



US TAX UPDATE: BASE EROSION & ANTI-ABUSE TAX

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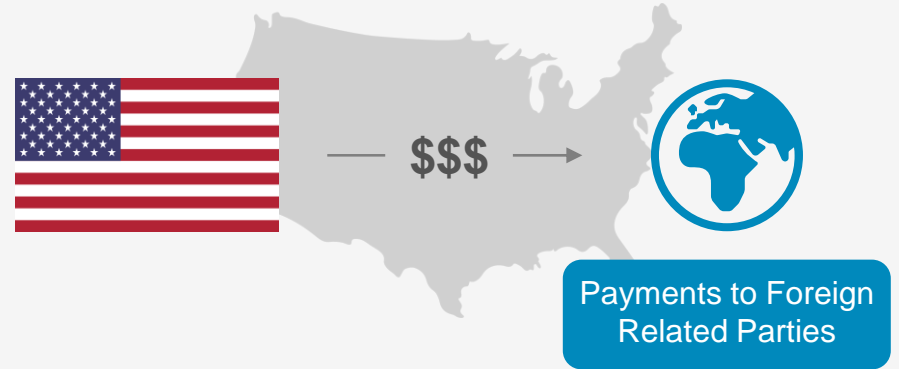
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BASE EROSION AND ANTI-ABUSE TAX



What is the Base Erosion and Anti-Abuse Tax (BEAT)?

- ❖ The BEAT is a new minimum tax targeted at US multinationals that make base eroding payments (ie certain deductible payments to related foreign parties).



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Who does the BEAT apply to?

- ❖ The BEAT applies to US multinational corporations who:
 1. Have average annual gross receipts in excess of **\$500 million** over the past three years
 2. Make base eroding payments in **excess of 3%** of the aggregate allowable deductions in the current taxable year.

BEAT Impact Profiles

- ❖ Large US corporations
- ❖ IT services – shared service center
- ❖ Customer base in US/value chain outside US
- ❖ Tech/cloud services/pharma – IP company.

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Good Payments v Bad Payments

- ❖ The BEAT targets outbound related-party transactions that strip earnings out of the US via deductible payments, and are generally defined as follows:

Good Payments

- ❖ Payments that are classified as a reduction to gross revenue
- ❖ Payments that qualify for the services cost method.

Bad Payments

- ❖ Deductible outbound payments to a foreign related party that are not considered 'good payments'.

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Cost of Services v Cost of Goods Sold ('COGS')

- ❖ Payments that are considered a reduction to gross revenue (COGS), are not considered base erosion payments. The following are some examples of what may be included in COGS, and thus are excluded from the BEAT:

Costs capitalised into inventory.



Royalties that may be properly capitalised into inventory.



The BEAT relies on existing tax law to determine whether a payment is treated as a deduction to which the BEAT would apply.



- ❖ Payments that are considered Costs of Services are not considered a reduction of gross revenue, and are thus classified as a base erosion payment.

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Services Cost Method (SCM)

- ❖ The cost portion of deductions for service payments made to non-US related parties that qualify for SCM, a concept under US transfer pricing rules, are specifically identified as an exception under BEAT
- ❖ Qualifying for SCM:

Services performed must be eligible for SCM

Median benchmark for services must not exceed a **7% mark-up**.



Services performed cannot be explicitly excluded from SCM pursuant to applicable published guidance. For example, R&D and sales activities are explicitly excluded.



- ❖ Only the costs associated with these services may be excluded from the BEAT calculation
 - The mark-up on these services can give rise to BEAT tax liability
 - Creates the potential for double taxation of the same mark-up.

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GLOBAL MANUFACTURER

US Corporate Income Tax (\$100 million x 21%): \$21 million

Base Erosion and Anti-Abuse Tax

Modified Taxable Income (\$100 million + \$150 million + \$50 million) \$300 million

MTI Liability (10% of MTI)* \$30 million

(Less) US Corporate Income Tax \$21 million

BEAT Liability \$9 million

Total US Tax Liability (\$21 million + \$9 million) \$30 million

*Base Erosion Tax Rate 5% in 2018, 10% in 2019-2025, and 12.5% for years after 2025.



US Taxable
Income: \$100 million



Related
Party

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GLOBAL SERVICES PROVIDER	
US Corporate Income Tax (\$100 million x 21%):	\$21 million
Base Erosion and Anti-Abuse Tax	
Modified Taxable Income (\$100 million + \$200 million + \$150 million + \$50 million)	\$500 million
MTI Liability (10% of MTI)*	\$50 million
(Less) US Corporate Income Tax	\$21 million
BEAT Liability	\$29 million
Total US Tax Liability (\$21 million + \$29 million)	\$50 million

*Base Erosion Tax Rate 5% in 2018, 10% in 2019-2025, and 12.5% for years after 2025.



US Taxable
Income: \$100 million



Related
Party



**SPEAKER
PROFILES**

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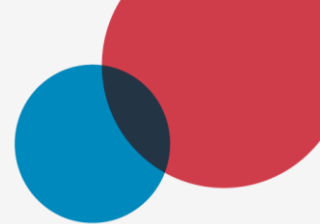
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Marc Alms is a Managing Director with Alvarez & Marsal Taxand, LLC in New York, focusing on transfer pricing. He has twenty years of experience assisting both public and privately-held clients. Mr. Alms' background includes leading teams in the evaluation of intercompany transactions to determine whether they meet applicable US and foreign transfer pricing regulations, including the latest OECD BEPS guidelines. Having worked and lived in different countries over the course of his career, he has significant experience providing clients practical advice in their transfer pricing arrangements and helping to resolve international tax controversy matters. Mr. Alms earned a Juris Doctor from the University of Pennsylvania Law School and a bachelor of arts degree in history from the University of California, San Diego. He was admitted to the bar in California and is a member of the California State Bar Association.

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Nicolaus McBee is a Senior Director with Alvarez & Marsal Taxand, LLC in New York. With over eight years of international and federal tax experience, Mr. McBee provides strategic and practical tax advice to clients. His expertise includes foreign currency issues, global supply chain planning/restructuring, international reorganisations, intangible property planning, holding company planning, international compliance, check-the-box planning and cross-border acquisitions. Prior to joining A&M, Mr. McBee spent two years with the Internal Revenue Service (IRS) where he assisted taxpayers with domestic and international tax compliance. Mr. McBee earned a J.D. from Thomas Jefferson School of Law and a master's degree in taxation (LL.M.) from Boston University. He is a licensed attorney in the state of Illinois. He has contributed to several articles and reports discussing international tax issues including intangible property planning, foreign tax credit utilisation, US international issues surrounding technology companies and tax reform.