What's Next After Tax Reform?

Bloomberg Tax Roundtable

Cheryl Saenz: Welcome all of you. I'm Cheryl Saenz. I'm the news director for tax and accounting. I appreciate your time here. I'd like to start by just having everyone go around the table, say their name and where you're from or what your -- whatever you would like to say about yourself. And then, we can go ahead with your questions.

Lisa Starczewski: Thank you. My name is Lisa Starczewski. And I am with Buchanan, Ingersoll, and Rooney. I focus my practice on business taxation, especially the taxation of pass-through entities.

Bill Alexander: Hi. I'm Bill Alexander. I'm with Skadden, Arps. I mostly work in the corporate M&A area.

John Harrington: Hi. I'm John Harrington. I'm with the law firm of Dentons. And I tend to work in the international area.

Richard Franklin: Hi. Richard Franklin. And I'm a trust and estates lawyer in Washington, D.C.

Joe Huddleston: I'm Joe Huddleston. I'm with Ernst and Young LLP in their national tax office here in Washington.

Laura Davison: I'm Laura Davison. I'm a reporter here at Bloomberg Tax.

Colleen Murphy: I'm Colleen Murphy. I'm an editor on the international tax.

Sony Kassam: I'm Sony Kassam. I'm a reporter for Bloomberg Tax.

Laura Davison: All right. So we'll go ahead and get started with Richard. In the bill, the estate tax exemptions were doubled, not repealed as was initially the game plan. So, what can we expect to see in terms of how strategies change in the -- in the short term and then also in 2026 when the doubling reverts back to what was previously current law?

Richard Franklin: Great. Well, you're right that the base exemption change from 5 million to 10 million is indexed for inflation so for an individual that means 11.2 million is exempt from estate taxes, gift taxes during lifetime, and the GST exemptions also matches that amount. So, that's 22.4 million for a married couple. That reduces the number of people subject to the estate tax from .02 percent to .01 percent. In effect, it repeals the estate tax for the vast majority of the population with a caveat, as you alluded to, that this provision sunsets in 2026.

The act leaves the entire estate, gift, and GST system in place, which made it easy for this

Congress to make the change. But it also makes it easy for, you know, future legislation to unwind these changes or simply leave them as they currently are, and they will sunset in 2026. And while it seems like it's impossible to remember before November 8th, 2016, the other candidate would have reduced the exclusion amount and increased the estate tax rate. So, it's important to keep in mind these changes are really set up easily to, you know, be changed in the future.

So, some of the planning implications would include that for those that can afford to make the changes that they should go ahead and quickly, you know, to use the exclusion to go ahead and quickly do it. And so, for the very wealthy that would be a strategy that they would currently employ to do that as soon as possible. The new doubling of the amount, I believe, that if the exclusion is used today, the entire 11.2 million, and the amount goes down in the future -- the exemption goes down in the future, that the taxpayer should always get credit for that.

But, in effect, you get credit for the new 11.2 million, the new doubling amount from 5.6 to 11.2. The original 5.6 has to be used. So, you can imagine that most Americans are not capable of giving away 11.2 million all at once. So, this provision is great for the uber-wealthy. It's going to make it much more complicated planning-wise for families who are not able to immediately use the exclusion. And in some sense, if they can't do it it's a use it or lose it system. In 2026 it sunsets. So, for those families that can't use it prior to that time, you know, it will be in effect illusory and somewhat confusing, because it makes the planning options more complicated.

Laura Davison: Great. Anything else you want to add?

Richard Franklin: Well, I would say that a lot of people will probably focus on using -- making gifts to trusts where if they're a married couple where one of the spouses is a beneficiary. It makes portability much more important, you know, than it was. It doubles the exclusion so the value of preserving that exemption of the first spouse to die is over 4 million now, so missing that exemption -- missing that election is more costly than it used to be. And because income taxes are being more important for most families than estate tax savings, it'll mean less funding I think of credit shelter trusts and more reliance on portability of the first spouse's death.

Laura Davison: Thanks. Bill and Lisa, I want to switch over to you guys and ask you, planning-side, for businesses, for corporations, and for pass-throughs, what opportunities exist now? We just heard from Richard kind of on what he's going to see on the estate tax side. What are we going to see on the business side and what can happen now and what needs to wait a little bit until we hear more from the IRS about how they're going to interpret some of these new changes?

Lisa Starczewski: Well, those are great questions. And before I specifically address them I just wanted to, you know, start off with a disclaimer of sorts. And, frankly, I think this applies to everything I'm going to say today and maybe to everything that everyone's going to say, but I only speak for myself.

I think it's -- I think everyone knows this, but I think it's very important just to think about it for a minute. We have this massive new tax act. It was signed into law December 22nd, and today is January 9th. So we have all been digesting, reading, thinking, analyzing. We've had two and a half weeks. We've had prior versions, but there are significant differences between those versions and what we ended up with in some instances. And so, the point is it's new. It's very new.

And secondly, it came to us in a relatively unique way -- a fast, unique way. We didn't get the benefit of hearings and debates and learning with respect to the intent behind these provisions, the way in which they're intended to be applied. So, we don't have the benefit of that process. We don't have a blue book yet. We have legislation that was quickly passed, but is quite impactful and has layers of complexity.

So, what this means, with respect to my answers right now and I think, you know, everything that we have to say, is that we might be right on right now, but there is a lot of additional guidance to come. There is a lot more thought and time that I know I'm going to give to this and I know my colleagues are going to give to this. And these answers are going to be fluid. So, that's my disclaimer to start with.

In many instances there is uncertainty, and additional guidance is necessary. And as I talk, and I'm sure all of us will do this today, we will try to point that out where we really feel as if additional guidance is critical. With respect to planning opportunities, I mean, certainly there are opportunities to plan. More of those opportunities will come as time goes by and as we understand more and we learn more about how these provisions interact with each other.

Everyone wants to talk about choice of entity as, you know, a planning opportunity. We get calls from clients on choice of entity literally every day. I personally don't believe and I haven't talked to many people who believe that we're going to see this wholesale, you know, conversion to C corporations. There are still a lot of benefits to operating in pass-through form that I think trump, [laughs] no pun intended, the reduced corporate tax rate. It is still, you know, beneficial in many instances to be a pass-through. And, in fact, if you look at the rate applicable to C corps and you add the second layer of tax when the income is distributed out as a dividend to owners there is still an advantage from rate perspective assuming that the 20 percent pass-through deduction is available to the pass-through.

But there is no question that for people starting new businesses, choice of entity got a little bit more complicated, a little bit different than the items we focused on before. We may see different conclusions than we've seen under current rules in specific circumstances.

Existing businesses, I think, also need to look at that issue and determine whether they need to make any changes depending on the type of business they're in, the availability of the pass-through deduction, whether or not they're going to be hit by the excess business loss provision. You may have U.S. non-C corps that have foreign subsidiaries that want to take advantage of the new dividends received deduction. There are all kinds of factors now that we have to at least talk with our clients about when it comes to choice of entity. In many cases, though, I think that when you do the modeling staying put is often going to be the right answer. It's just not always going to be the right answer.

I think with respect to the pass-through deduction there's a lot of planning that can happen there. There are going to be ways I think to plan into the deduction and out of the wage and qualified property cap. Maybe there can be some restructuring, for instance, of independent contractor relationships into employment relationships. Again, very fact- and circumstance-specific. All of this planning is very fact- and circumstance-specific.

Real estate businesses are highly impacted, I think, across the board by a lot of these provisions. I think for that type of business the business interest limitation may be incredibly impactful. There is going to need to be analysis and modeling about whether a business should elect out of that limitation, because that needs to be compared, that scenario, with the increased depreciation periods, the loss of bonus depreciation for qualified improvement property. There's a tradeoff to the election out of that limitation. And, again, we have sat down with a few clients. And what we have come up with is there's no one-size-fits-all answer to how to deal with that. It's client-specific. It's business-specific.

So for me, you know, I think it's very important to understand that under the Tax Act there's no quick and easy answer to what should we change. You know, if this and this are true, do we do this? It's more like a matrix. There are a lot of factors. And all of them have to be looked at to kind of get to the bottom line of, you know, should there be change.

I do think, and I'm sure Bill can expand on this, that in the context of C corporations certainly the reduced rate is going to, you know, create some planning opportunities. And we may see some of the tricks of the past to retain earnings in the C corporation and not distribute them out, because we want to avoid that second level of tax and stay with our 21 percent.

And, you know, I think the fact that the basis step-up is still there on the estate side, that there is some opportunity there to leave assets in corporate solution until death and get the step-up. Personal holding company rules might get in the way, accumulated earnings tax might get in the way. But, you know, from a planning perspective do you have to talk about it? I think -- I think you do.

So I think for us the moral of the story for -- you know, is that at the heart of the opportunity is the need to sit down, every business to sit down with their tax adviser and talk through the type of business they're in, what their business goals are, the economics of how their business works. And then think about that in the context of all this change and ask questions about, you know, am I best positioned under the new rules? That's where the opportunity is.

Laura Davison: Bill, I was wondering if you could share a little bit what -- you know, with this corporate rate going from 35 down to 21 what sort of planning, you know, are people starting to talk about? What do -- what do people need to consider?

Bill Alexander: Well, the largest corporations are already corporations. So, they don't have to consider whether they want to be corporations. They're stuck there. What I think they're mostly focused on right now is if they have a multinational business, how to structure that. Their worldwide business, is it configured the right way? And I think that's really where a lot of their attention is going to be. It's been over the last year in anticipation of this and will continue to be there for a while. And I think that's really, in terms of what people are thinking about, that's probably at the head of the list for the biggest businesses, multi -- at least the ones that are multinational.

In terms of the attractiveness of, you know, subchapter C, well, the rates are lower, but again, you know, there are a lot of things that have changed. I think Lisa used the word "modeling," and I think that's really critical. People will be sitting down in front of a spreadsheet and saying, is this good for me? One of the things people have to be mindful of is the fact that it is a lot easier to get into subchapter C than to get out. And so, you really have to believe in this. And, you know, I can't tell you one way or the other.

Laura Davison: Just to kind of follow up. You know, Lisa alluded to this, you know, matrix of solutions. One of the things that's tricky about this bill is that it's a mix of permanent and temporary. You know, all the pass-through stuff that is temporary. Full expensing, that's a five-year provision. The corporate stuff is all permanent, but of course, you know, nothing is really permanent in the tax code. It can always be changed or repealed or whatever by a future Congress.

How do you go about planning when these are the rules for now but in five or six or 10 years later, different president, different Congress, things could change drastically. You know, how do you advise clients in that world?

Lisa Starczewski: Well, no question that the fact that some of these provisions expire just adds a layer of complexity to all of it. You know, I think it's important to keep in mind that it may not be five or 10 years before it changes, that actually, you know, it could change as soon as -- if the president changes [laughs] and we have a new Congress we could see a change in any of this, including the permanent changes.

If there's one thing I think we've all learned, because we've all been doing this for a long time, is nothing is really permanent. And tax law -- you know, you know the tax law for this year, and maybe know it for next year. But you can't look very far down the road and know with certainty what the tax law's going to be. So, you're always kind of dealing with that on some level.

You know, I think here, when some of these changes that are sunsetting or expiring have to do with choice of entity, for instance. And you're modeling all of this and you're looking at all of these possible solutions and then you know that one piece of that might go away which could greatly impact, for instance, the pass-through rate. And you've made a decision -- you know, it's difficult.

Now, that might, as Bill pointed out -- because it's hard to get out of a C corp, but it's easier to get out of an LLC or partnership, right? That might be part of your decision. Well, you know, we've got think about what happens down the road and what impact that might have on our decision today. It just makes the job, you know, that much harder. It's just -- it's especially difficult to plan, in my opinion, when foundational pieces of your decision-making are moving pieces.

Bill Alexander: And then, there are some things where, well, you just have to go with what you have. In a sense, the theory behind expensing is that -- "Well, this depreciable property is on sale this year, so buy it now. And if you buy it now, well, you can't have made too bad of a mistake. You know how it's going to work out. If you wait, we can't make you any promises."

Joe Huddleston: You know, and there's another factor here that I keep thinking about as we talk about structuring and planning -- not necessarily at the federal level, but certainly at the federal level and then throughout all the state entities also -- is the new partnership audit rules --

Laura Davison: Yes.

Joe Huddleston: -- that impact all of these discussions, because so many of these pass-through are structured in partnership structures that are going to have to make substantial changes in how they look. Really, by the end of this coming year, they're going to have these things in place. And nobody is moving very much in that direction right now -- at least I don't seem to see it.

Lisa Starczewski: Well, I think there's a -- I think everyone is waiting, to the extent that they can, for some sort of final guidance with respect to those rules, because even deciding how to draft -- which we've been doing a great deal of -- and change your operating agreement is tricky when you're operating in a vacuum, and you're not quite sure exactly how these rules are going to be applied. We have the proposed regulations, but you know, we really cannot completely rely on that.

Joe Huddleston: I guess because we keep hearing that a lot of those may change, but we've not really -- I've not really seen any indication that they are going to change, just the discussion about whether they're going to change.

Lisa Starczewski: And there's also been requests for some sort of delay with respect to the effectiveness of the rules -- or the effective date, rather -- of those rules.

Laura Davison: And Joe, you bring up an interesting point, to sort of -- kind of the uncertainty surrounding many parts of the tax code. And even, you know, Lisa was talking about how clients are sitting down, and this law is only two-and-a-half weeks old. And states are also sitting down and saying -- you know, trying to figure out what's the best way for them to react.

So, I wanted to ask, you know, that, you know, is it safe to assume that many states won't follow the full expensing provision, just as they decoupled from bonus depreciation, you know? And what do you expect there, why, and kind of how do you factor that from a state-side --

Joe Huddleston: Sure, let me give you a little background on what's going on in the states, certainly last year and the year before. And while the projections are better this year, one of the key indications for the states is that they have missed their projections substantially over the last few years. Somewhere close to 30 of the 50 states have substantially missed their revenue projections over the last couple of years. That's causing real problems. So, when you add to that what's happening at the federal level, the likelihood that states would not decouple is very small.

Clearly, in the area, as we looked at this in the 1st of the year, as Lisa pointed out, the discussion that was talked about -- tax reform at the federal level -- is substantially different than what we have seen it end up being. The states were really intensely looking at modeling because most states thought, early on, that there was going to be substantial windfalls to the states, and they were trying to figure out how they would react to that. But as we moved into the summer and fall, the states began to understand that there was not going to be substantial windfall.

Some particular states might see a windfall; others might not, depending on repatriation issues. But largely, states where they would see a revenue reduction, they clearly are going to decouple, much as they did with bonus depreciation before, but at the expensing level and in depreciation. States will decouple if they have to.

Many states will not have to decouple because of the nature of their relationship to the Internal Revenue Code to begin with. Many states may not have to decouple. They just -- they find themselves in a position where they either have to substantively pick up these changes or they're not impacted by them. And that's true in a couple of other areas also. But I find it very unlikely that states, in their current economic situation, are going to ride any kind of a bus that results in reduction in revenue for them.

Laura Davison: And so, what does that mean for the pass-through deduction, whether they couple or decouple from that?

Joe Huddleston: Well, it clearly is a problem. The states are all over the board on how they treat pass-throughs. And so, it's highly unlikely that the states are going to do anything, as I mentioned before, that negatively impacts their revenue in the short term.

Laura Davison: So, one of the political hot-button issues -- as this was moving through Congress -- particularly in the House, was that, you know, what they were going to do with the SALT, the state and local tax deduction. So, now, the conversation -- you know, obviously, they ended up with that $10,000 cap, which was pleasing to some -- not so much to others.

At the state level, they're talking about ways to sort of lessen the blow for residents, whether that be, you know, payroll taxes instead of income taxes, or creating a charitable deduction to fund public services. You know, does that sound like a viable way to get around this? You know, what do you -- how do you see that playing out in the next couple years?

Joe Huddleston: Well, I think that many people up -- right up until the end were very hopeful that the state and local deduction would be maintained. So, a lot of states have not given a lot of thought to what was going to happen as a result of that. But clearly, with a cap, they're going to be impacted. But keep in mind, there's a real distinction here between individual citizens of the state -- who are going to see a direct impact on themselves, particularly in those high tax states that we all know around the country -- whether it's California, New York, Connecticut. The individual citizens are going to see an impact.

The state governments, on the other hand, may not see anything but a marginal impact as a result of that. So, there's the real question, as between the two -- do the citizens and the state demand some kind of action? Because if you're talking about state revenues as a result of this cap, the alteration is going to be marginal.

Colleen Murphy: And John, on the international side, we've talked a lot about planning today, and certainly one group that's been paying really close attention as this bill has developed and as it was passed is multinational companies. So, what should companies with cross-border operations consider as they're crafting a long-term tax strategy?

John Harrington: Yeah. I think just -- I think as the discussion that we just had -- had shown -- I mean, the Tax Cuts and Jobs Act is so big and so complicated, so many interactive elements that, as an initial matter, I think just as Bill pointed out, the companies need to spend some time -- so did Lisa -- about understanding how it affects them and when the various impact of the provisions start to apply. So first, I think you have to do a scoping kind of aspect, in terms of what the short-term, the long-term impact are -- is going to be.

And then, I think the company needs to decide, you know, whether it needs to change its structure. And that could be fundamental changes, like where the parent company is located -- whether it's the United States or somewhere else. It's also going to mean re-evaluating or revisiting more minor issues, such as whether an entity should remain disregarded or a controlled foreign corporation -- a CFC -- or whether it should convert, you know, from one to the other; whether or not you need to insert a domestic holding company into the structure or take one out. Also, you have -- you can have assets such as intellectual property that are held in, you know, in a particular holding company -- or used in a certain way. And you need to -- that structure was based on a law that may not make sense anymore.

So, revisiting that structure and those types of things -- structural -- I think are important. And then I think, then you have to move into the more -- call it "transactional issues," in terms of looking at what you're doing now. You know, is it something that -- the new law, does that make it -- is there a more favorable way to do it or is it -- or what you're doing now is unfavorable; you need to re-visit it? So, it's like a whole level of things I think you have to proceed.

Colleen Murphy: And the European Union has been -- members have been pretty vocal about some concerns that they have over these provisions, particularly the base erosion and anti-abuse tax provision, the BEAT. The EU has warned about a WTO challenge over some of the provisions of the bill, saying that it could break their trade principles. What do you think is the likelihood of such a case? And what would the impact of that be?

John Harrington: Well, I mean, first of all, whether to bring a WTO challenge is ultimately a political decision. You can have a very strong case and decide for -- a country could have a very strong case and think, for political reasons, they don't want to bring a dispute. They can also defer bringing a dispute. They can also have a relatively weak case and decide, for domestic consumption or something else, it's worth bringing the case. So, ultimately, that's tied to both the strength of the challenge and also just, you know, international politics.

And you also have to recognize -- I mean, since the Ways and Means Committee, the Finance

Committee have jurisdiction over trade as well as taxes, you know, presumably they did take a close look at this, in terms of feeling comfortable that this is compliant with our trade agreements.

But having said that, you know, being someone who, on the Hill worked on the replacement of the foreign sales corporation with the extra-territorial income regime, and then replacement of the extra-territorial income regime when I was at Treasury, that -- I mean, the track record of the United States on this isn't good. I mean, each time, we seem to think we've found some way to create, you know, an incentive for exports, following the rules for consumption taxes without actually having a value-added tax, or sales tax.

But in -- but on each time that European countries have brought that under GATT or under WTO, and the U.S. has lost that. And the decisions have been typically the -- you know, the World Trade Organization or the GATT, you know, bodies -- appellate body has said these are things that, if you want to get the provisions of a value-added tax, consumption tax, enact one. So, whether this is like Roadrunner against, you know, Wile E. Coyote is -- remains to be seen. So --

Joe Huddleston: John, don't these disputes generally take a long time?

John Harrington: They do, and I think we certainly heard that, in terms of that. And again, there are settlements that are associated with them and so forth. But in terms -- they could go back to Lisa's sort of point, about whether -- what happens first, if these were challenges or a decision before this was changed? You know, who knows? It could be a moving target as well. But you're right; they do take -- they typically take, you know, years, if it goes to the appellate body and if there's challenges to sanctions and so forth. But --

Colleen Murphy: And some countries, like China and Australia, have been concerned that the reforms in the U.S. could hurt their own competitiveness. And there's been talk about different countries making their own reforms, kind of in response to what the U.S. is doing. Is there a risk that some of that could clash with what the OECD is trying to do around base erosion and profit shifting?

John Harrington: Yeah. I mean, when it comes to BEPS, I -- just two points I'll make about that. You know, I mean, first, I don't view BEPS as being this principled attempt to change the international tax rules. I mean, countries got together and did what the antitrust rules prevent companies from doing, you know? They saw themselves as losing revenue because of what other countries were doing. You know, they kind of -- they decided that they couldn't change their own rules without -- unless other countries tightened there. And so, BEPS was creating a common framework, getting buy-in, and proceeding in that way.

So, and even then, BEPS was always kind of acting -- countries acting in their own interest. They just found it made sense to act in a coordinated way for a period of time. And the second other -- when it comes to BEPS, the United States did participate in the OECD as part of the BEPS process. But that was the executive branch. And it was also the executive branch in a prior administration.

A lot of these international provisions really were generated, you know, through Congress, which wasn't really part of the BEPS process, didn't have the same sort of buy-in that you'll see, like, in a parliamentary country, where the Treasury -- you know, the Treasury Department and the Parliament are tied. You know, the -- so, I think, in that sort of sense, you know, there's not the same buy-in to BEPS that would have occurred. And also, BEPS, I think, is just reaching its natural progression, where countries now are starting to implement BEPS, often taking unilateral actions. It's -- the same forces that kind of led to BEPS are leading to the unilateral actions. So, I think, to a certain extent, this is just kind of returning to the norm.

You know, countries change their tax rules and other countries react to that, either because they like or -- either they don't like something another country did, so they change the rules in response to it, or they really like what a country did so they need -- they change the rules to correspond to that. So, each country always changes their rules, saying, "Yeah, this is going to make us more competitive," but everybody else wants to do the same thing.

Sony Kassam: So, John, you talked a little bit about companies with cross-border activity, thinking about restructuring. So, now that we have a lower corporate income tax rate of 21 percent, do you think U.S. companies will consider moving their operations to the United States and their intangibles back to the U.S. as well? And then, how do you think the new foreign-derived income rules factor into that?

John Harrington: Yeah. I mean, you make a good point. I mean, the corporate tax rate is plainly a lot lower. But you know, most companies had effective tax rates below, you know, the statutory rate. So, in terms of deciding whether your operations will be taxed less in the U.S. than where they are, you'd have to look at not just a lower rate, but also the changes to the tax base. You know, there's deductions that have been lost, and you know, in -- you know, whether it's interest deductions or the manufacturing deduction -- things like that -- you have to, you know, see how that changes your effective tax rate.

And then, also, there can be tax costs to moving operations. You know, if you're in a foreign country, there can be an exit tax. You could be recapture of credits if you try to move operations. And just like we'll talk about what the U.S. has done in, you know, intellectual property, some countries tax intellectual property movement being moved out as well. So, there could be a tax cost as well that you have to take into account. So, certainly probably countries should be -- you know, companies will be looking seriously at this, but they'll have to look at both the benefits and the foreign tax cost.

The foreign -- as for the foreign-derived intangible income, how that's going to impact things, it's quite -- I mean, that's -- it should be quite interesting. I think we talked about some of the interactive elements to this. You know, you can see that interacting with the global low intangible taxed income, the GILTI income, you know, where, you know, just kind of superficially, you know, you look at your, you know, the -- you can see how that interacts, but -- and we'll probably get to that, you know, later.

But I do want to point out in terms of moving intangible property, though, that one, you premove something into the U.S. just like Bill mentioned about, you know, sort of like if you're a corporation it's easy to get in, it's hard to get out. Same thing is true when it comes to intellectual property in the U.S. If you move intangible property in the U.S. you've got to be pretty sure that you're not going to move it back out. That was true before, it's even more true now, I think, under the rules at the time of taxation.

And then, second, if you do this to benefit from the foreign-derived intangible income, it also raises the question about how long, you know, how come you feel that those rules are going to continue to stay there? I mean, it's supposed to become less favorable over time. It's also something, which we talked about, could potentially be subject to a challenge, you know, by other countries, and then also it's the kind of thing that if there are political -- you know, if there's changes to the act to raise revenue or for political reasons, this is the one that might be taken into account. So, even if it's available now you got -- you don't know how long it would be available, at least in its present form.

Sony Kassam: Okay, and then you mentioned a little bit about GILTI, the global intangible low-taxed income rules. So what -- could there be any unintended consequences of that, such as companies wanting to increase their foreign manufacturing operations?

John Harrington: Yes. Yeah, because I mean, you can see where the two kind of, you know, interact between the FDII and the GILTI. And you know, just kind of superficially, I mean, you look at, say, tangible depreciable property. You know, you would -- it makes sense to have tangible depreciable property, you know, outside the United States, because that reduces the potential amount of GILTI, because that reduces your GILTI inclusion.

At the same time, you know, tangible depreciable property, you know, it's not helpful from a -- to have that in the U.S. if it's otherwise qualifying for the FDII, because that reduces the amount of your FDII, which is tax favored. So, just at least for a corporation that's subject to both GILTI and the FDII, there's incentive for your tangible depreciable property to be outside the United States. And so the employment that would be associated with that type of property, you know, there's incentive for it to be outside the U.S. You know, so, but you know, presumably that would, you know, that would affect that type of employment. There's other types of employment that potentially shifts to the U.S. for that similar reason.

But also, you know, corporations and individuals have different incentives as well. You know, GILTI is tax favored for domestic corporations. They get a deduction for GILTI. That's not true for, you know, for individuals if they own a foreign corporation. So, earning GILTI income is a lot harsher on individuals than it is for domestic corporations. So, the incentives are even stronger if it's an individual owning a foreign corporation than domestic corporation. I mean, it just fits in this whole interaction where, you know, the, you know -- it's, you know -- the answers are always yes with a very -- or no with a very long "but" following it. So, --

Sony Kassam: Since there's so much of the focus on intangibles and where it's placed and the value of them, do you -- how likely is it that U.S. companies will face more audits by foreign tax administrations?

John Harrington: You know, it's been an increasing risk, you know, on -- for several years now about, you know, increased audits from foreign countries, particularly, you know, regarding intangible property and, you know, country -- you know, I think country -- you know, companies are particularly concerned about it, you know, with as country-by-country reporting comes online. You know, so -- and so I think when there's risk other countries will plainly continue to go after it.

I think there's also -- you have to be concerned about potential double or multiple taxation because the U.S. rules for outbound transfer intangible have been tightened as well in terms of both repeal of the -- you know, the active conduct tests, you know, in terms of the, you know, for transfer of outbound assets including intellectual property, the fact that the value of intellectual property is -- intangible property is -- can be increased because of the new rules. So, greater U.S. taxation also -- if other countries are being aggressive means potential greater double taxation.

And it just goes, I think, just to the fundamental issue that because intangible property -- because it's intangible, you don't know where it's located, and that's created opportunities for companies, because they've often been able to tell a foreign government it's -- our intangible properties are located here or somewhere else and are low-taxed or no- or low-taxed jurisdiction. The flip side of that is it's hard to prove it's not there, either. So, if a country says we think it's here, we think you're using it in the U.S., there's a pretty, you know, it's hard to prove it's not.

So, you know, the intangibles -- they've always been sort of a double-edged sword. There's a lot of opportunity to reduce taxes by saying they're in a low-tax jurisdiction. There's now increasing risk that you're going to be subject to multiple taxation because they're viewed as being in lots of places, lots of high-taxed jurisdictions. So --

Joe Huddleston: Yeah, I'd like to say something on that also, John, because I think as your point is well taken as you talked about the increased importance of intangibles in the discussion. States are also very focused on intangibles in the base, embedded intangibles, and transfer pricing rules that everyone on the international and national level have relied on extensively. It's important to note that most states only consider the 482 rules as advisory, as guideposts. They do not consider themselves bound by 482 at all. And states are increasingly looking at transfer pricing issues, particularly in the area of intangibles and embedded intangibles, where they are almost invisible in the overall structure.

So, as states continue to look harder at transfer pricing issues, this issue of embedded intangibles, such as royalty structures, are increasingly important to the states, and you're going to see the states look more and more at these kinds of structures.

John Harrington: No, that's a good point, Joe.

Lisa Starczewski: One thing I wanted to piggyback on with respect to something that you said, John, and I think it's a really important point circling back to choice of entity and how complex that can be, I think the fact that you mentioned that so many corporations were not paying the effective tax rate.

And so, when you are, you know, looking at choice of entity and you're thinking about well, what rate will a C corp pay, you really do have to consider that they have a significant number of deductions and exclusions available to them to lower that effective tax rate, the dividends received deduction being a significant one. And depending on the type of business that you're conducting, you could end up in a better situation in a C corp for that reason alone. So, you know, again, just wanted to say that's an important point to keep, you know, to think about with respect to a lot of these planning opportunities.

Sony Kassam: Great. So, as a general question for everyone to wrap up, what aspects of the new tax law do you think have the most staying power? And then what aspects do you think would need to be revised because of unintended consequences?

Lisa Starczewski: Oh, do I get to start that one? [laughter]

Okay. Well, I think my answer is that I am concerned about unintended consequences, because I think what is really hard to get your head around is the way in which all of this is going to play together.

And when you look at any one thing in and of itself you can say, "All right, maybe I can make sense of this, I may need a little bit more guidance to fully understand it or fully apply it, depending on the facts, but all right. I think I know what they were trying to do." But they did a lot and they did a lot of different things. And when you look at how it all plays together, I think we are definitely going to have some consequences we didn't intend, they didn't intend.

And so, I do not know the exact answer to what is going to stay and what is going to go, but I will tell you that I do think that we are going to have consequences we didn't expect. Even just something as simple as business losses and the fact that they are so limited now out of pass-throughs, and that we also have this new interest limitation, that all of that's impacting basis, that -- you know, when you -- we have a very complicated set of tax laws, especially -- and I won't say especially, because we all work in complicated areas -- but pass-through taxation is incredibly, you know, complex. And what they've done here is add an entire other layer of complexity in hopes of simplification. [laughter] And under the guise of simplification.

So, I think it remains to be seen what stays and what goes, but I do think that we are going to have, you know, effects of this that we haven't even begun to think about or to realize.

Bill Alexander: I don't have really good psychic powers, but I wouldn't be surprised if 6 to 12 months into the next major recession we have loss carrybacks again. Typically that's something that you get -- until then it's going to be a little bit rough for struggling businesses. They're not going -- loss carryback is cash in hand. It's not just a tax asset, and their competitors are going to have an extra, you know, if they're profitable, an extra 14 cents on the dollar. So, their situation may be rough in the short run, but if things get really rough for the country as a whole, I wouldn't be surprised to see that return.

Other than that, I'm not sure I'm in the position to make a lot of predictions here. There will be things to be patched, but that doesn't necessarily mean they're going to go away.

John Harrington: Yeah, no, I mean, it's -- this is a little humbling, because I had a hard time predicting this bill came out looking the way it did, so predicting how it's going to change makes it kind of tricky.

But the -- you know, I think the question kind of has both a political and practical component. I mean, from a political standpoint they have to be -- you know, take into account the fact this was passed with only Republican votes, and so if the Democrats take one or both houses then you would expect there to be changes over the types of things they've criticized in the bill. You know, the corporate tax rates and the rate reductions on -- for -- two highest rate brackets or so.

From a practical standpoint, you know, again, this sort of is awfully cloudy crystal ball, but you know, to me the more novel and the more complicated the provision, the more likely it's going to have unintended consequences and need to be tweaked. So, there -- again, the international area I see the GILTI and the foreign-derived income -- intangible income and the deemed repatriation provision as being areas that probably fall in that category.

There's also a provision that probably had conceptual appeal, but I'm not sure the consequences were fully thought out. There's changes to constructive ownership rules for control of foreign corporations. You know, the distinction between liquid and illiquid assets and the deemed repatriation and the new rules for transfers valuing intangible assets. I mean, a lot of those seem like conceptual ideas. Turning that into sort of specifics is going to be kind of an issue.

Richard Franklin: So, I'd sort of answer your question in a slightly different way, at least in the context of the gift, estate, and GST tax system. I think the act sort of demonstrates that they are going to be enduring, that they're not repealed. And if you look at the landscape there and historically the modern estate tax has been around for 101 years and it's been gone for one year -- less than 1 percent out of that period of time.

And we look at first world countries. The United States, by some metrics, is the most unequal country for income and wealth inequality. So, just looking at the landscape, to me, says the gift, estate, and GST tax system will endure and some people are -- you know, repeal is alluring, but I think it's ephemeral and it's imprudent if your idea is you want to preserve family wealth to rely on the vagaries of, you know, our government about keeping or not keeping the federal estate tax, and the moral of the story is to plan.

So, that's what I would say about -- at the state level, it's also interesting, you know, what will be enduring with them. The District of Columbia's estate tax exemption was $2 million last month. It's on autopilot, is now $11.2 million for this year. So, you know, harking back to what states will do, I doubt that's what they intended. And even the carryover basis there will be lots of games that people play with increasing the basis of assets, which not only will affect the federal system, but the states as well. So what, you know, that -- whether that will be enduring is another issue.

Joe Huddleston: Now, I think that Lisa began this discussion by reminding us all that we're two or three weeks into this, and her view of unintended consequences is very significant, I believe, here.

One thing that I believe will endure is that the relative significance of state and local taxes is increased, both for the individual and for the corporations, and the scattershot approach that the states have always used will continue to be a huge problem for both corporate and individual planning. Some of the unintended consequences could well reach into the area of both corporate and individual migration.

Do businesses, do individuals stay in the states they're in? Or if there are dramatic shifts in the relative tax burden, do they begin to find other places to have their headquarters or to live? If you have an effective tax burden in California, 50 or 60 percent, when the same entity can be in Tennessee and have a substantially 30 points less effective tax rate. There's some pretty strong incentives for both corporate and individual migration.

Beyond that, we see that some of the impacts at the state and local level can impact how municipalities or governments are able to fund themselves, how they are able to issue bonding and whether or not the bond companies, the people who are providing public finance, are going to have to make adjustments relative to the calculations that have changed for them. And I'll suggest to you that they will be making those adjustments.

So, there are a lot of unintended consequences out there that we're just beginning to come to grips with and just beginning to question. So, Lisa's absolutely right: It's early. Ask these same questions next year.

Colleen Murphy: Well, thanks so much, everyone for taking the time, and we definitely will follow up with you as this all sort of shakes out over the next months and coming years.

Bill Alexander: Thanks for having us.