35th Annual TEI-SJSU High Tech Tax Institute
IP Planning and Structuring for Intangibles:

"Is IP Planning Dead?"
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Your Panel

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IP Planning and Structuring for Intangibles-Tax Reform

Transition Tax

One-time tax on US shareholder's share of post-1986 earnings of foreign corporations in which it owns at least 10% (CFCs and 10/50 companies); tax rate is 15.5% (to extent of cash) or 8% (non-cash).

GILTI

US shareholder must include share of CFC income (with certain exclusions) in excess of 10% of CFC's basis in depreciable tangible property (=GILTI). For corporations is 10.5%, but increases to 13.125% for taxable years beginning after 2025

Global Intangible Low-Taxed Income

FDII

FDII is taxed at 13.125% and 16.406% for taxable years before and after 2026, respectively

Foreign derived intangible income

BEAT

Potential tax of 10%/12.5% (before/after 2026) applies to base erosion (e.g.

Interest expense

Interest expense that exceeds 30% of adjusted taxable income

"US shareholder" definition now based on vote or value

Tax Reform

- US adopts what is intended to operate as a global minimum tax disguised as a territorial system, barring unusual circumstances, foreign

  - The GILTI and FDII provisions together create a theoretical worldwide minimum tax

FDII Planning

- Current rate is 13.125%. This rate will increase to 16.406% for tax years beginning after December 31, 2025.
- Potential challenges to the deduction (e.g., WTO) add uncertainty to structuring for FDII.
- A foreign person is generally a person that is not a US person under Section 7701(a)(30), including a foreign partnership and a foreign government.
- Foreign use means any use, consumption, or disposition that is not in the US.
- Documentation is an important aspect of FDII. Both the status of a buyer as a foreign person and the foreign use of the intangible property must be documented.

US Tax Reform – Other Considerations – Subpart F

- Planning is generally advisable to obtain the lower GILTI effective tax rate (often 10.5% for US corporate shareholders) rather than the higher Subpart F tax rate of 21%.
  - However, consider that the foreign tax credit relating to Subpart F carries forward, while any unused GILTI foreign tax credit is lost.
  - Also consider that high tax kick out currently only applies to Subpart F income. Proposed regulations (not currently in effect) would expand the high tax kick out to GILTI.
  - The sale of IP by a CFC generally would qualify as either Subpart F income or as GILTI depending on the prior usage of the IP.

- There will be mandatory amortization of R&D costs beginning in tax years after December 31, 2021.
  - Research conducted in the US – 5 year amortization period
  - Research conducted outside the US – 15 year Amortization Period
  - This change will affect the desirability of the R&D credit and whether non-core R&D costs are deducted under IRC §174 or another code section.
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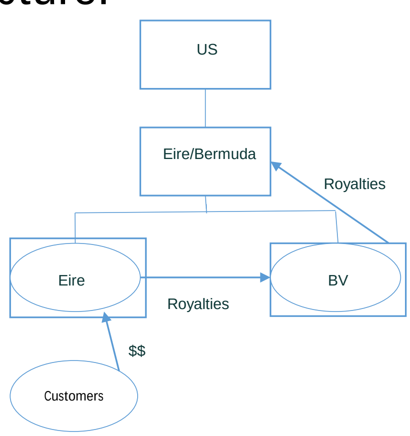
US Tax Reform – Other Considerations – States

- State adoption of TCJA changes has been inconsistent and has led to varying conformity to Section 965, GILTI, and FDII.
  - Fixed Conformity vs. Rolling Conformity
- Trends in state apportionment (single sales factor) and sourcing of sales (market-based sourcing) have also had an affect on IP placement.

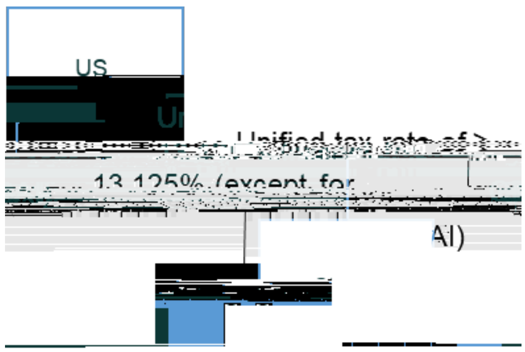
Pre-2017 US Intangibles Planning

The famous Double Dutch Irish Structure:

- Irish/Bermuda IP Holdco
- Dutch licensing
- Irish principal
- Result: lots of low tax profits, and
- France and Germany not happy



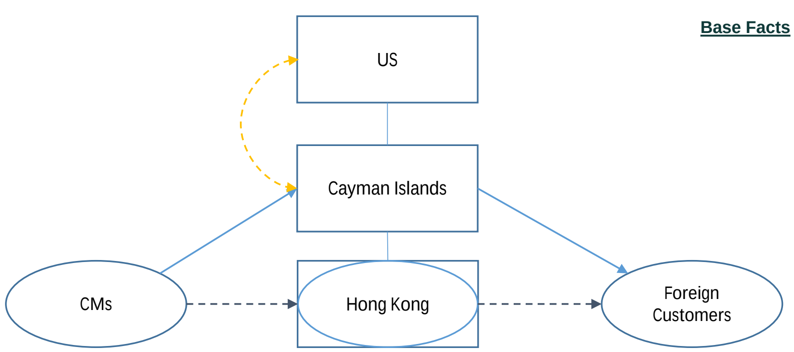
US Corporate Tax – After 2017



- CFC subject to tax in home country
- US parent subject to 21% tax on current year CFC earnings, but potentially mitigated by: i) 50% Section 250 deduction, and 80% Section 960 foreign tax credit and theoretical 901 credit; “QBAI” safe harbor
- No US tax on dividend (regardless of whether the income was subject to GILTI)
- 960 FTC one time “use it or lose it” for GILTI: no excess credit carryover
- FDII export incentive: target tax rate of 13.125%
- Individuals do not get the 13.125% FDII rate. To get a reduced GILTI rate, individuals must make a Section 962 election.

Life After US Tax Reform – “Old School” Tech Example

Example: Fabless Chip Company



IP Planning and Structuring for Intangibles

GILTI Results:

US Profit*	100x
GILTI (Gross Inclusion)	1,000x
Section 250(a)(1)(B) Reduction	(500x)
Taxable Income	600x
US Federal Income Tax (21%)	126x
Global Effective Tax Rate (126x/1100x)	**11.45%**

* Available for FDII Section 250 deduction

IP Planning and Structuring for Intangibles

FDII Alternative: Cayman Royalty Structure

US Profit*	100x
Royalty Income (Max)	1,000x
Less: Section 250 Deduction	(375x)
Taxable Income	725x
US Federal Income Tax (21%)	152x
Global Tax Rate (152x/1100x)	**13.82%**

* Available for FDII Section 250 deduction

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Key Valuation Questions: Applicable Rules

Mechanisms

- Transfers
- Contributions
- Dividends
- Exchanges
- Redomiciling
- Dual incorporation
- Licensing

Example

Applicable Rules

- Transfer pricing rules (ALS)
- Financial reporting rules
- Local specific tax valuation rules
- Capital Gains Tax rules
- Other
  - §367(d) super royalty

Limitations on Amortization: Tax Amortization Benefits

US IRC §197 amortization and the anti-churning rules:

- August 10, 1993 §197 amortization rules changed to allow amortization of indefinite lived assets
- Indefinite lived assets existing before August 10, 1993 are not eligible for §197 amortization

Non-amortizable assets

- Depends on local rules

Tax vs Financial Reporting Definitions

- Asset purchase vs Business combination

Limitations on Amortization: Tax Amortization Benefits

FOR ILLUSTRATION ONLY- DO NOT RELY ON THIS TABLE - CAPITAL ALLOWANCE AND AMORTIZATION RULES ARE COMPLEX								
Intangible Tax Amortization Benefit Period for Selected Countries (years)								
Country	Valuation Standard[7]	Patents	Software / copyrights	Other Technology[1]	Trademarks	Customers / Relationships	Goodwill	Last Updated
United States	ALS or FMV	15	15	15	15[2]	15	15[2]	2019
Canada[6]	ALS or FMV	RUL or Elect 25% reducing bal	1 year or RUL	RUL	15~20[5]	15~20[5]	15~20[5]	2019
Ireland[4]	FMV or FV	RUL[3] or Elect 15	RUL[3] or Elect 15	RUL[3] or Elect 15	RUL[3] or Elect 15	No TAB	No TAB	2019
Netherlands	ALS or FMV	Greater of RUL or 5 years	Greater of RUL or 5 years	Greater of RUL or 5 years	Greater of RUL or 5 years	Greater of RUL or 5 years	10 years or longer	2019
United Kingdom[8]	FMV or FV	RUL or Elect 25	RUL or Elect 25	RUL or Elect 25	RUL or Elect 25	6.5% pa (15.4 years)	6.5% pa[9] (15.4 years)	2019
Australia[10]		20	5	5	No TAB	No TAB	No TAB	2016
Singapore	"Open Market Price" similar to FV	Irrevocable election for 5, 10 or 15 years	Irrevocable election for 5, 10 or 15 years	Irrevocable election for 5, 10 or 15 years	Irrevocable election for 5, 10 or 15 years	No TAB	No TAB	2019
Hong Kong		1	1	1	5	No TAB	No TAB	2016
China		RUL or Elect 10	RUL or Elect 10	RUL or Elect 10	RUL or Elect 10	RUL or Elect 10	No TAB	2016
Malaysia		5	2.5	2.5	5	No TAB	No TAB	2016

Income Approach: Projections and Tax Rates

Impact of TCJA

- Important to have a discrete forecast period in the DCF extend to ***2027 or later*** to account for some of the tax policy implications that are temporary
- Expected impact on tax savings in initial years likely leads to an ***increase in operating cash flow***. This may not always translate to ***Free Cash Flow***.
- Capex and R&D rule changes mean that ***mid-term cash flows may reduce significantly***.

How should valuations take into account tax uncertainty?

- Will there be challenges to FDII at the WTO?
- Some concern in the tax community about potential reversals of tax rates by subsequent administrations.
- What's the impact of digital taxes on international tax developments?

Valuations should only include expectations of events that are known or knowable

Best Practice: probability weighted expected outcomes based on different scenarios…if you've got the time

Projections: US Commensurate with Income / OECD Hard to Value Intangibles

- Similarities between US CWI and OECD HTVI
  - Deal with asymmetry of information between taxpayer and tax authorities
- Differences between US CWI and OECD HTVI
  - Replacement vs recalculation
  - Special rules (US CSA's and US intangibles)
- Mitigation (if desirable):
  - Have probability weighted outcome scenarios with sufficient breadth.
  - Contingent consideration
  - Built in adjustment trigger clauses