Guide to U.S. Taxes presented by PwC

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pwc

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This guide is current as of this December 2018, and is not updated regularly.

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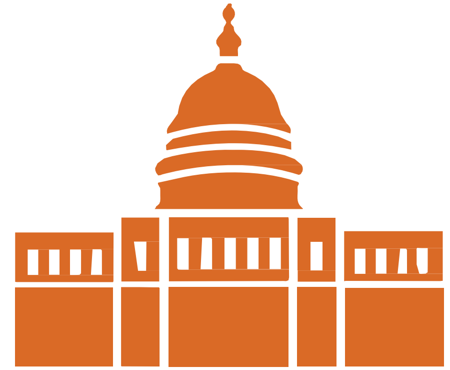


Federal Income Tax

Who is subject to US Income Tax?

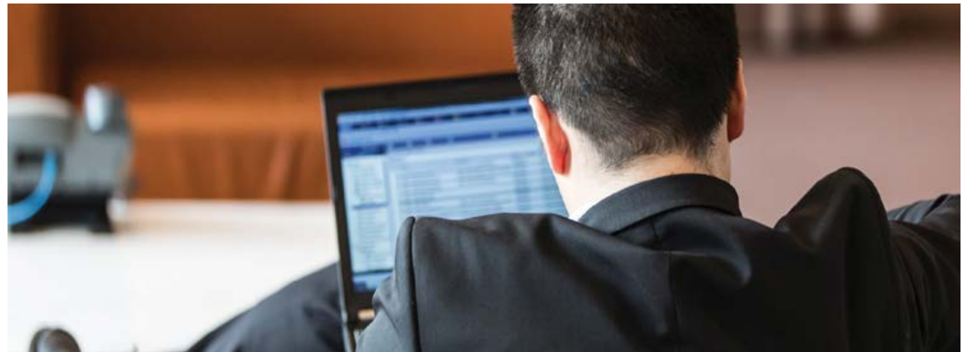
All US corporations must file an annual federal corporate tax return.

What do I need to file?

Form 1120, the annual corporate tax return, is used to determine your taxable income and federal tax liability. In addition to the 1120, there are other informational forms that may be required. For example, Form 5472, is required to be filed by a foreign owned, US company.

How can my taxes be reduced?

Numerous credits to reduce tax are available, including credits for certain research activities. If a company is in losses in tax years ending before January 1, 2018, the losses may be carried back two years and, if not fully used, carried forward 20 years. NOLs generated in tax years ending after December 31, 2017, generally may not be carried back and must instead be carried forward indefinitely; for such NOLs the deduction is limited to 80 percent of taxable income (determined without regard to the deduction).



How much tax will I owe?

US corporations will be taxed at a standard rate on their taxable income. US taxable income is based on the corporation's gross receipts less various business expenses (e.g., cost of goods sold, salaries and wages). For tax years beginning after December 31, 2017, taxable income of US corporations is subject to a flat rate of 21%.

When do I have to file my taxes?

A corporate taxpayer must file their annual tax return by the 15th day of the fourth month following the close of its tax year. A taxpayer can obtain a six-month extension to file its tax return, provided it timely and properly files Form 7004, and pays the full amount of any tax due by the original due date. For example, if a corporate taxpayer whose year end is December 31, 2018, properly obtains an extension, its 2018 federal tax return that would normally be due on **April 15, 2019** is extended to be due on **October 15, 2019**.

When are tax payments due?

All of your federal income taxes are due by the 15th day of the third month following the close of the tax year, regardless of an extension granted for filing the actual return. Following your first tax year in the US, you may be required to make estimated tax payments at the close of each quarter. Companies expecting a taxable profit for the year should consider whether or not estimated taxes are owed, and how much is required to be paid in the year.

State Income Tax

What do I need to file?

Each state in the US has their own tax system that requires annual filings depending on your activity in the state. These filings are separate from the US federal return submitted to the IRS, and are submitted to tax authorities of the individual states. The tax rates vary across the states but generally result in an additional income tax of up to 10%.

Federal vs. State taxable income?

The starting point for determining US state taxable income generally is an entity's federal taxable income. However, there are several items that may be treated differently for state taxable income purposes (e.g., depreciation, state taxes paid, interest deductions and charitable contributions). The states will then apportion taxable income according to the company's relative presence in the state using various factors (e.g., sales, property, payroll).

Which states do I need to file?

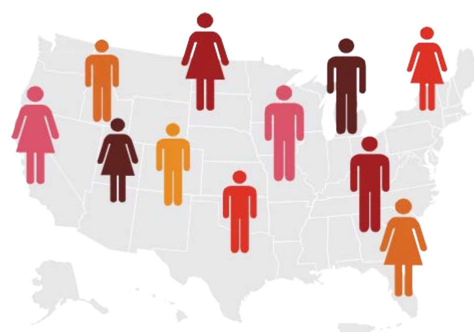
A state generally may impose its tax on an entity to the extent a sufficient 'nexus,' or taxable connection, exists between the entity and the state. Forty-four US states impose a corporate income tax, and a company can be subject to income tax in as many states as they have nexus. Each state has their own criteria for nexus but, in general, owning property, paying for rental property, or storing inventory in a state are examples of situations that would lead to a filing requirement in that state. Other factors, such as the location of employees and sales activity, can also be considered depending on the state.

When are state taxes due?

Most states require the corporate taxpayer to file their annual tax return by the 15th day of the third or fourth month following the close of its tax year. Some states permit a five or six-month extension to file the return, provided the taxpayer timely and properly files the extension form for that jurisdiction and deposits the full amount of any tax. Similar to federal income taxes, most require tax-paying corporations to submit estimated taxes on a quarterly basis.

Other state tax issues

A handful of states impose a franchise or gross receipts tax in addition to or in place of an income tax, reported on the annual tax return. There may be situations in which a company is not required to pay an income tax, but still may be subject to a filing requirement and payment of a franchise, capital, or gross receipts tax. These taxes are a way for states to tax companies based on gross receipts or balance-sheet capital rather than taxable income.



Transfer Pricing

Transfer pricing regulations govern how related entities set prices for the transfers of goods, intangible assets, services, and loans. The US looks to what is known as the arm's length standard to determine the appropriate price.

If you have multiple entities within your structure that interact with each other, transfer pricing may be applicable to you. If multiple related parties within the US have transactions, there may also be state transfer pricing issues to consider.

The arm's-length standard is met if the results of a related party transaction are consistent with results that would have been realized if unrelated parties had engaged in a similar transaction under similar circumstances. Analyzing comparables in your industry is important for appropriate transfer pricing and tax compliance.

The IRS may adjust your profits and taxes you owe, as well as impose penalties for incorrect transfer pricing. Having your transfer pricing positions accurately documented can help you avoid penalties.

Examples of Transfer Pricing considerations:

Foreign parent sells inventory to a US subsidiary which will be used in production of the subsidiary's inventory.

- Is the amount charged by the foreign parent the same amount that they would have charged to an unrelated third party?
- If IRS determines the purchase price was not at 'arm's length' then an adjustment will be required on the purchase price

Foreign parent licenses software to be used by the US subsidiary

- What rate does the foreign parent charge the US subsidiary for use of the software license?
- If the IRS determines the rate being charged is too high, when considering the 'arm's length' standard, the deduction taken in the US may be adjusted.

US Subsidiary provides sales support to foreign parent, in the US

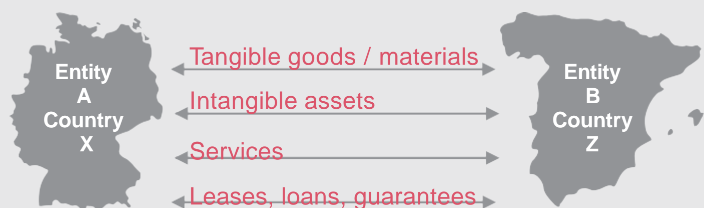
- Does the US Subsidiary charge the foreign parent for the services they are providing?
- If so, is the rate being charge appropriate under the 'arm's length' standard?
- If the neither are considered, the IRS may consider an adjustment and impute income in the US for the services being provided, and the income would be taxable

US subsidiary uses the name brand of the foreign parent

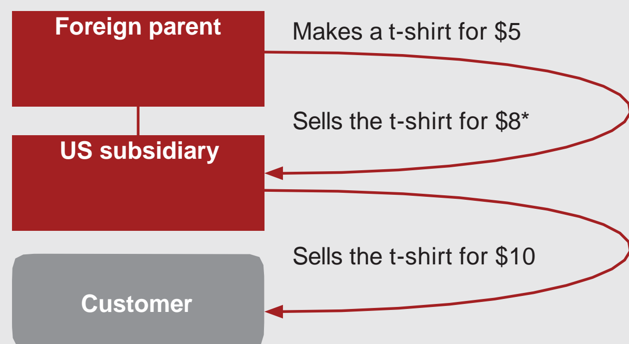
- What royalty payment does the foreign parent charge the US subsidiary for use of the brand name?
- If the IRS determines the rate being charged is too high, when considering the 'arm's length' standard, the deduction taken in the US may be adjusted

Transfer pricing in practice

- A and B are related parties in different tax jurisdictions.
- Tax authorities can be concerned that differences between jurisdictional tax rules and rates create the opportunity for related entities to shift income from a higher tax jurisdiction to a lower tax jurisdiction (true for cross border transactions both internationally and between states).
- To deal with this concern, transfer pricing regulations govern the price when items or services are transferred between related entities.



Example of how profits can be taxed



Entity	Sales	Cost	Profit
Foreign Parent	$8	$5	$3
US Subsidiary	$10	$8	$2

In this simplified example, the profit subject to tax in the US ($2) represents its sales less cost of purchasing the T-shirt. The US subsidiary may have other operating expenses that it can also deduct to further reduce taxable income.

* Price must be similar to what the foreign parent would charge to unrelated parties in the US.

Other Taxes

Indirect Taxes

- There is no federal value added tax (“VAT”) or similar consumption tax. As a result indirect tax generally is a state tax issue.
- The most common indirect taxes are a state's sales and use tax, and franchise taxes.

Sales and Use Taxes

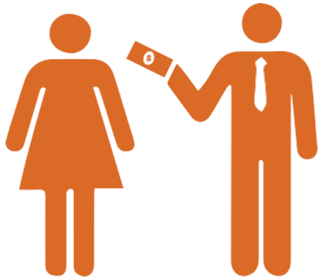
- Generally, once a company has nexus to a state with respect to sales and use taxes, that company must register with the state’s tax department, file sales tax returns, and pay its sales tax liabilities.
- Depending on the volume of sales, the company may be required to file returns on an annual, quarterly, or monthly basis. Physical presence is not required for the imposition of sales and use tax by certain states.
- Generally, sales tax is imposed on retail sales, leases, rentals, barters, or exchanges of tangible personal property and certain enumerated services unless specifically exempted or excluded from tax.
- Sales tax generally is imposed in the jurisdiction in which the ‘sale’ occurs. The definition of ‘sale’ differs from jurisdiction to jurisdiction; however, the definition generally includes both (1) consideration and (2) transfer of title, right to use, or control (possession) in the case of tangible property and completion of the service act in the case of a service.

Delaware Franchise Tax

- Any corporation that is incorporated in Delaware (regardless of where you conduct business)must file an Annual Franchise Tax Report and pay Franchise Tax for the privilege of incorporating in Delaware.
- Franchise Taxes and annual Reports are due no later than March 1st of each year.
- The Delaware Franchise Tax will range from $175 to $200,000 depending on the amount of the company’s authorized shares. For example, a corporation having 10,000 authorized shares will have a tax of $250. Generally, the more shares the US corporation has, the higher the Franchise Tax (with a maximum annual tax of $200,000). An Annual Report filing fee of $50 is also required.

The United States has separate federal, state, and local government(s) with taxes imposed at each of these levels. Taxes are levied on income, payroll, property, sales, withholding, as well as various fees (see detailed descriptions of each below). These taxes are constantly evolving to keep up with new industries, to meet the changing needs of a state, or one of countless other factors. For example, on June 21, 2018, the US Supreme Court in South Dakota v. Wayfair overturned prior Court decisions and ruled that a physical presence is not required for the imposition of sales and use tax. This decision will have far-ranging tax and accounting impacts on companies. Therefore as a business owner/member, it is important to be aware of the constant changes, and account for them to reduce your potential risk.

Other Taxes *(continued)*



Withholding Taxes

- People and companies making payments such as interest, dividends, and royalties, to foreign people or foreign companies generally must withhold 30% of the payment amount as tax withheld at source.
- A lower rate of withholding can apply if the payee is eligible for a reduced rate under a tax treaty or by operation of the US tax laws. The ability to apply a reduced rate requires valid documentation evidencing the foreign payee's eligibility for a lower rate of withholding. For further details on applicable tax treaties, please refer to the Addendum.
- Any taxes withheld on payments made to foreign payees must be reported to the IRS before March 15 following the calendar year in which the income subject to reporting was paid. An extension of time to file can also be obtained.

Payroll Taxes

- A payroll tax obligation will exist for a US company if it has employees.
- All payments for employment within the US are wages subject to (1) federal income tax withholding, (2) Federal Insurance Contributions Act (FICA) taxes (i.e., social security and Medicare), and (3) the Federal Unemployment (FUTA) tax, unless an exception applies.
- The employer must pay and withhold social security taxes equal to 6.2% of wages for the employer and 6.2% for the employee, up to $132,900 of wages in 2019, and Medicare taxes equal to 1.45% for the employer and 1.45% for the employee.
- The employer generally must file quarterly and annual employment tax returns and annual wage statements (Forms W-2) in its name and employer identification number unless such statements are filed by a properly authorized third party.

Further guidance

For a more comprehensive discussion of US Taxation, please see the following section, "A guide to the key US tax issues."

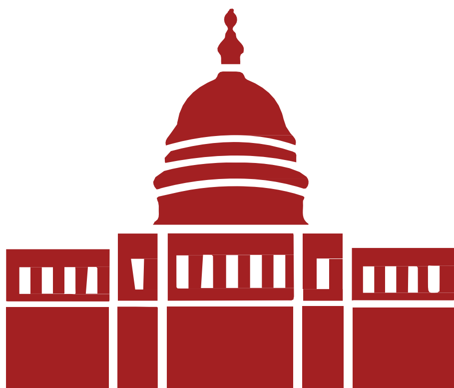
Contact us

To schedule a discussion with a PwC professional on general US tax issues, please contact pwc@stripe.com

A guide to the key US tax issues

2018

Federal tax issues



Taxes on corporate income

1. Corporate income tax

All US corporations are subject to federal income taxes. Generally, US taxable income is based on your gross receipts less various business expenses (e.g., cost of goods sold, salaries and wages).

The Tax Cuts and Jobs Act significantly revised the federal tax regime. The Act permanently reduced the 35-percent corporate income tax rate to a flat 21-percent rate for tax years beginning after December 31, 2017.

2. Alternative Minimum Tax (AMT)

AMT previously was imposed on corporations other than small corporations (generally those not having three- year average annual gross receipts exceeding $7.5 million). The tax was 20% of alternative minimum taxable income (AMTI) in excess of a $40,000 exemption amount (subject to a phase-out). AMTI was computed by adjusting the corporation's regular taxable income by specified adjustments and 'tax preference' items.

The Act repealed the corporate AMT effective for tax years beginning after December 31, 2017, and provides a mechanism for prior-year corporate AMT credits to be refunded by the end of 2021.

Tax Reform

1. Base-erosion and anti-abuse tax (BEAT)

The Act creates a new US federal tax called the 'base erosion and anti-avoidance tax,' or BEAT. The Act targets US tax-base erosion by imposing an additional corporate tax liability on corporations (other than RICs, REITs, or S corporations) that, together with their affiliates, have average annual gross receipts for the three-year period ending with the preceding tax year of at least $500 million and that make certain base-eroding payments to related foreign persons during the tax year of three percent (two percent for certain banks and securities dealers) or more of all their deductible expenses apart from certain exceptions

The most notable of these exceptions are the net operating loss (NOL) deduction, the new dividends received deduction for foreign-source dividends, the new deduction for foreign-derived intangible income (FDII) and the deduction relating to the new category of global intangible low-taxed income (GILTI), qualified derivative payments defined in the provision, and certain payments for services.

The BEAT is imposed to the extent that 10 percent (five percent for the 2018 calendar year) of the taxpayer's 'modified taxable income' — generally, US taxable income determined without regard to any base-eroding tax benefit or the base-erosion percentage of the NOL deduction — exceeds the taxpayer's regular tax liability net of most tax credits. (The above percentages are changed to 11 percent and six percent, respectively, for certain banks and securities dealers.)

A base-eroding payment generally is any amount paid or accrued by the taxpayer to a related foreign person that is deductible for acquiring property subject to depreciation or amortization, or for reinsurance payments. The category also includes certain payments to 'expatriated entities' under the anti-inversion rules of Section 7874.

The provision is effective for base-erosion payments paid or accrued in tax years beginning after December 31, 2017. For tax years beginning after December 31, 2025, the percentage of modified taxable income that is compared against the regular tax liability increases to 12.5 percent (13.5 percent for certain banks and securities dealers) and allows all credits to be applied in determining the US corporation's regular tax liability. Special rules apply for banks, insurance companies and 'expatriated entities.'

2. Mandatory deemed repatriation 'toll charge' (Section 965)

The Act uses the mechanics under subpart F to impose a one-time 'toll charge' on the undistributed, non-previously taxed post-1986 foreign E&P of certain US-owned foreign corporations as part of the transition to a new territorial regime. The toll charge, found in revised Section 965, is reduced by a deduction computed in a manner that ensures a 15.5-percent effective tax rate on earnings represented by 'cash' and an 8-percent effective tax rate to the extent the earnings exceed the cash position..

Taxpayers will need to analyze numerous issues before actually repatriating their earnings. While the deemed mandatory repatriation under Section 965 will eliminate (or substantially reduce) any additional US tax cost on the repatriation of earnings, local country implications — such as the imposition of withholding tax on cash dividends or the lack of sufficient distributable reserves in certain jurisdictions — could affect such repatriations.

Other Federal Taxes

1. Sales and use taxes

The US does not impose a federal sales tax, use tax, or value-added tax (VAT). For information related to sales and use taxes that are imposed by the States, please refer to Section II. State and Local Tax Issues.

2. Customs duties and import tariffs

All goods imported into the United States are subject to customs entry and are dutiable or duty-free in accordance with their classification. The classification also identifies eligibility for special programs and free-trade agreement preferential duty rates.

When goods are dutiable, ad valorem, specific, or compound duty rates may be assessed. An ad valorem rate, the type most often applied, is a percentage of the value of the merchandise. A specific rate is a specified amount per unit of measure (weight or quantity). A compound rate is a combination of both an ad valorem rate and a specific rate. US Customs and Border Protection (CBP) requires that the value of the goods be properly declared regardless of the dutiable status of the merchandise.

Payment of duty becomes due at the time an entry is filed with CBP. The obligation for payment is on the person or firm in whose name the entry is filed, the importer of record. The importer of record has a legal obligation to exercise reasonable care in all aspects of its importing activity.

3. Excise taxes

The US government imposes excise taxes on a wide range of goods and activities, including air travel, gasoline and diesel fuel used for transportation, and manufacturing of specified goods.

The excise tax rates are as varied as the goods and activities on which they are levied.

Payroll Taxes

All payments for employment within the United States are wages subject to (1) federal income tax withholding, (2) Federal Insurance Contributions Act (FICA) taxes (i.e., social security and Medicare), and (3) the Federal Unemployment (FUTA) tax, which are withheld by the employer on behalf of the employee. Exceptions may apply. For employees sent to the United States by their foreign employer, there is a de minimis exception for amounts less than $3,000 and visits of less than 90 days; also, certain treaty provisions may eliminate the need to withhold income taxes (but generally not the need to report).

If a company has US employees, it must pay and withhold social security taxes equal to 6.2% of wages for the employer and 6.2% for the employee, up to $132,900 of wages in 2019, and Medicare taxes equal to 1.45% for the employer and 1.45% for the employee. There is no cap on wages subject to Medicare taxes. The employer also must withhold an additional 0.9-percent Medicare tax on wages above $200,000. The FUTA tax is between 0.6 and 6.0% (depending on credits for state unemployment taxes) on the first $7,000 of wages paid to an employee.

A company generally must file quarterly and annual employment tax returns and annual wage statements (Forms W-2) in its name and employer identification number unless such statements are filed by a properly authorized third party.

Transfer pricing

Transfer pricing regulations govern how related entities set internal prices for the transfers of goods, intangible assets, services, and loans in both domestic and international contexts. The regulations are designed to prevent tax avoidance among related entities and place a controlled taxpayer on par with an uncontrolled taxpayer by requiring inter-company prices to meet the arm's-length standard.

The arm's-length standard generally is met if the results of a controlled transaction are consistent with results that would have been realized if uncontrolled taxpayers had engaged in a similar transaction under similar circumstances.

If a company is not in compliance with the arm's-length standard, the IRS may adjust taxable income and tax payable in the United States.

For additional information on global tax issues, including additional transfer pricing guidance, please see Appendices E and F.

Determining income

1. Gross Receipts

Income received in the normal course of business will be treated as ordinary and taxable income, eligible to be offset by various tax deductions, as discussed below.

2. Capital Gains

Gains or losses on the sale or exchange of capital assets held for more than 12 months are treated as long-term capital gains or losses. Gains or losses on the sale or exchange of capital assets held for 12 months or less are treated as short-term capital gains or losses. The excess of net long-term capital gain over net short-term capital loss is considered net capital gain.

For corporations, capital losses are allowed only as an offset to capital gains. An excess of capital losses over capital gains in a tax year may be carried back three years and carried forward five years to be used to offset capital gains.

3. Other Income

Other common forms of income include interest, rent, and royalties. Please see page 1 of Form 1120, lines 1-10 for a list of general sources of revenue included in taxable income.

Corporate deductions

1. Depreciation and amortization

Depreciation deductions are allowances that may be taken for capital expenditures for tangible property.

Additionally, corporations can elect to expense, up to a statutory amount per year, the cost of certain eligible property used in the active conduct of a trade or business, subject to a taxable income limitation and to a phase-out of the deduction.

2. Charitable contributions

Deductions for allowable charitable contributions may not exceed 10% of a corporation's taxable income computed without regard to certain deductions, including charitable contributions themselves. Deductions for contributions so limited may be carried over to the five succeeding years, subject to the 10% limitation annually.

3. Research and experimental expenditures

For tax years beginning before January 1, 2022, corporations can elect to expense all research and experimental (R&E) expenditures that are paid or incurred during the tax year or to defer the expenses for 60 months. Taxpayers also can make a special election to amortize their research expenditures over 120 months.

For tax years beginning after 2021, the Act repeals expensing of R&E expenditures and requires such expenditures to be capitalized and amortized over a five-year period, beginning with the midpoint of the tax year in which the specified R&E expenditures were paid or incurred.

4. Other common business expenses deductible for tax

- Salaries and wages
- Repairs and maintenance expenses
- Bad debts
- State, local, and other taxes (excluding federal income tax)
- Advertising and marketing
- Interest expense. The Act limits US net business interest expense deductions to the sum of business interest income, 30 percent of 'adjusted taxable income' (ATI), and floor plan financing interest of the taxpayer for the tax year, effective for tax years beginning after 2017.

See Form 1120, page 1 lines 12-29 for the common deductions available to offset revenue and arrive at taxable income.

5. Other significant items

- No deduction generally is allowed for a contingent liability until such liability is fixed and determinable
- Costs incurred for entertainment must meet strict tests to be deductible; the Act generally eliminated this deduction for amounts paid or incurred after December 31, 2017
- Royalty payments, circulation costs, mine exploration and development costs, and other miscellaneous costs of carrying on a business are deductible, subject to certain conditions and limits.

6. Net operating losses (NOLs)

An NOL is generated when business deductions exceed gross income in a particular tax year. An NOL may be carried back to offset past income and possibly obtain a refund or carried forward to offset future income. Generally, a loss generated in tax years ending before January 1, 2018, may be carried back two years and, if not fully used, carried forward 20 years. NOLs generated in tax years ending after December 31, 2017, generally may not be carried back and must instead be carried forward indefinitely; for such NOLs the deduction is limited to 80 percent of taxable income (determined without regard to the deduction).

Credits and incentives

1. Foreign tax credit (FTC)

Generally, in any year, a US company can choose whether to take as a credit (subject to limitation) or as a deduction foreign income and excess profit taxes paid or accrued during the tax year to any foreign country or US possession. An FTC reduces US income tax liability dollar for dollar, while a deduction reduces US income tax liability at the marginal rate of the taxpayer.

2. General business credit

Various business credits are available to provide special incentives for the achievement of certain economic objectives. In general, these credits are combined into one 'general business credit' for purposes of determining each credit's allowance limitation for the tax year. The general business credit that may be used for a tax year is limited to a tax-based amount. In general, the current year's credit that cannot be used in a given year because of the credit's allowance limitation may be carried back to the tax year preceding the current year and carried forward to each of the 20 years following the current year.

3. Research credit

The research tax credit is available for companies that make qualified research expenditures to develop new or improved products, manufacturing processes, or software in the United States. The deduction for R&E expenditures described above must be reduced by the entire amount of the credit unless an election is made to reduce the amount of the credit.

Administrative issues

1. Reporting and Withholding

Withholding payments are required to be made by the corporation making the payments. If the payment falls into the categories noted below, requiring a withholding, the payor withholds the tax from the payment, which is then reported to the recipient on the appropriate form.

a. 1099-K

Form 1099-K is an IRS information return used to report certain payment transactions to improve voluntary tax compliance. If you have received payments from card transactions (e.g., credit or stored-value cards), or payments in settlement of third party network transactions, you will receive Form 1099-K by January 31st of the following year from your payment service provider.

As you must report on your income tax return all income you receive, you will need the information from Form 1099-K when computing your income taxes.

b. Reporting payments to US people or companies

A US entity engaged in a trade or business that during the calendar year makes payments to a US non-exempt payee totaling $600 or more must report the amount of the payments on Form 1099-MISC, *Miscellaneous Income*. Payments subject to Form 1099-MISC reporting include compensation for services (other than wages paid to employees), rents, royalties, commissions, gains, and certain types of interest. US payers are responsible for reporting the payment whether made by cash, check, or wire transfer. Amounts paid by payment card (including debt, credit, and procurement) are not subject to Form 1099-MISC reporting by the payor. Form 1099-MISC must be furnished to payees no later than January 31 of the year subsequent to the year of payment and must be filed with the IRS by February 28 of the year following the payment. Requests to extend these dates maybe made, but extensions are not automatic.

The payor also must file Form 945, *Annual Return of Withheld Federal Income Tax*, to report any backup withholding. Form 945 must be filed with the IRS by January 31 of the year succeeding the year of payments.

c. Withholding on payments to non-US people and non-US companies

If your new US company makes certain payments to entities or individuals outside of the US, you must consider withholding requirements in the US.

People and companies making US-source payments ('withholding agents'), such as US-source interest, dividends, and royalties, to foreign people or foreign companies generally must withhold 30% of the payment amount as tax withheld at source. In other situations, withholding agents may apply a lower rate of withholding if the payee is eligible for a reduced rate under a tax treaty or by operation of the US tax laws (e.g., portfolio interest exemption).

The ability to apply a reduced rate depends on whether the withholding agent receives valid documentation evidencing the foreign payee's eligibility for a lower rate of withholding. Valid documentation includes documentation provided using Form W-8. Since there are various Forms W-8, the payee must determine which one is the correct form to be completed.

d. Withholding on payments to US people and US companies

All US and non-US entities are responsible for information reporting and backup withholding for payments made to US non-exempt recipients. Backup withholding at the current rate of 24% is required if the US non-exempt recipient fails to provide a taxpayer identification number (TIN) in the proper manner prior to payment or if the payor is instructed to backup withhold by the IRS.

Payments made to US exempt recipients are not subject to reporting or backup withholding and such recipients are not required to provide a TIN. Exempt recipients include governments (federal, state, and local), tax-exempt organizations under IRC Section 501(a), individual retirement plans, international organizations, foreign central banks of issue, and most corporations and financial institutions.

Payments made to US non-exempt recipients for dividends, gross proceeds, interest, compensation for services, rents, royalties, prizes, awards, and litigation awards, among others, must be reported. A proper TIN should be obtained from all US payees to avoid backup withholding. A TIN is best obtained by receiving a valid Form W-9, *Request for Taxpayer Identification Number and Certificate*, from US payees, including exempt recipients. The IRS's TIN Matching Program also can be utilized to verify names or TINs with IRS records to ensure accuracy.

e. Reporting payments to non-US people and non-US companies

Any taxes withheld on payments made to foreign payees must be reported to the IRS on Form 1042, *Annual Withholding Tax Return for US Source Income of Foreign Persons*. Form 1042 must be filed with the IRS on or before March 15 following the calendar year in which the income subject to reporting was paid, unless an extension of time to file is obtained. Form 1042 must be filed if a Form 1042-S is filed (see below), even if there is no withholding on the payment.

A withholding agent must file with the IRS and furnish to each foreign payee Form 1042-S, *Foreign Person's US Source Income Subject to Withholding*. Form 1042-S is the information return used by withholding agents to report US-source payments paid to foreign payees. Form 1042-S must be filed with the IRS and furnished to the foreign payee on or before March 15 following the calendar year in which the income subject to reporting was paid, unless an extension is obtained. Form 1042-S is required whether or not withholding on the payments has occurred.

f. FATCA

FATCA, the Foreign Account Tax Compliance Act, was enacted in 2010 to prevent and detect offshore tax evasion. FATCA requires many foreign financial institutions (FFIs) and some nonfinancial foreign entities (NFFEs) to enter into agreements with the IRS under which they undertake procedures to identify which of their accounts are held by US people or US companies and annually report information regarding such accounts to the IRS.

FATCA imposes registration, due diligence reviews, information reporting, and tax withholding obligations on entities that qualify as foreign financial institutions (FFIs). Legal entities with FFI characteristics must determine whether they are, in fact, FFIs and, if so, whether they are required to register with the IRS.

Businesses that do not adhere to the new obligations under FATCA may face a variety of consequences.

g. Other Informational Forms

As part of your federal income tax return, you may be required to submit other informational forms. For example, Form 5472 is required for foreign-owned US companies and is used to report certain transactions that occur between foreign and US companies that are related.

2. Filing requirements

a. Tax period

US corporate taxpayers are taxed on an annual basis. Corporate taxpayers may choose a tax year that is different from the calendar year. New corporations may use a short tax year for their first tax period, and corporations changing tax years also may use a short tax year.

b. Tax returns

The US tax system is based on the principle of self-assessment. A corporate taxpayer must file an annual tax return (generally Form 1120) by the 15th day of the fourth month following the close of its tax year; C corporations may obtain a six-month extension to file its tax return, provided it timely and properly files Form 7004, and pays the full amount of any tax due by the original due date.. Failure to timely file may result in penalties.

c. Payment of tax

A taxpayer's tax liability generally must be prepaid throughout the year in four equal estimated payments and fully paid by the date the tax return is initially due for that year. For calendar-year corporations, the four estimated payments are due by the 15th days of April, June, September, and December. For fiscal-year cor porations, the four estimated payments are due by the 15th days of the fourth, sixth, ninth, and 12th month of the tax year. Generally, no extensions to pay are allowed. Failure to pay the tax by the due dates can result in estimated tax and late payment penalties and interest charges.

3. Statute of limitations

The IRS generally has three years after an original return is filed to assess income taxes. A return will be deemed to have been filed on its due date, even if the return is actually filed on an earlier date.

4. Accounting for income taxes

For US federal tax purposes, the two most important characteristics of a tax method of accounting are timing and consistency. If the method does not affect the timing for including items of income or claiming deductions, it is not an accounting method and generally IRS approval is not needed to change it. In order to affect timing, the accounting method must determine the year in which an income or expense item is to be reported.

In general, in order to establish an accounting method, the method must be consistently applied. Once an accounting method has been adopted for federal tax purposes, any change must be requested by the taxpayer and approved by the IRS. Changes in accounting methods cannot be made through amending returns. The two most common methods of accounting are the accrual-basis and cash-basis methods.

5. Penalties

Civil and criminal penalties may be imposed for failing to follow the Internal Revenue Code when paying US taxes. The civil penalty provisions may be divided into four categories: delinquency penalties, accuracy-related penalties, information reporting penalties, and preparer or promoter penalties. Many, but not all, of these provisions include exceptions for reasonable cause in not complying. In addition, many include rules as to how a particular penalty interacts with the other penalties.

State and local tax issues

Foreign companies with activity in the United States often are surprised that such activity may trigger both federal and state-level taxes. Even more surprising, there are no uniform rules among the states as to whether state tax liability attaches; in some cases, significant state tax liabilities may be imposed even if little or no US federal tax obligations exist.

Activities that could subject an entity to state tax

A state generally may impose its tax on an entity to the extent a sufficient 'nexus,' or taxable connection, exists between the entity and the state. While US federal taxation generally requires a threshold level of activity of being 'engaged in a trade or business' or having a 'permanent establishment,' mere physical presence in a state, such as having employees, owning property, storing inventory, or paying for rental property in the state, generally may be sufficient for nexus to exist for state taxation purposes.

Following the US Supreme Court's 2018 decision in *South Dakota v. Wayfair*, which eliminated the "physical presence" requirement for the imposition of state sales and use tax collection obligations, it is possible that actual physical presence in a state may no longer be required for nexus to exist for state income taxation purposes.

There is no clear cut answer if you need to file – it depends. Practically speaking, you may not owe any taxes, but some states require returns even if you owe no tax. It's important to know the requirements of each state.

Economic nexus could be deemed to exist between a state and a company based on the presence of intangible property in a state. For example, the license of trademarks to a company located in a state could create nexus for the out-of-state licensor on the basis that the intangibles are 'present' in the state.

Dividing up taxable income among the states: multistate apportionment

For US state tax purposes, a percentage of the entire net income of an entity, may be subject to tax by a state. That percentage generally relates to the proportionate level of activity (e.g., sales, property, and payroll) the entity has within the state as compared with its activity outside the state.

Indirect tax considerations

State 'indirect taxation' generally refers to any state tax that is not based on income. The most common indirect tax is a state's sales and use tax; other indirect taxes include franchise taxes, real estate transfer taxes, telecommunications taxes, commercial rent taxes, and hotel occupancy taxes. The indirect taxes that apply depend on the nature of the company's business activities.

Once a company has nexus to a state with respect to sales and use taxes, that company must register with the state's tax department, file sales tax returns, and pay its sales tax liabilities. Depending on the volume of sales, the company may be required to file returns on an annual, quarterly, or monthly basis. Generally, sales tax is imposed on retail sales, leases, rentals, barters, or exchanges of tangible personal property and certain enumerated services unless specifically exempted or excluded from tax.

Sales tax generally is imposed in the jurisdiction in which the 'sale' occurs. The definition of 'sale' differs from jurisdiction to jurisdiction; however, the definition generally includes both (1) consideration and (2) transfer of title, right to use, or control (possession) in the case of tangible property and completion of the service act in the case of a service.

Local taxation

Many cities impose separate income tax filing obligations. Compliance complexities multiply because US taxation geographies are further divided within states and some US cities have significant taxing powers.

In addition, cities may impose local-level sales and use taxes. Administratively, the sales taxes usually are collected by and remitted to the state, and then allocated to the localities. Generally, the rules for the localities are modeled after the rules for the states, but this is not always the case. The rules can vary from jurisdiction to jurisdiction. Overall, there are thousands of indirect taxing jurisdictions in the United States.

Delaware Franchise Tax

Any corporation that is incorporated in Delaware (regardless of where it conducts business) must file an Annual Franchise Tax Report and pay Franchise Tax for the privilege of incorporating in Delaware. Franchise Taxes and annual Reports are due no later than March 1st of each year.

The Delaware Franchise Tax will range from $175 to $200,000 depending on the amount of the company's authorized shares. A corporation having 5,000 authorized shares or less is considered a minimum stock corporation with a tax of $175.

Generally, the more shares the US corporation has, the higher the Franchise Tax (with a maximum annual tax of $200,000). An Annual Report filing fee of $50 is also required.

Corporations having nexus in Delaware are also required to file corporate income tax returns. However, corporations that maintain a statutory corporate office in Delaware but that do not do business in Delaware and corporations whose activities in Delaware are limited to the maintenance and management of intangible investments are exempt from corporate income tax.

Delaware requires that businesses with nexus in the state must be licensed to do business in the state and pay a fee, the amount of which varies depending upon the type of business. Additionally, such business are generally required to pay a gross receipts tax. The gross receipts tax is imposed on a business's gross receipts in Delaware.

US Tax Treaties

The United States has in place income tax treaties with more than 60 countries, including treaties with most European countries and other major trading partners, including Mexico, Canada, Japan, China, Australia, and the former Soviet Union countries. There are many 'gaps' in the US tax treaty network, particularly in Africa, Asia, the Middle East, and South America.

US income tax treaties typically cover various categories of income, including:

- business profits
- passive income, such as dividends, interest, and royalties
- income earned by teachers, trainees, artists, athletes, etc.
- gains from the sale of personal property
- real property income
- employment income
- shipping and air transport income
- income not otherwise expressly mentioned

The categories of income covered vary from treaty to treaty, and no two treaties are the same.

To gain treaty benefits, it is necessary to satisfy the conditions of the residency article as well as certain other requirements.

How can PwC help?

The United States remains a favorable destination for global investment and offers a competitive environment in which to do business. Given the new tax law and the existing multi-tiered structure of US taxation, global companies doing business in the United States have an even greater incentive to examine thoughtfully their approach to taxation and management of their operations.
Our US Inbound Tax practice specifically focuses on helping you formulate your US inbound policies and develop strategies so you can meet your business needs and goals in the United States.

In the current challenging economic environment, we can work together on:

- financing your US operations
- managing your domestic and state taxation
- planning for growth through transactions and deals
- transforming your value chain
- navigating the new US federal tax law.
- setting up your tax department in the United States

Our approach is designed to identify tax opportunities and help manage efficiently adverse tax outcomes, so that the US business of a foreign MNC plays its part in implementing a globally effective and integrated approach to tax planning for the group and so that desired tax outcomes are integrated seamlessly into business objectives and operations.

Appendix A: Other Taxes

1. Stamp taxes

There is no federal-level stamp tax. However, state and local governments frequently impose stamp taxes at the time of officially recording a real estate or other transaction. The state or local sales tax on real estate may be a stamp tax on the documents recording the transfer of the real estate.

2. Capital gain taxes

The corporate tax rate on long-term capital gains currently is the same as the tax rates applicable to a corporation’s ordinary income. (by contrast, individuals may be subject to a lower rate on long-term capital gain than on short-term capital gain.)

3. Accumulated earnings tax

The accumulated earnings tax equals 20% of ‘accumulated taxable income.’ Generally, accumulated taxable income is the excess of taxable income with certain adjustments, including a deduction for regular income taxes, over the dividends paid deduction and the accumulated earnings credit. Note that a corporation can justify the accumulation of income, and avoid tax, based on its reasonable business needs.

4. Personal holding company tax

US corporations that receive substantial 'passive income' and are 'closely held' may be subject to personal holding company tax. The personal holding company tax, which is levied in addition to the regular tax, is 20% of undistributed personal holding company income.

Appendix B: Other Issues

1. Group taxation

An affiliated group of US ‘includible’ corporations, consisting of a parent and subsidiaries directly or indirectly 80% owned, generally may offset the profits of one affiliate against the losses of another affiliate within the group by electing to file a consolidated federal income tax return.

Filing on a consolidated (combined) basis is also allowed (or may be required or prohibited) under the tax laws of certain states.

Sales, dividends, and other transactions between corporations that are members of the same group generally are deferred or eliminated until such time as a transaction occurs with a non-member of the group. Losses incurred on the sale of members of the group are disallowed under certain circumstances.

2. Payments to foreign affiliates

A US corporation generally may claim a deduction for royalties, management service fees, and interest charges paid to foreign affiliates, to the extent the amounts are actually paid and are not in excess of what it would pay an unrelated entity (i.e., are at arm’s length). US withholding on these payments may be required. Under certain circumstances, such payments also may give rise to a BEAT liability for the US payor, as discussed above.

Appendix C: Information reporting

Form W-8BEN, *Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding*, is the most commonly used Form W-8. That version is used to establish that the payee is not a US person and is the beneficial owner of the income related to which the Form W-8BEN is being provided. Form W-8BEN also can be used to claim a reduced rate of withholding based upon an applicable income tax treaty. **Note**: Form W-8BEN is used only by individuals. Entities use Form W-8BEN-E.

Form W-8BEN-E, *Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)*. Among other purposes (e.g., FATCA), this form is used to establish that the payee is not a US person and is the beneficial owner of the income related to which the Form W-8BEN-E is being provided. Form W-8BEN-E also can be used to claim a reduced rate of withholding based upon an applicable income tax treaty. **Note**: Form W-8BEN-E is used only by entities. Individuals use Form W-8BEN.

In addition to Form W-8BEN or Form W-8BEN-E, other forms that can be provided by a foreign payee to reduce or eliminate withholding are:

- Form W-8ECI, *Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States*, is provided by a non-US entity or individual that is engaged in a US trade or business and has income that is effectively connected with such US trade or business.
- Form W-8EXP, *Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding & Reporting*, is provided by non-US governments or non-US tax-exempt organizations.
- Form W-8IMY, *Certificate of Foreign Intermediary, Foreign Flow Through Entity, or Certain US Branches for United States Tax Withholding & Reporting*, is provided by non-US flow-through entities (e.g., partnership) that is not engaged in a US trade or business and non-US intermediaries. Form W-8IMY generally must be accompanied by Forms W-8 and/or Form W-9 for the beneficial owners and a withholding statement that allocates the income to the beneficial owners.

Treaty claims made by nonresident alien individuals who provide independent personal services in the US are made on Form 8233, *Exemption from Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual*, instead of on Form W-8BEN.

Forms W-8BEN, W-8BEN-E, W-8ECI, and W-8EXP generally are valid for three years from the date the form is signed. New forms are required prior to the expiration of three years if there is a change in the information disclosed by the payee on the forms. For some purposes (not applicable if treaty benefits are claimed), the forms can remain valid indefinitely absent a change in circumstances. Form W-8IMY is valid indefinitely unless there is a change in the information disclosed by the payee on the forms. Form 8233 is valid for only one year.

Appendix D: Foreign company considerations

When foreign individuals or corporations are investing in the US they should be aware of the potential US tax implications for the foreign entity interacting with the US. While the US tax consequences of the US corporation are described throughout this Guide, there are other tax considerations for a foreign company to manage the US tax risk of the activities of the foreign company. The following issues should be considered:

US trade or business

Generally, a foreign corporation engaged in a US trade or business is taxed on a net basis at regular US corporate tax rates on income from US sources that is effectively connected with that business and also is subject to a 30-percent branch profits tax on the corporation's effectively connected earnings and profits to the extent treated as repatriated to the home office; the branch tax can be reduced or eliminated under an applicable US tax treaty.

There is no definition in the tax statute of a trade or business within the United States—instead, that concept has been developed mainly by the IRS and court decisions through a facts-and-circumstances analysis. The following have been considered by the courts and/or the IRS:

- The business must have a profit motive.
- Activities generally must be 'considerable, continuous, and regular.'
- Ministerial, clerical, or collection-related activities generally are not sufficiently profit-oriented to constitute a US trade or business.
- Isolated activities generally do not rise to the level of a trade or business.
- An agent's activities in the United States may result in a US trade or business.

Effectively connected income

If a non-US person has a US trade or business, the question arises as to what income is 'effectively connected' to such US trade or business.

All US-source active income earned by a non-US person is treated as effectively connected, except that passive-type income and gain from the sale of capital assets are treated as effectively connected to a non-US person's US trade or business only if a connection with the US trade or business exists. Such a connection exists if the passive-type income or capital gain is derived from assets used in the US trade or business or if the activities conducted in the US trade or business are a material factor in the production of the passive-type income or capital gain.

Certain types of foreign-source income generated through a US office can be effectively connected income. These include:

- Rents or royalties for use of intangible property outside the United States that are derived in the active conduct of a US trade or business

- Foreign-source dividends or interest derived in active conduct of banking business in the United States, or received by a corporation the principal business of which is trading in stocks or securities for its own account

- Gain from the sale outside the United States of inventory property and property held for sale to customers, when the sale is made through a US office or fixed place of business, unless the property is sold for use outside the United States and a non-US office materially participates in the sale.

Permanent establishment (PE)

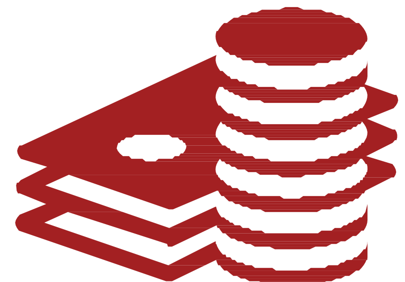
Multinational businesses face a variety of tax systems in the countries where they operate. To reduce or eliminate double taxation between countries, promote cross-border trading, and alleviate the burden of administration and enforcement of tax laws, countries typically enter into income tax treaties outlining how parties to the treaty (contracting states) will be taxed on income earned in each contracting state.

Income tax treaties contain an article describing whether the activities of an enterprise rise to a level of a PE in a contracting state. The existence of a PE is important because it gives the contracting state the right to tax the enterprise's income attributable to the PE. This includes income from carrying on a business in the contracting state and passive income, such as interest, dividends, and royalties.

A PE generally means:

- there is a fixed place of business through which the business of an enterprise is wholly or partly carried on, or
- an agent acting on behalf of the enterprise has and habitually exercises the authority to conclude contracts binding on the enterprise.

This is a very factual determination that requires a full understanding of a company's particular facts and circumstances.



Appendix E: Transfer pricing

Due to growing government deficits, many jurisdictions are putting additional pressure on transfer pricing in order to secure a larger portion of entities' profits for their tax bases. This can result in the risk of tax assessments, double taxation of the same income by two jurisdictions, and penalties for failure to properly allocate income among two or more jurisdictions. Therefore, virtually all large MNCs should regularly review their international transfer pricing strategies and potential risks.

Transfer pricing applies to a wide range of intercompany transactions, including transactions involving:

- tangible goods (e.g., manufacturing, distribution)
- services (e.g., management services, sales support, contract R&D services)
- financing (e.g., intercompany loans, accounts receivable, guarantees, debt capacity)
- intangible property (e.g., licenses, royalties, cost sharing transactions, platform contribution transactions, sales of intangibles).

The international standard for determining the appropriate transfer price is the arm's-length principle. Under this principle, transactions between two related parties should not produce results that differ from those that would have resulted from similar transactions between independent companies under similar circumstances. This principle is cited in the US transfer pricing rules (IRC Section 482 and the Treasury regulations thereunder), the OECD Transfer Pricing Guidelines, and the UN Manual for developing countries. There are some countries (e.g., Brazil) that do not follow the international application of the arm's-length principle.

If a transaction between related parties is priced differently than if it were between unrelated parties, the IRS has authority to reallocate income or expenses to reflect the amounts that would have resulted had the transaction been conducted at arm's length.

The Section 482 regulations are extensive and attempt to address a full range of transactions in light of the arm's-length standard. In practice, however, it is not easy to determine the appropriate arm's-length result based on a given set of facts and circumstances. Transactions in goods and services may embody unique, company or industry-specific elements that are difficult to compare with transactions involving other companies. The Section 482 regulations concede the rarity of identical transactions, and instead attempt to determine the arm's-length results based on the 'best method' rule.

Best method rule

The Section 482 regulations provide several methods to test whether a price meets the arm's-length standard. Although there is no strict priority of methods, and no method invariably will be considered to be more reliable than another, every transaction reviewed under Section 482 must be judged under the method that, under the facts and circumstances, provides the most reliable measure of an arm's-length result (i.e., the 'best method').

The selection of a method also varies depending on the type of transaction. For example, the regulations provide five specified methods for transactions involving tangible property, and six specified methods for service transactions, while only three are specified for transactions involving intangible property. Methods not specified in the regulations are also potentially applicable. Note that while each method is important to understand, an examination of each is beyond the scope of this discussion.

Comparability factors

To determine the best method for a particular transaction, the relative reliability of a method must be evaluated on the degree of comparability between the controlled transaction or taxpayers and uncontrolled comparables, taking into account certain factors. While a specific comparability factor may be of particular importance in applying a method, each method requires an analysis of all the factors that affect comparability under that method.

Quality of data and assumptions

Whether a method provides the most reliable measure of an arm's-length result also depends upon the reliability of the assumptions and the sensitivity of the results to possible deficiencies in the data and assumptions.

The completeness and accuracy of the data affect the ability to identify and quantify those factors that would affect the result under any particular method. Likewise, the reliability of the results derived from a method depends on the soundness of assumptions made in applying the method. Finally, the sensitivity of results to deficiencies in data and assumptions may have a greater effect on some methods than others. In particular, the reliability of some methods depends heavily on the similarity of property or services involved in the controlled and uncontrolled transaction, while other methods rely on broad comparisons of profitability.

Arm's-length range

The Section 482 regulations recognize that a method is likely to produce a range of arm's length results and provide that a taxpayer will not be subject to adjustment if the taxpayer's results fall within such an arm's-length range. The arm's-length range ordinarily is determined by applying a single pricing method selected under the best method rule to two or more uncontrolled transactions of similar comparability and reliability.

The comparables used for the uncontrolled transactions must be sufficiently similar to the controlled transaction. If material differences exist between the two transactions, adjustments must be made in order for the uncontrolled transaction to have a similar level of comparability and reliability. In many cases, the reliability of the analysis will be improved by adjusting the range through the application of a valid statistical method, often the interquartile range of results.

Penalties and documentation

The Internal Revenue Code imposes penalties if a taxpayer receives an IRS transfer pricing adjustment exceeding certain thresholds. The penalties do not apply, however, if the taxpayer has prepared and documented a reasonable transfer pricing analysis supporting its reported transfer pricing.

Under Section 6662(e), the transfer pricing penalty generally is equal to 20% of the underpayment of tax attributable to the transfer pricing misstatement, but increases to 40% of the underpayment of tax for larger adjustments. Having contemporaneous transfer pricing documentation that satisfies the requirements under Section 6662(e) in place at the time the tax return is filed can provide protection against these penalties.

Another avenue for avoiding potential transfer pricing penalties can be an advance pricing agreement (APA)—an agreement between a government and a taxpayer that provides prospective 'certainty' for a defined term regarding covered intercompany transactions. APAs can be unilateral (between the taxpayer and the IRS), bilateral (with the IRS and another tax authority), or multilateral (with the IRS and more than one other tax authority).

Appendix F: The OECD's BEPS project

OECD BEPS Action Plan

Since 2012, G20 countries and the OECD have pursued an initiative to reform international tax regimes by addressing opportunities for base erosion and profit shifting (BEPS). On October 5, 2015, the OECD released final recommendations from its BEPS project, which then were endorsed by the G20 leaders at their summit in Antalya, Turkey, on November 15-16, 2015. A number of non-G20 countries also have been involved in work on the Action Plan and contributed to the proposals.

On May 23, 2016, the OECD Council approved the amendments to the Transfer Pricing Guidelines, as set out in the 2015 BEPS Report on Actions 8-10, 'Aligning Transfer Pricing Outcomes with Value Creation,' and the 2015 BEPS Report on Action 13, 'Transfer Pricing Documentation and Country-by-Country Reporting." In July 2017, the OECD released the 2017 edition of the Transfer Pricing Guidelines.

The OECD's BEPS Action Plan categorized its various focus areas into three themes: addressing substance; coherence of the international tax system; and transparency.

Substance actions seek to align taxing rights with the relevant value-adding activity. Coherence actions aim to remove gaps and 'black holes' among countries' tax systems. Transparency actions look to provide significant additional disclosure to tax authorities.

In addition to the various actions grouped under these three themes, the BEPS Action Plan also seeks to address digital business, improve dispute resolution, and create a multilateral instrument for rapid updating of bilateral tax treaties. Finalized proposals for all these items were included in the package of measures released by the OECD.

There are three fundamental ways in which the OECD's work on BEPS has had a practical impact:

- First, and most obvious, there has been the direct application of the BEPS package itself, whether through changes to tax treaties — by amendment of the OECD model tax convention (updated in November 2017) — or the multilateral instrument (with 78 signatories as of January 2018) and transfer pricing guidelines, or through changes to domestic legislation as a result of individual recommendations of the BEPS Action Plan.

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- Second, there have been unilateral actions by some countries, notwithstanding OECD efforts to discourage such actions. Countries adopting unilateral measures may do so because they disagree with the direction of the BEPS package or think the recommendations do not go far enough

Third, and perhaps most important, there has been a behavioral impact — specifically, in emboldening the behavior of tax authorities. This is likely to continue, resulting in more aggressive and more protracted challenges by tax authorities, higher thresholds for obtaining advance rulings, and increased tax controversies in general.

Increased risk of double taxation

Historically, the goal of the OECD has been to promote global economic growth and development through the unfettered exchange of goods and services, and the movement of capital, technology, and persons across borders. To that end, the OECD's focus has been on eliminating impediments to cross-border flows, such as double taxation, by expanding income tax treaty networks, by establishing clear rules for governments with respect to taxing companies with a limited presence in their jurisdictions, and by reducing gross-basis withholding taxes.

The OECD BEPS project, by contrast, focused on eliminating so-called ‘double non-taxation.’ In this quest, the OECD sought to coordinate action among participating governments in order to avoid increasing the risk of unrelieved double taxation.

As a consequence, there are serious concerns that one outcome of the BEPS project could be a surge in instances of double taxation and tax disputes worldwide.

The OECD has undertaken two measures to mitigate these concerns. In December 2016, the OECD launched the Mutual Agreement Procedure (MAP) peer review and monitoring process under Action 14 of the BEPS Action Plan with the aim to improve the MAP process. In addition, the OECD began its Inclusive Framework, under which developing countries have formally participated and been engaged since the beginning of the BEPS Project.

Under this framework, more than 80 developing countries and other non-OECD/non-G20 economies discuss the challenges of BEPS through direct participation in the Committee on Fiscal Affairs.

Most significant impacts for taxpayers

With regard to BEPS, the most significant impacts on taxpayers are likely to be in the following areas:

• Tax treaty access becoming more constrained and in some cases uncertain

• Increases in transfer pricing documentation, new ‘country-by-country’ (CbC) reporting requirements, and the wider transparency agenda necessitating company information system changes

• Increased focus on conduct as a relevant test in assessing transfer pricing compliance

• Increases in assertions of PE and erratic interpretation of PE profit attribution rules

• Restrictions in the relief for interest and other financial payments

• Rise in the level of cross-border controversy and number of disputes on formulas for allocating income and deductions across jurisdictions, with double taxation possible as a result of non-uniform formulas.

Digitalization of the economy

The most significant global tax policy development in 2017 was the emergence of taxation of the digital economy as the biggest focus for policymakers and multinational companies. When the OECD BEPS Project Report on the Tax Challenges of the Digital Economy (Action 1) was released in October 2015, the OECD Task Force on the Digital Economy (TFDE) concluded that digitalization exacerbated the opportunities for BEPS, but that the other BEPS Action Item recommendations should suffice to address such risks. The TFDE also concluded that the digital economy could not be ring-fenced because it ‘is increasingly becoming the economy itself.’

While consensus was reached that these areas should be revisited in a full review by 2020, there was an understanding that countries might not await the result of this review before acting unilaterally – albeit consistently with their treaty obligations – through introducing measures such as virtual PEs, equalization levies, and withholding taxes. During 2016, a few countries sought to introduce ‘innovative’ tax measures, but 2017 saw a significant acceleration in the consideration of such measures – particularly by some European countries.

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To schedule a discussion with a PwC professional on general US tax issues, please contact pwc@stripe.com.

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