances that may not. Accordingly, we urge the FASB to adopt a method for disclosing the financial impacts of the GILTI regime that is similar to current guidance on Subpart F, which does not provide a single prescribed accounting standard. The method should provide preparers sufficient ability to make judgments on their GILTI tax accounting based on individual facts and circumstances. We believe this position aligns with the views expressed in Big 4 commentary published to date.

II. Application of ASC 740 to the BEAT

A. Mechanics of the BEAT

Section 14401 of the Act provides for a new "Base Erosion Anti-Abuse Tax" (or BEAT) through enactment of new section 59A entitled, "Tax on Base Erosion Payments of Taxpayers with Substantial Gross Receipts." The BEAT requires a qualifying corporation to pay a base erosion minimum tax amount (BEMTA) in addition to its regular tax liability (after reduction for certain credits such as foreign tax credits). The BEMTA is equal to the excess of the applicable tax rate (5 percent in 2018, 10 percent starting in 2019, and 12.5 percent starting in 2025) multiplied by the corporation's modified taxable income over its regular tax liability. "Modified taxable income" is a corporation's taxable income increased by its "base erosion tax benefits."[4] Calculating the "regular tax liability" requires a taxpayer to add back certain credits allowable in computing the taxpayer's regular tax liability. BEMTA is zero if 10 percent (or other applicable percentage) of the taxpayer's modified taxable income is less than its regular tax liability reduced by applicable credits.

A "base erosion payment" (BEP) generally includes any amount paid or accrued by a taxpayer to a related foreign person and with respect to which a deduction is allowable, including amounts paid or accrued for acquisitions of depreciable property.[5] The base erosion tax benefit means any current-year deduction allowed in arriving at taxable income for (i) a BEP and (ii) any amortization or depreciation arising from a BEP.[6]

Economically, when a BEAT liability is owed, it always results in a higher tax burden than a taxpayer's regular tax liability at a 21 percent rate. For example, a taxpayer with $100 of taxable income (assuming no section 38 credits) and $200 of BEPs would have base erosion modified taxable income of $300 ($100 TI + $200 BEPs). The additional BEMTA would be $30 ($300 BEMTA x 10% rate) less $21 (regular taxable income of $100 x 21% tax rate) or $9, resulting in a $30 tax liability absent credits. This yields an economic tax rate burden of 30 percent, considering $30 of income tax in relation to $100 of taxable income, which is well above the corporate statutory rate of 21 percent (despite the headline 10 percent BEAT rate). In fact, the

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[4] The statute requires taxpayers to calculate modified taxable income by "disregarding" base erosion tax benefits. Modified taxable income would also not include any "base erosion percentage" of any net operating loss deduction allowed for the year.

[5] A BEP also includes any amount that constitutes a reduction in gross receipts of the taxpayer that is paid to or accrued by the taxpayer with respect to: (1) a surrogate foreign corporation which is a related party of the taxpayer, and (2) a foreign person that is a member of the same expanded affiliated group as the surrogate foreign corporation. A surrogate foreign corporation has the meaning given in section 7874(a)(2).

[6] Base erosion tax benefits also include any reduction in gross receipts described in the immediately preceding footnote. In addition, base erosion tax benefits exclude any BEPs that are subject to withholding tax and have had withholding tax withheld. The exclusion is reduced, proportionately, to the extent the rate of withholding tax was reduced pursuant to an income tax treaty with a foreign country.

minimum BEAT burden, if it applies, is necessarily always higher than a 21 percent tax rate on income because the BEAT is always in addition to "regular" tax at a 21 percent rate.

The BEAT can apply even where a taxpayer has a taxable loss for the year, but not if the loss is sufficiently large. To illustrate, if the taxpayer in the above example had a loss of ($50), its BEMTA would be $15. If the corporation's loss were ($250), however, there would be no modified taxable income (*i.e.*, ($250) + $200 = ($50)) and hence no BEMTA.[7] Therefore, the BEAT operates very much like the historic AMT calculation, where various addbacks are made and tax liability is calculated at a lower rate. Unlike AMT, however, if a corporation is required to pay a BEMTA in any given tax year, no credit is allowed in a subsequent year for such BEMTA payment.

B. Application of ASC 740 to the BEAT

1. Big 4 Commentary

The BEAT introduces a new level of complexity in the traditional application of ASC 740. ASC 740-10-30-8 establishes that deferred tax liabilities or assets should be measured using the enacted tax rate(s) expected to apply to taxable income in the periods in which the deferred tax liability or asset is expected to be settled or realized.[8] ASC 740-10-30-10 further clarifies, the applicable tax rate in the U.S. federal tax jurisdiction is the regular tax rate, and a deferred tax asset is recognized for alternative minimum tax credit carryforwards in accordance with the provisions of paragraph 740-10-30-5(d) through (e).

Each of the "Big 4" public accounting firms has published commentary reflecting their respective views of the proper ASC 740 treatment of the BEAT. KPMG's commentary provides as follows: [9]

> **Question C.60**: How is the accounting for the BEAT different from the accounting for AMT?
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> **Answer**: For operations subject to tax in the United States, ASC 740 requires all companies to measure deferred taxes for temporary differences using regular tax rates regardless of whether the company expects to be a perpetual AMT taxpayer. This requirement was based

[7] Mathematically, the BEAT is owed only where BEPs exceed either taxable income or taxable loss (expressed as a positive number). Put another way, if the ratio of BEPs to taxable income (expressed as a positive number) exceeds 1, BEAT will be due (ignoring foreign tax credit add-backs to tax liability).
[8] Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes, para. 18 (Financial Accounting Standards Board, Feb. 1992).
[9] KPMG, Tax Reform Enacted in 2017; SEC Staff Provides Relief to Registrants, DEFINING ISSUES, No. 17-31, 6 (Dec. 23, 2017) (the KPMG Commentary).

> primarily on the fact that AMT credit carryforwards (*i.e.*, the amount of tax paid under the AMT system in excess of the amount payable under the regular tax system) could be used to offset future taxes paid under the regular tax system and those carryforwards were available indefinitely. As a result, a company could expect to be subject to regular income tax rather than AMT over the course of its life.
>
> Unlike the legacy AMT system, amounts paid under the BEAT in excess of the tax that would otherwise be payable under the regular income tax system are not permitted to be carried forward to offset future taxes payable under the regular income tax system. Accordingly, we currently believe the BEAT tax and the regular tax system should be considered two separate income tax systems, which would require a company to determine which system will apply when its basis differences are expected to reverse. However, this question is not resolved. We will update our guidance as necessary in response to future developments. (Emphasis added.)

PwC's commentary aligns with KPMG's, stating, in part, "[b]ecause it effectively operates as a parallel but separate income tax system, we believe that companies should, for purposes of both current and deferred income tax accounting under ASC 740, determine whether they expect to be subject to regular income tax in all periods, the BEAT in all periods, or a combination of the two, depending on the tax year in question (emphasis added)."[10]

Deloitte's commentary differs materially from that offered by KPMG and PwC, stating as follows:[11]

> 6.1 What tax rate should companies that are subject to the BEAT provisions use when measuring temporary differences?
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> We believe that the BEAT system can be analogized to an alternative minimum tax (AMT) system. ASC 740 notes that when alternate tax systems like the AMT exist, deferred taxes should still be measured at the regular tax rate. Because the BEAT provisions are designed to be an "incremental tax," an entity can never pay less than its statutory tax rate of 21 percent. Like AMT preference items, related-party payments made in the year of the BEMTA are generally the BEMTA's driving factor. The AMT system and the BEAT system were both designed to limit the tax benefit of such "preference items." Further, as was the case under the

[10] PwC, Accounting Considerations of U.S. Tax Reform, IN-DEPTH, No. US2017-34, 11 (Dec. 22, 2017) (the PwC Commentary).
[11] Deloitte, Frequently Asked Questions about Tax Reform, Financial Reporting Alert, 18-1 (Jan. 3, 2018) (the Deloitte Commentary).

> AMT system, an entity may not know whether it will always be subject to the BEAT, and we believe that most (if not all) taxpayers will ultimately take measures to reduce their BEMTA exposure and therefore ultimately pay taxes at or as close to the regular rate as possible. Accordingly, while there is no credit under the Act such as the one that existed under the AMT regime, we believe that the similarities between the two systems are sufficient to allow BEAT taxpayers to apply the existing AMT guidance in ASC 740 and measure deferred taxes at the 21 percent statutory tax rate. (*See* ASC 740-10-30-8 through 30-12 and ASC 740-10-55-31 through 55-33.) However, we are aware that views on this topic are diverse; thus, practitioners should stay tuned for developments.

EY has not offered a definitive public view on the treatment of deferred taxes for the BEAT. Its commentary, however, differs from that offered by KPMG and PwC, stating, "[t]he income subject to tax under the bill's BEAT provisions should generally be treated in a manner similar to Subpart F income (*i.e.*, it should be included in the US parent's taxable income in the current year) and included in its US income tax provision) (emphasis added)."[12] The reference to Subpart F could be read to suggest that EY views the BEAT not as a separate tax system, but rather as an integrated addition to regular tax. The commentary, however, is preliminary.

2. TEI Analysis of the IETU Approach

KPMG's commentary on the BEAT mirrors the firm's commentary on the Mexican IETU flat tax, which was enacted in 2008 and remained in-force until 2013. The IETU was an alternative tax regime, which replaced a prior "asset tax" regime. Taxpayers were liable for the higher of their IETU or "regular" tax. At that time, KPMG concluded the IETU should not be treated like the AMT, largely because it lacked a credit against future "regular" taxes for additional IETU taxes paid.[13]

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[12] EY, Accounting for the Effects of the Tax Cuts and Jobs Act, Technical Line, 7 (Dec. 18, 2017) (the EY Commentary).

[13] KPMG Accounting for Income Taxes (Mar. 2017), Section 9.179[-9.180]:

> For operations subject to tax in the United States, ASC Topic 740 requires that all entities measure deferred taxes for temporary differences using regular tax rates regardless of whether the entity expects to be a perpetual AMT taxpayer. This conclusion, in large part, is based on the fact that AMT credit carryforwards (*i.e.*, the amount of tax paid under the AMT system in excess of the amount payable under the regular tax system) may be used to offset future taxes paid under the regular tax system and those carryforwards are available indefinitely. As a result an entity can expect to be subject to regular income tax rather than AMT over the course of its life. Unlike the AMT system in the United States, amounts paid under the IETU in excess of the tax that would otherwise be payable under the regular income tax system are not permitted to be carried forward to offset future taxes payable under the regular income tax system. Accordingly, Mexico's regular income tax and the IETU should be considered two separate systems resulting in the need for entities to determine

KPMG's commentary on the BEAT appears to turn on whether it should be considered similar to the U.S. AMT—and hence deferred taxes should not be re-measured (to the equivalent of an AMT rate)—or whether the BEAT should be treated like the IETU. Characterization of the BEAT as a "separate" or "parallel" taxing system appears to be significant to the views KPMG and PwC have asserted regarding the proper ASC 740 treatment of the BEAT.

To test the reasoning that the BEAT is akin to a parallel taxing system, more similar to the Mexican IETU than the repealed AMT, TEI compared technical details of the BEAT against the IETU and AMT. This comparison, which is provided in the attached Appendix, demonstrates the Mexican IETU and the BEAT have critical differences, and we submit the BEAT is, in fact, more akin to the AMT than the IETU. Accordingly, we reject the notion that the FASB should be concerned about adopting a different disclosure method for the BEAT than the method accounting firms applied to the Mexican IETU.

The better analysis is that the BEAT is an integrated part of the new U.S. international tax system with functionality (and difficulties) similar to the AMT. This view is shared by Deloitte, whose commentary states:[14]

> Like AMT preference items, related-party payments made in the year of the BEMTA are generally the BEMTA's driving factor. The AMT system and the BEAT system were both designed to limit the tax benefit of such "preference items."

3. Adverse Consequences of Adopting the IETU Approach

As discussed in detail below, adoption of the IETU Approach would result in significant financial statement volatility, counter-intuitive financial statement results, and the risk of misleading users of financial statements. Further, unlike disclosures for impacts of the IETU, which was limited to companies with Mexican operations, financial statements bearing these risks would be widespread, as BEAT disclosures will not be limited to companies operating in a particular country or to any particular industry and will likely impact industries as far reaching as technology to manufacturing to financial services.

The FASB, in its original observations of the now repealed AMT, recognized risks similar to those that would be experienced when attempting to apply the IETU Approach to the BEAT. FAS 109, Paragraphs 90 and 91, are quoted in full below, as the description of risk mirrors what TEI believes to be the issues with the BEAT today:

> A few respondents to the Exposure Draft suggested measurement of deferred taxes using the lower alternative minimum tax (AMT) rate if an

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which system will apply in each future year that temporary differences under the two tax systems are expected to reverse in order to measure deferred taxes.

[14] *See* Deloitte Commentary.

> enterprise currently is an AMT taxpayer and expects to "always" be an AMT taxpayer. The Board believes that no one can predict whether an entity will always be an AMT taxpayer. Furthermore, it would be counterintuitive if the addition of AMT provisions to the tax law were to have the effect of reducing the amount of an enterprise's income tax expense for financial reporting, given that the provisions of AMT may be either neutral or adverse but never beneficial to an enterprise (emphasis added). It also would be counterintuitive to assume that an enterprise would permit its AMT credit carryforward to expire unused at the end of the life of the enterprise, which would have to occur if that enterprise was "always" an AMT taxpayer. The Board concluded that all enterprises should measure deferred taxes for temporary differences using regular tax rates and assess the need for a valuation allowance for an AMT credit carryforward deferred tax asset using the guidance in this Statement. Otherwise, an enterprise's deferred tax liability could be understated for either of two reasons:
>
> a. It could be understated if the enterprise currently is an AMT taxpayer because of temporary differences. Temporary differences reverse and, over the entire life of the enterprise, cumulative income will be taxed at regular tax rates.
>
> b. It could be understated if the enterprise currently is an AMT taxpayer because of preference items but does not have enough AMT credit carryforward to reduce its deferred tax liability from the amount of regular tax on regular tax temporary differences to the amount of tentative minimum tax on AMT temporary differences. In those circumstances, measurement of the deferred tax liability using AMT rates would anticipate the tax benefit of future special deductions, such as statutory depletion, which have not yet been earned.[15]

FAS 109, paragraph 90, does not base its conclusion regarding AMT on the credibility of the AMT. Instead, the guidance first states: "No one can predict whether an enterprise will always be an AMT taxpayer." Indeed, TEI believes this prediction not only is ***more*** difficult for the BEAT than for the AMT, but also relies on facts and circumstances outside of the taxpayer's control and thus not subject to reliable forecasting. Under the IETU Approach, predicting whether an entity would be a BEAT taxpayer required to measure deferred taxes would require entities to schedule out the years in which their deferred tax assets would turn and make judgments of application of the BEAT in those years. Deferred schedules could reach ten to twenty or even thirty-nine years (*i.e.*, the longest depreciation period for non-residential

[15] FAS 109, para. 91.

property). Attempts to forecast taxable income for BEAT would require predictability for a number of factors well beyond the control of the reporting entity, including long-term stock price changes; predictions of related-party transfer pricing; forecasts of not only customer revenue, but also customer location and behavior; capital gains; FX gains/losses; other equity-based forecasting not subject to controls; as well as other amounts not generally subject to prediction or control.

For instance, guidance issued by the FASB in the context of Accounting Standards Update (ASU) 2016-09 to ASC 718, which governs the accounting for stock-based compensation (SBC), specifically instructs companies not to forecast the tax benefits and deficiencies related to excess SBC and to report such amounts as discrete items in the reporting period in which they occur. This guidance also explicitly provides that entities should not forecast excess tax benefits and deficiencies related to SBC in determining the annual estimated effective tax rate.[16] Yet, adoption of the IETU Approach for BEAT would require entities to forecast SBC to anticipate tax benefits and deficiencies. SBC forecasting requires forecasting the valuation, in many cases, of public securities. This proposed treatment does not align with current accounting standards and would be unreliable if attempted (as demonstrated by the position the FASB took in ASU 2016-09).

SBC forecasting is not the only significant hurdle that would be encountered applying the IETU Approach to the BEAT. Accurate BEAT forecasting could require 5-10 (or more) years of forecasts not only of taxable income (including ***all*** timing differences which, in turn, would require forecasting income statements and balance sheets for every entity), but also of intercompany BEPs, expected "Foreign Derived Intangible Income" (FDII), and GILTI.

FDII and GILTI are two new regimes introduced under the Act.[17] Both FDII and GILTI tax foreign-derived and CFC income, respectively, at a rate lower than 21 percent, after accounting for a hurdle of a 10 percent return on tangible assets. Each regime achieves the reduced rate by providing for a tax deduction equal to a percentage of the FDII and GILTI income. Accordingly, taxable income could only be measured after estimating both the FDII and GILTI deductions. Commentary published by KPMG and Deloitte concerning the FDII and GILTI deductions reasons they are "special deductions" and, as stated in the KPMG commentary, "[s]pecial deductions are recognized no earlier than the year in which the deduction is available to be included on the tax return and, therefore, generally are not considered in the tax rate when measuring deferred taxes."[18] Under the IETU Approach, it is not clear how to reconcile the conflicting views that the FDII and GILTI deductions should not be accounted for when measuring deferred taxes, yet would be required to measure deferred taxes with respect to the BEAT.

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[16] Accounting Standards Update No. 2016-09, Compensation – Stock Compensation (Topic 718), Issue 1 (Financial Accounting Standards Board, Mar. 2016).
[17] *See* sections 250, 951A.
[18] *See* KPMG Commentary and Deloitte Commentary.

Regardless, FDII presents a particular challenge because it requires forecasting the amount of sales or services provided by a U.S. person to a foreign party for ***each*** unrelated-party and related- party revenue stream, as well as the allocation of expenses to such amounts. TEI is not aware of any large reporting entities capable of forecasting to this level of customer granularity, in part because an enterprise cannot control customer purchasing locations and behavior, particularly in technology sectors, and certainly not on a 5-10 year basis. Reliable forecasting in this context would also require entities to forecast the directionality to a precise level of their outsourcing vs. insourcing of activities, such as shared services, research and development, manufacturing, quality control services, and beyond. TEI does not believe preparers of financial statements could perform such forecasting with the precision and reliability necessary for financial statement disclosures. Certifying the accuracy of these forecasts and demonstrating internal controls to auditors would be nearly impossible because the forecasted data would be uncontrollable and unknown to financial planners.

Entities are required, at times, to make long-term forecasts to measure valuation allowances under ASC 740-10-30-16–25. Valuation allowance guidance, however, has clarified that pre-tax book income forecasts are sufficient for this purpose and generally require a three-year cumulative tally. Accounting firms have expressed varying views on the level of permanent difference forecasting required. Nevertheless, in all cases, the forecasting exercise is at a far less granular legal entity and customer level than would be required for application of the IETU Approach to the BEAT. The forecasting that would be required under the IETU Approach is similar to what would have been required to forecast the financial impacts of the AMT had the AMT been subject to a similar method. The FASB appropriately rejected such a method for the AMT and should do the same for the BEAT.

As noted above, failure to accurately predict the amounts of BEPs (*i.e.,* in-sourcing vs. out-sourcing relative to op-ex growth), FDII or GILTI under the IETU Approach could result in inaccurate predictions of whether an entity would, in the future, be subject to the BEAT. Adjustments of the forecasts would then result in a re-measurement of deferred tax assets/liabilities and cause significant balance sheet and income statement volatility. This level of forecasting would be required at each balance sheet date (*e.g.,* quarterly) to appropriately report tax expense pursuant to ASC 740-270.

The lack of reliable forecasts was acknowledged in FAS 109, Paragraph 90, as a basis for not using the AMT as an enacted rate. In addition, FAS 109 states that it would be "counter-intuitive" to account for deferred taxes at a lower statutory rate when a taxpayer in the AMT is always economically worse off than under the regular tax.[19] This is exactly the case for the BEAT as well. A taxpayer will never owe less taxes under application of the BEAT than it would absent application of the BEAT. In fact, the BEAT may cause some taxpayers with low "regular" income and high BEPs to rise well above the former 35 percent statutory rate when

[19] *See* FAS 109, Para. 90, quoted on page 9, above.

measured on an economic basis (*i.e.*, taxes paid/regular taxable income).[20] The inability to perform reliable forecasting would add volatility to balance sheets because, inevitably, forecasts would change. Investors would then see repeated counter-intuitive results as entities with large deferred tax liabilities move from "regular" tax forecasts to BEAT forecasts. The mark-down of liabilities would show investors profits in the quarter of re-measurement, yet the entity would be economically worse off if it expected to pay the BEAT long-term. Conversely, entities forecasting a movement from BEAT to regular tax would show investors a loss from the re-measurement of the liabilities, while expecting lower economic costs long-term. Neither result would provide investors with an accurate measure of the entity's future expected tax costs.[21]

These counter-intuitive results would have real-world consequences. Section 906 of the Sarbanes-Oxley Act of 2002 ("Sarbanes-Oxley") requires CEOs and CFOs of issuers of public financial statements to certify the accuracy of those financial statements, subject to criminal liabilities.[22] As Congress clarified in the legislative history of Sarbanes-Oxley, accuracy as measured for GAAP is insufficient in certain instances to meet the expectations of Section 906.[23] TEI has concerns whether reporting entities could apply the IETU Approach to the BEAT with sufficient accuracy to satisfy the Sarbanes-Oxley requirements.

Should the FASB adopt the IETU Approach it would also be difficult in certain circumstances to represent that a measurement of deferred tax assets or liabilities at a 10 percent tax rate is an accurate portrayal of financial information when it is known that the economic burden or benefit, respectively, would be well above 21 percent.[24] While this issue existed with the

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[20] Taxpayers in a "regular" taxable loss can owe BEAT, leaving an economic tax burden not measurable as a tax rate but in all cases a burden greater than a 21 percent tax on income.
[21] Conversely, an entity with net deferred tax assets would report lower DTAs when forecasts showed the entity subject to the BEAT, yet in fact those assets would shield taxes economically higher than a 21 percent statutory rate.
[22] The language of the certification is found at 18 U.S.C. § 1350 and required as an exhibit to certain SEC reports by 17 C.F.R. § 240.13a-14(b) and § 240.15d-14(b). Congress also directed the SEC in Section 302 of Sarbanes-Oxley to adopt a civil certification regime for public company filers that includes the same language as required by Section 906 but goes further with respect to a company's internal control over financial reporting. *See* 17 C.F.R. § 229.601(b)(31) (form of certification promulgated bv SEC under Section 302 of Sarbanes-Oxley).
[23] 149 Cong. Rec. S5325, S5331 (daily ed. Apr. 11, 2003) ("Note that Section 906 does not require certification that the financial statements are in accordance with generally accepted accounting principles (GAAP). That omission is intentional in that the certification is designed to ensure an overall accuracy and completeness that is broader than financial reporting requirements under generally accepted accounting principles. In so doing, for purposes of this section, Congress effectively establishes possible liability where statements may be GAAP-compliant but materially misleading. *See States v. Simon*, 425 F.2d 796, 808 (2d Cir. 1969) (finding that accountants can be criminally liable for preparing financial statements that are GAAP-compliant but materially misleading)").
[24] In fact, commentators are noting already that pro-forma financial statements for 2017 may be more accurate than GAAP-compliant statements due to tax reform. Applying the IETU Approach to the BEAT would exacerbate this issue. Peter J. Reilly, "Earnings Havoc Unleashed by Tax Reform," Dec. 31, 2017 (at

Mexican IETU, its scope and materiality were far more limited as compared to the multi-billion dollar adjustment measurements already being publicly announced by major banks.[25]

Another issue that could arise if the IETU Approach is adopted is a lack of comparability of BEAT taxpayers with their peers with respect to key financial statement tax disclosures. For instance, a U.S. company subject to the regular tax would present its annual effective tax rate ("ETR") reconciliation table beginning with the 21 percent federal statutory tax rate or dollars of tax expense calculated by applying this rate to pretax income. A company in the BEAT, however, may need to reconcile to tax expense calculated at the statutory BEAT rate, unless the BEAT is presented as a separate line item in the ETR reconciliation, either approach being complicated. This could create disclosure variability among peer companies, which TEI believes the FASB wishes to avoid through its simplification effort. Further, a company that alternates annually between paying regular tax and the BEAT would likely need to reconcile the ETR at differing rates within the same Form 10-K ETR income taxes footnote disclosure table. In contrast, adopting the AMT Approach, which would more clearly reflect the economic tax burden, would allow easier comparison among companies for financial statement readers.

TEI acknowledges many of the issues described above would arise where an entity predicts moving into and out of BEAT liability. An entity consistently subject to the BEAT and applying the IETU Approach might be able to reflect deferred taxes in a manner consistent with ASC paragraph 740-10-10-3 by using the statutory BEAT rate to measure its deferred taxes. However, FASB guidance concerning the AMT stated at paragraph 90, "[it] would be counterintuitive to assume that an enterprise would permit its AMT credit carryforward to expire unused at the end of the life of the enterprise, which would have to occur if that enterprise was 'always' an AMT taxpayer."[26] It would be counter-intuitive to assume a taxpayer would not alter its operations over time to minimize or eliminate the BEAT.[27] Deloitte's commentary on the BEAT echoes this point, stating, "we believe that most (if not all) taxpayers will ultimately take measures to reduce their BEMTA exposure and therefore ultimately pay taxes at or as close to the regular rate as possible."[28] Stated differently, it is

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https://www.forbes.com/sites/peterjreilly/2017/12/31/earnings-havoc-unleashed-by-tax-act/#2bd2b776492f).

[25] *See, e.g.*, Bank of America Corporation, Form 8-K as filed with the Securities and Exchange Commission on December 22, 2017 (available at [https://www.sec.gov/Archives/edgar/data/70858/000007085817000056/bac122 2178-k.htm](https://www.sec.gov/Archives/edgar/data/70858/000007085817000056/bac1222178-k.htm)); Goldman Sachs Group, Inc., Form 8-K as filed with the Securities and Exchange Commission on December 29, 2017 (available at [https://www.sec.gov/Archives/edgar/data/886982/000119312517381960/d5109](https://www.sec.gov/Archives/edgar/data/886982/000119312517381960/d510945d8k.htm) 45d8k.htm).

[26] *See* FAS 109, Para. 90.

[27] The BEAT includes a threshold application provision requiring taxpayers to have over a 3 percent "base erosion percentage," which is the ratio of BEPs to total deductible payments. Presumably, the BEAT will achieve its goals in that planning over time will reduce BEPs to maintain thresholds below 3 percent wherever possible. In addition, certain "service cost method" payments are exempted as BEPs and presumably taxpayers will avail themselves of this exclusion if out-sourced services are necessary.

[28] *See* Deloitte Commentary.

counter-intuitive that an entity making significant BEPs would not, at a minimum, restructure its operations to move into and out of the BEAT, rather than be subject to chronic risk of economic tax burdens well above the 21 percent statutory rate. Further, under the IETU Approach even an entity consistently subject to the BEAT would present users of financial statements with counter-intuitive balance sheets for deferred tax assets and liabilities and raise the same SOX 906 certification issues discussed above.[29]

The IETU is sufficiently distinguishable from the BEAT, both in its less-cumbersome forecasting and its status as an "alternative" rather than "additional" tax base, to warrant a different disclosure approach. As detailed above, complications arising from applying the IETU Approach to the BEAT would be daunting, the required forecasting would be unreliable, and, most importantly, the end-result would be confusion for financial statement users. Adopting the IETU Approach would result in enormous complexity, far beyond any implementation complexity under prior regimes, and run directly counter to the FASB's ongoing simplification initiatives. In contrast, adoption of the AMT Approach would avoid complexity, volatility and counter-intuitive presentational issues, allowing taxpayers to measure tax expense for the BEAT as it arises—a measurement date that coincides with the time information required to calculate the BEAT is readily available, eliminating the need for significant and unreliable forecasting. Adoption of the AMT Approach for the BEAT is fully supported by prior FASB commentary, as well as FASB actions concerning adoption of disclosures rules for the AMT. Accordingly, TEI urges FASB to adopt this approach.

III. Application of ASC 740 to the GILTI Regime

A. Mechanics of the GILTI Regime

New section 951A entitled, "Global Intangible Low-Taxed Income" or GILTI, creates a new type of tax on foreign offshore income. Prior to its enactment, earnings of a CFC were taxable to a U.S. shareholder on a current basis only if such income constituted certain types of passive or related party income classified as Subpart F income. Otherwise, the U.S. taxation of all non-Subpart F earnings of a CFC was deferred until paid as a dividend distribution. The Subpart F regime acted as a "worldwide" taxation system on foreign income, as all foreign source income was intended to be subject to eventual U.S. taxation (with foreign tax credits available for offset). The Act moves away from a worldwide taxation system towards a "territorial" taxation

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[29] One such counter-intuitive result would arise in acquisition accounting. Net deferred tax liabilities as a result of acquisition step-ups for book purposes would be measured at 10 percent for a chronic BEAT taxpayer. As discussed throughout this letter, this would understate the actual cash tax outflows occurring as these DTLs reverse (and this is true regardless of acquisition accounting). But within acquisition accounting, the DTL would have the effect of reducing goodwill relative to a DTL measured at 21 percent, thereby giving the financial statement reader the impression that the premium paid on a particular acquisition was far ***less*** than it actually was.

system by providing a dividends received deduction for dividends paid to a U.S. shareholder by a CFC out of foreign source earnings.[30]

The new territorial system, however, imposes current U.S. tax on certain foreign source income of CFCs through the GILTI regime. New section 951A requires U.S. shareholders to calculate all "net CFC tested income" for a taxable year and reduce such income by the "net deemed tangible income return" to arrive at each U.S. shareholder's GILTI.[31] Unlike traditional Subpart F, the GILTI calculation is agnostic regarding activities that generate income. In other words, although the Act purports to implement a new "territorial" regime, in practice, the GILTI subjects all foreign earnings over and above a "net deemed tangible return" to current U.S. taxation. In addition, unlike Subpart F, this GILTI inclusion is not measured by or limited to "earnings and profits" of the CFCs and is therefore unaffected by cumulative losses. New section 250 provides a deduction equal to 50 percent of recognized GILTI income (limited by a taxpayer's taxable income), thereby yielding a 10.5 percent rate of taxation on GILTI income.[32]

A credit is provided for any foreign taxes paid with respect to GILTI income, reduced by 20 percent and subject to a new foreign tax credit (FTC) "basket." The net effect is taxpayers not subject to other FTC limitations (*e.g.*, section 904(a) limitations) would owe no GILTI tax provided the CFC is subject to tax at a rate above 13.125 percent (*i.e.*, 80% of 13.125% = 10.5%). In essence, the United States has expanded CFC income subject to current U.S. tax (above a normalized return on tangible investments), while providing a foreign tax credit to offset U.S. taxes on a current basis.

B. Application of ASC 740 to the GILTI Regime

Historically, ASC 740 would generally look to the outside basis in a CFC to measure deferred taxes related to U.S. taxation of foreign earnings. Under the Act, however, such an outside basis approach appears less rational in some cases, because of the new territorial dividends-received-deduction system. In other words, the basis differences between book and tax of a foreign subsidiary will not reflect future U.S. income tax cost because foreign source dividends paid out of earnings are no longer subject to U.S. tax (yet sale on the gain inherent in such entities is subject to tax). Accordingly, the new regime lacks predictable U.S. tax consequences with respect to outside basis differences.

Under existing ASC 740 guidance, the Big 4 firms have acknowledged alternative views in measuring deferred taxes for Subpart F income where an indefinite reinvestment assertion has otherwise been made. PwC's commentary denotes two acceptable views in defining the unit of account for the Subpart F income as either inside basis or outside basis.[33] In applying the inside basis unit of account view, the reversal of applicable temporary differences of the foreign

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[30] Pub. Law No. 115-97, § 14101 (2017).
[31] Pub. Law No. 115-97, § 14201 (2017).
[32] Pub. Law No. 115-97, § 14202 (2017).
[33] PwC's Income Taxes Guide, Section 11.10.2 (Aug. 2017 update).

subsidiary will create Subpart F income, creating the equivalent of an inside basis US taxable temporary difference because the US tax liability in the form of Subpart F is deferred but not permanently avoided. In applying the outside basis unit of account view, the Subpart F income is a component of the parent entity's outside basis difference, and deferred taxes would be recorded for the portion of the outside basis difference that corresponds to the amounts already recognized for financial reporting purposes, not to exceed the parent's book-over-tax outside basis difference.

Like Subpart F, the GILTI regime presents significant ASC 740 complications. Recent commentary published by KPMG and Deloitte expresses the view that it may be appropriate for entities to record U.S. deferred tax assets or liabilities that would, upon reversal, impact the calculation of future GILTI liabilities. KPMG's commentary states:[34]

> Question 4.10
> Should a company recognize deferred taxes for basis differences expected to reverse as GILTI?
>
> Interpretive response: This question is not resolved. Currently, we believe the current tax imposed on GILTI is similar to the tax imposed on Subpart F income and may require companies to recognize deferred taxes. Because GILTI is included in the US shareholder's taxable income when earned by the CFC, we believe the US shareholder may need to recognize deferred assets and liabilities when basis differences exist that are expected to affect the amount of the GILTI inclusion upon reversal. Companies should consider the partial effects of foreign tax credits provided under the Act when measuring the liability. However, as announced in the January 4, 2018 FASB Action Alert, the Board will be discussing its staff's research on this issue at its January 10, 2018 meeting. We will update our guidance as necessary in response to future developments.

Deloitte's commentary is similar, also stating companies "may" be permitted to record deferred taxes, both assets and liabilities, related to GILTI:[35]

> Q&A #4.2
> If the financial reporting basis in the investment exceeds the tax basis, we tentatively believe that the company should determine whether the outside basis difference will reverse in a taxable manner through recognition of income as result of the GILTI provision. In making this determination, the company should consider how the inside basis

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[34] KPMG, Tax Reform, Supplement to KPMG's Handbook, Accounting for Income Taxes (Jan. 5, 2018)
[35] Deloitte, Financial Reporting Alert 18-1, Frequently Asked Questions About Tax Reform (Jan. 3, 2018).

differences will reverse and whether such reversals will result in a GILTI inclusion.

Q&A #4.4
However, because the Act's GILTI provision creates a new category of Subpart F inclusions that may often cause a deductible outside basis difference to partly or wholly reverse and directly affect the GILTI inclusion, not recording a DTA in these circumstances may distort the financial statements. Therefore, we currently believe that recording a DTA may be an acceptable alternative approach if the underlying inside basis differences were expected to (1) reverse in a period in which the parent has a GILTI inclusion and (2) result in a reversal of the outside basis difference.

C. TEI Analysis and Recommendation for a Flexible Disclosure Approach

Similar to current guidance on Subpart F, TEI favors a flexible approach to reporting the financial impacts of the GILTI regime; an approach that acknowledges certain facts and circumstances may warrant recording GILTI deferred taxes, but other facts and circumstances may not. We believe this position aligns with views expressed in Big 4 commentary addressed above.

Depending on specific circumstances, TEI believes period cost GILTI charges could be appropriate. In other cases, however, recording deferred taxes for temporary differences, including applying branch accounting, might yield a more appropriate reflection of financial statement income. This recommended approach is illustrated by the following two examples:

Example A	Example B
US1 owns 100 percent of CFC1, formed and operating in Country Y. CFC1 owns no intangible property and manufactures widgets, which requires significant capital investment, but does not require expertise and yields a relatively low return on investment.	US2 owns 100 percent of CFC2, formed and operating in Country X. CFC2 owns intellectual property but has relatively little tangible assets. The intellectual property is licensed to third-parties, earning CFC2 significant profits.

In Example A, US1 is unlikely to owe GILTI taxes because CFC1's capital investments will yield high tangible asset basis and will therefore generate "net deemed tangible income" in excess of "net CFC tested income." In such a case, recording U.S. deferred taxes for temporary inside basis differences would require recording deferred tax assets and liabilities, the reversal of which would not be expected to reduce or increase any U.S. taxes related to GILTI because there are no such taxes to reduce or increase in the foreseeable future.

In Example B, however, US2 is likely to owe GILTI taxes in each period because CFC2 has relatively limited capital investments and holds intangible property earning a high rate of return. While it may be appropriate to record period charges, reporting such charges could result in significant effective tax rate variability that does not appropriately reflect accrual accounting. Instead, recording deferred tax assets or liabilities for inside basis differences could, in the case of CFC2, result in appropriate timing of accruals for expected U.S. taxes owed with respect to the GILTI. In certain circumstances, the operations of CFC2 would be effectively taxed by the United States in a manner more similar to a branch than to the former CFC regime prior to enactment of GILTI. This is because, other than the small tangible return, all income of CFC2 would be subject to current U.S. taxation, regardless of whether such income would or would not qualify as Subpart F. In such a case, permitting US2 to account for basis difference in CFC2 under branch accounting rules may yield a more appropriate measurement of effective tax rate.[36]

There could be further complexity in determining whether US2 should record both deferred tax assets and liabilities. Historically, companies expecting to generate Subpart F inclusions were generally required to accrue deferred tax liabilities for basis differences that might generate future Subpart F income. But because GILTI applies across all income types, there may be a question as to whether the deferred taxes should also be thought of more broadly such that assets should not be treated differently than liabilities, similar to the guidance that both KPMG and Deloitte have recently published. The merits for recording assets may be similarly fact-specific. TEI urges the FASB to provide entities with the ability to make policy judgments as appropriate on these points.

The nature of the GILTI and similarities to the prior Subpart F regime support the adoption of a facts-and-circumstances-based analysis to determine the appropriate method to record the financial statement impacts of the GILTI, and we urge the FASB to issue guidance allowing preparers to make appropriate judgments. While this position may lead to some lack of comparability across entities, the approach would ensure that the tax expense and effective tax rate of each particular entity is appropriately reflected based on its unique facts and circumstances.[37] ASC 740 currently allows a diversity of reporting positions for the recordation

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[36] An additional complexity not addressed herein would arise where CFC2 receives a transfer of intellectual property in which CFC2 has a local country tax basis, but no U.S. tax basis. Absent the ability to recognize the impact of GILTI on the transfer, companies would face the dilemma of whether or not to disclose why GAAP would not accurately reflect the economics of the transaction. This is yet another factual circumstance that demonstrates a need for the flexible approach advocated by TEI.

[37] As drafted, GILTI currently applies as measured on a "US shareholder" basis, meaning one reporting entity could have multiple US entities in varying GILTI positions. The Treasury Department, however, may issue regulations or guidance applying GILTI across U.S. consolidated groups, meaning most reporting entities would have one GILTI policy. We acknowledge it could be possible for the facts and circumstances to change over time such that the proper policy could change, as with current Subpart F judgments made by entities. We would not expect this to be a common fact pattern, but rather, exceptional circumstances where the structural or underlying business has substantially changed.

of deferred taxes inside CFCs with respect to Subpart F, and this has not adversely impacted investors' abilities to compare tax expense across financial statements. The GILTI regime is broader than, but in many ways akin to, Subpart F,[38] and TEI believes a reporting rule allowing similar flexibility is appropriate.

Adopting a flexible, facts-and-circumstances approach to recording GILTI deferred taxes may appear inconsistent with adopting a definitive, "add-on" approach to accounting for BEAT. A closer look demonstrates, however, that a rational and compelling basis exists for adopting different approaches to accounting for the BEAT and the GILTI regime. Even assuming financial statement preparers could reliably forecast their expected BEAT into future years (something we contend cannot be done to current GAAP standards), measuring deferred taxes at the 10 percent BEAT rate remains counter-intuitive, would not reflect the economic higher tax burden, and would create a high likelihood of financial statement volatility as described above. Recording GILTI deferred taxes does not suffer such infirmities. Additionally, adopting different approaches for the BEAT and the GILTI regime is actually consistent with existing GAAP, as the BEAT/GILTI treatment TEI is advocating aligns with the historic AMT/Subpart F treatment under existing FASB guidance. As previously noted, ASC 740 relied on measuring deferred taxes at the regular statutory rate, in part, because "no one can predict whether an entity will always be an AMT taxpayer." Simultaneously, entities were required to decide whether to record or not record deferred taxes for outside basis differences associated with expectations of Subpart F income. TEI contends that the BEAT and the GILTI regime are best analogized to these prior regimes and the different approaches to recording deferred taxes remains appropriately consistent. The question posed by BEAT and AMT is a matter of measurement in addressing ***which*** statutory tax rate is appropriate for an entity to measure its deferred taxes. In contrast, the deferred tax considerations of the GILTI and Subpart F regimes are a matter of recognition of US taxable or deductible temporary differences. This question of ***whether*** an organization should record deferred taxes—following either an outside basis or branch accounting approach ***if*** deferred taxes are recorded—should be made based on reasonable judgement, consistently applied using the well-reasoned, still appropriate historic FASB guidance. Ultimately, TEI is requesting the FASB to clarify guidance that currently allows sufficient flexibility to account for these differences by situation, as with Subpart F treatment. Like Subpart F, the GILTI regime provides no simple, singular financial accounting answer due to circumstantial differentiations, while the BEAT presents a clear solution following the recommended add-on approach toward maintaining more reliable, less volatile, and intuitive financial statement results.

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[38] To illustrate, new Section 951A(f) is entitled, "Treatment [of GILTI] as Subpart F Income for Certain Purposes."

TEI appreciates this opportunity to share its membership's view on the proper application of ASC 740 to the BEAT and the GILTI regime. These comments were prepared by TEI's Financial Reporting Committee, whose Chair is Stephen Dunphy. Patrick Evans, Chief Tax Counsel for TEI, coordinated the preparation of the comments. If you have questions about TEI's comments, please contact Mr. Dunphy at (925) 965-4277 or stephen.dunphy@ros.com or Mr. Evans at (202) 464-8351 or pevans@tei.org.

Respectfully submitted,
Tax Executives Institute

Robert L. Howren
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Appendix
Comparison of Technical Details of the BEAT against the IETU and AMT

To test the reasoning that the BEAT is akin to a parallel taxing system, more similar to the Mexican IETU than the repealed AMT, TEI compared technical details of the BEAT against the IETU and AMT. The comparison demonstrates that the BEAT is more like the AMT than the IETU. Indeed, the only substantive similarity between the BEAT and IETU is the lack of creditability against regular tax liability. This fact alone does not support treating the BEAT the same as the IETU for ASC 740 disclosure purposes.

The following table summarizes the distinctions and similarities among the regimes. A detailed analysis follows.

	BEAT	**AMT**	**IETU**
Tax Base	Taxable Income	Taxable Income	Cash Receipts
Adjustment Regime	Elimination of "Base Erosion Payments"	Elimination of "Preference" Items	Elimination of certain deductible and depreciable items
Tax Due Under Regime	Additional amount above regular liability	Additional amount above regular liability	Alternative amount based on higher liability
Stock-Based Compensation	Deductible	Deductible	Non-Deductible
Taxes Paid Creditability/NOL Carryforward	None	Yes, creditable against future regular tax	IETU NOL carry-forwards reduce future IETU liability
Tax Credit Offsets to 'Regular' Tax Liability?	Yes, certain Section 38 credits offset	Yes, with possible exceptions	No
Intercompany Forecasting Necessary?	Yes, extensive if IETU Approach adopted; Only current year if AMT Approach adopted	Only current year expense	Yes, long-term intercompany royalty and financing adjustment
Forecasting of timing differences for both domestic and controlled foreign corporations required?	Yes, extensive if IETU Approach adopted; Only current year if AMT Approach adopted	N/A	N/A
Forecasting of allocation of domestic taxable income by legal entity portion allocable to US vs non-US customers?	Yes, extensive if IETU Approach adopted; Only current year if AMT Approach adopted	N/A	N/A

It does not appear Congress intended the BEAT to operate as a separate tax system. Section 59A is entitled, a "Tax on Base Erosion Payments," and it functions effectively as an add-on tax to discourage offshoring of jobs and, eventually, encourage the return of outsourced jobs to the United States. The effect of the BEAT is to tax additional BEPs at a 10 percent rate, yet the functionality of the provision is fully integrated with the income tax system.[1] The BEAT is formally calculated as an addition, not an alternative.[2] In this way, it is not dissimilar from the AMT or IETU. We understand, however, that in the case of the IETU, its status as an "addition" held no bearing on ultimate tax due, *i.e.*, in effect it was a parallel system. When a taxpayer was subject to IETU, its taxes were the IETU-calculated amount. When a taxpayer was not taxed under IETU, the tax liability was the regular tax amount. Yet for the BEAT, the status as an "addition" is critical in that the regular tax amount remains subject to section 38 credit offsets.

There are critical distinctions between the IETU and BEAT. The BEAT calculation, as noted earlier, starts with a taxpayer's "regular" taxable income and, at base, adds back deductions taken for BEPs. The IETU starts with an entirely different taxable income base—cash flow receipts—and then denies a number of deductible items. From this perspective, the IETU appears to be more of a "parallel," rather than integrated system, in that it creates an entirely different income tax base. This is not surprising given that the IETU replaced an older "asset tax" system in Mexico, which also operated in parallel to the regular income tax system.

Meanwhile, in this sense, the BEAT appears more like the AMT in that both begin from the same taxable income base. The AMT is then adjusted for denial of certain "preference" items, while the BEAT is adjusted for BEPs. But, as with the AMT, a taxpayer with a sufficiently large taxable loss or taxable income under "regular" tax calculations would owe neither AMT nor BEAT. This does not hold true for the IETU given the differing starting points for gross receipts.

The IETU has another important distinguishing factor in that Mexican tax law does not generally allow deductions for stock-based compensation (SBC) absent a re-charge mechanism with related parties providing shares. SBC deductions do not factor into the IETU or "regular" Mexican tax base for taxpayers without this mechanism.[3] Accordingly, entities would not have been required to forecast SBC in order to determine whether they were expecting IETU or

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[1] Given this integration, the BEAT appears to be an "income tax" subject to the disclosure rules of ASC 740.

[2] Section 59A(b)(1). Note that the BEAT also creates an effective denial of foreign tax credits. Section 59A(b)(1)(B)). The inability to forecast amounts of foreign taxes that might be creditable adds to the complexity of forecasting BEAT because such credits drive ***up*** the BEAT liability but also create another point of integration with the "regular" tax system.

[3] SBC was not deductible under IETU and therefore it would not have been necessary to forecast whether the IETU rate should apply to deferred assets and liabilities. We understand, however, that IETU allowed for a .175 percent credit against taxes due for wages. So, the IETU would use SBC to determine ultimate liability, but that would not have been a factor in whether IETU (and the IETU rate) was expected to apply.

regular tax to apply. Because the BEAT starts from regular U.S. taxable income, SBC would generally be a deductible expense. Given the BEAT's application is largely dependent on whether taxable income is greater than BEPs, SBC, in many cases, may be a critical forecasting input for the BEAT (as well as the AMT) but not the IETU.[4]

[4] Again, foreign tax credits will also factor into a BEAT calculation for many taxpayers.