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5 Biggest Tax Policy Changes Of 2015

By **Eric Kroh**

Law360, New York (December 21, 2015, 6:27 PM ET) -- The Organization for Economic Cooperation and Development's ambitious base erosion and profit shifting project, new rules governing the audits of large partnerships and Congress' massive $622 billion tax extenders deal were among some of the largest tax policy stories of 2015.

OECD BEPS Project

After two years of deliberation, the OECD in October released its recommendations to stem tax base erosion and profit shifting, with implications for areas as diverse as transfer pricing, tax treaty abuse and international arbitration.

The recommendations are meant to effect a shift in the international tax system to prevent multinational corporations from exploiting holes in the tax laws to amass so-called stateless income that is not taxed by any country. American companies, however, saw the BEPS project as a thinly veiled scheme by OECD countries to tax a larger share of the income of U.S.-based multinationals such as Apple Inc. and others that have thrived in the increasingly global economy. And U.S. tax officials complained that implementing the rules would erode the U.S. tax base.

Under the BEPS regime, countries will have access to an unprecedented amount of information on companies' economic activity and transfer pricing operations, and tax practitioners said the recommendations when carried out will require American companies to change their operations to avoid running afoul of new tax laws.

“The BEPS reports encourage tax administrators to try to look to substance rather than just form,” David Fischer of Crowell & Moring LLP said.

With the bulk of the OECD's work on the project complete, tax practitioners and stakeholders will now be watching how the recommendations are adopted by member countries and are bracing for a rise in disputes as countries seek to increase their share of the tax pie.

Partnership Audit Rules

Tucked inside of a two-year budget bill signed into law in early November was an overhaul of partnership audit and tax collection rules that will affect nearly every partnership in the country.

In a broad sense, the new law repeals the Tax Equity and Fiscal Responsibility Act of 1982 and ushers in a new regime in which tax adjustments are made at the partnership level rather than at the level of the individual partners.

Partnerships have long posed a challenge for the IRS because of their multiple layers of complexity and the agency's limited resources, but the law is expected to make the daunting task easier — as well as bring in nearly $10 billion in additional revenue over 10 years, according to estimates from the Joint Committee on Taxation.

Perhaps the biggest shift under the new law will be that current partnership members will by default be liable for taxes imposed by the IRS on the partnership's previous tax returns, rather than the partners who were members during the year in question. That shift will change the way that partnership investors will think about that purchase, since now they could be on the hook for taxes on positions taken by the partnership years in the past, according to Crowell & Moring LLP's Jennifer A. Ray.

The new audit regime will not take effect until 2018, and tax practitioners will be keeping an eye on the rulemaking process to see exactly how the law will be implemented, Ray said.

"There's a lot of work to be done by IRS," she said.

Tax Extenders

After years of lawmakers failing to reach an agreement on permanent policy for the so-called tax extenders — a set of 50 or so targeted tax benefits — tax practitioners and their clients received an early Christmas present when congressional leaders announced a deal to permanently extend several of the most popular extenders days before recessing for the year.

The Protecting Americans From Tax Hikes Act of 2015 makes permanent several popular tax incentives for businesses including the research credit, increased expensing limits and a provision that defers the taxation of active financing income earned by foreign subsidiaries.

Energy tax breaks, including the renewable energy production tax credit and incentives for the production of renewable fuels, were renewed for two years, through the end of 2016, under the act. The PATH Act passed as part of an omnibus spending bill that also made wind energy and solar facilities eligible for a tax credit through the end of 2019. The deal also delayed for two years the "Cadillac" tax on high-cost health insurance plans that was scheduled to take effect in 2018 and placed a two-year moratorium on the medical device excise tax for 2016 and 2017.

Though the law would largely forbid tax-free spinoffs of real estate investment companies, it includes an exception for companies that sought the IRS' blessing on such transactions prior to Dec. 7, 2015, meaning planned deals by Hilton Worldwide Holdings Inc. and others are not at risk.

Victor Hollender of Skadden Arps Slate Meagher & Flom LLP underlined the PATH Act's easing of restrictions on foreign investment in the U.S. real estate market imposed by the Foreign Investment in Real Property Tax Act of 1980.

While there is still room to expand on FIRPTA reform, the loosening of the restrictions is a "step in the right direction" and represents "a small victory for tax neutrality," Hollender said.

Inversions Notice

Following up on an announcement made in 2014, the IRS in November said it was planning to release further regulations to tamp down on corporate inversions to deter American companies from merging with competitors in low-tax jurisdictions.

Under the forthcoming rules, a foreign acquiring corporation would be required to be subject to tax as a resident of the foreign country or face adverse tax consequences, the IRS said. The agency said it would also write rules to address certain post-inversion tax avoidance transactions. The announcement came just days before U.S. pharmaceutical giant Pfizer said it was combining with Irish drugmaker Allergan in a $160 billion inversion deal.

In the wake of the inversions guidance, officials from the U.S. Department of the Treasury said they were taking aim at transactions such as the one contemplated by Pfizer, but that they would need lawmakers to write legislation to truly address the problem.

Peter J. Connors of Orrick Herrington & Sutcliffe LLP said the Pfizer inversion may be looked at as the "straw that broke the camel's back" and signal to Congress that an overhaul of the U.S. international tax regime should be a top priority.

"You can only do so much with statutes that weren't really designed to correct the problems that are in the system," Connors said.

MLP Guidance

The IRS in May released proposed regulations on qualifying income for master limited partnerships that in some cases redraw the lines for activities that qualify for the preferential tax status.

The regulations are wide-reaching, not only addressing service providers to the oil and gas industry but also providing an exhaustive list of what activities qualify for MLP treatment along the entire process of mineral and natural resource production, from the exploration, development, mining and processing of resources to refining, transportation and marketing.

In some cases, the IRS has narrowed the definition of what qualifies as MLP income, withholding the status from activities that the agency previously said had qualified in individual letter rulings.

At an October public hearing on the proposed regulations, several MLPs **criticized the guidance**, arguing the agency has turned its back on years of in-house rulings and caused investors to scatter.

Tax practitioners and stakeholders will be watching to see whether the IRS will take the criticisms to heart and amend the forthcoming final regulations to be more inclusive.

--Editing by John Quinn and Kelly Duncan.