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Tax Regulation And Legislation To Watch In 2016

By **Eric Kroh**

Law360, New York (December 24, 2015, 8:38 PM ET) -- In 2016, tax practitioners will be keeping a close eye on the implementation of the Organization for Economic Cooperation and Development's anti-tax base erosion plan, guidance on inversions from the U.S. Department of the Treasury and the Internal Revenue Service, and the prospects for an overhaul of the tax code in Congress.

BEPS Implementation

In 2015, the OECD completed its ambitious two-year project to crack down on tax base erosion and profit-shifting with the release of a set of recommendations to close international tax loopholes, and tax attorneys and stakeholders will turn their attention in 2016 to how the recommendations are adopted by countries throughout the world.

Of particular importance to U.S. multinationals will be a requirement to submit country-by-country reports of their income, taxes and other economic activity in each jurisdiction in which they do business. Country-by-country reporting is the only part of the BEPS plan for which Treasury has committed to writing regulations.

"If you're a U.S.-based multinational, you're really monitoring everything that's going on out there in the different countries," Joseph Calianno of BDO USA LLP said. "There's a lot of moving parts around the world."

The recommendations are not binding, and tax practitioners and multinationals fear that countries will take a pick-and-choose approach to adopting the provisions that are most beneficial to them, leading to a patchwork of policies. Some early-adopter countries such as the U.K. have already drafted legislation to put some of the changes in place.

Inversions Guidance

In November, Treasury and the IRS issued another notice announcing that further rules were forthcoming to discourage American companies from merging with competitors in low-tax jurisdictions in so-called inversion transactions.

Under the forthcoming rules, a foreign acquiring corporation would be subjected 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 followed a similar warning issued in late 2014 that said the IRS would craft regulations to slash the benefits of corporate tax inversions by prohibiting so-called hopscotch loans and other tax maneuvers.

But the IRS has yet to issue the regulations under the formal notice and comment rulemaking procedures, and the rules will not be binding until they are finalized. The agency has said the regulations will apply to deals that close after Sept. 22, 2014.

Tax practitioners and multinationals will be waiting for the release of proposed rules to implement the inversions regulations so they can begin planning in response to them. Stakeholders will also be following Congress to see if lawmakers will write legislation to address inversions as the Obama administration has said its authority to curtail the transactions are limited under current law.

Tax Reform

New House Speaker Paul Ryan, R-Wis., former chairman of the chamber's tax committee, has said he wants to pass a comprehensive revamp of the tax code in the House of Representatives in 2016.

Tax reform has been a priority for Ryan going back to his days as chairman of the House Budget Committee. He has expressed support for a plan that would allow U.S. companies to repatriate overseas profits at a significantly reduced corporate tax rate, use the additional tax revenue to prop up the highway fund and reduce the top tax rate for individuals and corporations to 25 percent while eliminating the majority of specialized tax deductions and credits in the code.

Many tax attorneys are skeptical, however, that major changes to the tax code can be enacted into law next year. It has been historically difficult to enact major legislation in an election year when lawmakers' attentions are turned elsewhere.

Still, tax reform talks could set the stage for more significant negotiations once a new president takes office.

"I don't think it's going to happen in 2016," Calianno said. "The earliest we would likely see something significant on it is 2017."

IRS Budget

The IRS' operating budget has been cut by more than $1 billion since 2010, and the strain on the agency's resources has begun to show, with services being eliminated and wait times for the dedicated tax practitioner hotline stretching to 30 minutes or more.

IRS Commissioner John Koskinen has warned about the threats posed by a shrinking budget, but his pleas have fallen on deaf ears in the Republican-controlled Congress, which is still fuming over the recent controversies surrounding the agency's treatment of conservative social welfare groups.

David Newman of Mitchell Silberberg & Knupp LLP said not enough attention is being paid to the problem, which threatens to upend the entire tax system that rests on the voluntary reporting of tax obligations. The urgency of the problem was underlined by a letter penned by seven former IRS commissioners who asked Congress to increase the agency's budget, Newman said.

High levels of tax compliance in the U.S. have been dependent on the fact that the IRS has enough auditors to watch over the system, Newman said. If the public knows that the agency is understaffed, more people may feel they can get away with cutting corners or outright cheating on their taxes, he said.

“You can’t keep cutting the budget and therefore cutting the number of sticks out there,” Newman said. “You can’t keep doing that and expect people to still voluntarily comply with their tax obligations.”

LB&I Reorganization

In 2015, the IRS announced a reorganization of the Large Business and International Division, which oversees the nation’s largest multinational corporations. The agency envisions winding down the coordinated industry case, or CIC, program, which places large multinational companies under continuous audit by a rolling team of examiners, and moving toward an approach that will target areas for examination based on compliance risks.

Under the changes set to be rolled out beginning in early 2016, the division, which examines companies with assets greater than $10 million, will be organized into nine groups focusing on four geographical areas and five practice areas, including pass-through entities, enterprise activities, cross-border activities, international individual compliance, and treaty and transfer-pricing operations.

The reorganization is a sign of the IRS’ slimming budget, according to David J. Fischer of Crowell & Moring LLP. The agency is trying to bring its more limited resources to bear on the most pressing tax issues, which tend to be in the international arena, he said.

“The IRS is trying to figure out how to make use of their fewer resources to still do their job,” Fischer said.

Fischer said the change also represents a shift at the agency to focus on transfer-pricing issues, which have caught the attention of tax administrations around the world as companies come up with innovative ways to shift income from country to country.

--Editing by Christine Chun and Philip Shea.
