NYC DEPARTMENT OF FINANCE

18-9 September 1, 2019

FINANCE MEMORANDUM

New York City Tax Treatment of Foreign-Derived Intangible Income Deduction, Global Intangible Low-Taxed Income, and Repatriation Amounts Under the Business Corporation Tax

The federal Tax Cuts and Jobs Act[1] (the Act) created new provisions in the Internal Revenue Code (IRC) addressing income earned from overseas operations including mandatory deemed repatriation income, foreign-derived intangible income (FDII), and global intangible low-taxed income (GILTI).

This Finance Memorandum generally explains the impact of these federal changes, as well as related changes enacted in the 2018-19 New York State budget,[2] on taxpayers that are subject to the Business Corporation Tax.[3]

Mandatory Deemed Repatriation Income

The Act required taxpayers to recognize mandatory deemed repatriation income as Subpart F income. In general, this is accomplished by U.S. shareholders recognizing post-1986 accumulated earnings and profits and deficits of specified foreign corporations under IRC § 965(a) and (b) (together referred to as the IRC § 965(a) inclusion amount). These taxpayers are then allowed to deduct a portion of the IRC § 965(a) inclusion amount under IRC § 965(c), resulting in a net IRC § 965 amount. The amounts recognized under IRC § 965 include amounts earned directly by U.S. shareholders as well as their distributive shares of IRC § 965 amounts from flow-through entities.

Unlike federal law, which allows certain taxpayers to elect to defer payment of a portion of their federal tax liability related to their mandatory deemed repatriation income, New York City taxpayers, including combined groups, cannot defer payment of any portion of their New York City tax associated with mandatory deemed repatriation income.

Treatment of Repatriation Income Under the Business Corporation Tax

For tax years beginning on or after January 1, 2017, the IRC § 965(a) inclusion amount received from both unitary and non-unitary corporations not included in a combined return with the taxpayer is considered gross exempt controlled foreign corporation (CFC) income. It is never considered gross investment income.

The IRC § 965(a) inclusion amount, less any interest deductions directly or indirectly attributable to the income (or less 40% of the IRC § 965(a) inclusion amount if the safe harbor election is made), is considered exempt CFC income and deducted from entire net income (ENI) when computing business income. Since the IRC § 965(a) inclusion amount is considered gross exempt CFC income, the federal deduction under IRC § 965(c) is not allowed.

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[1] *See* Public Law 115-97.

[2] *See* Part KK of Chapter 59 of the Laws of 2018.

[3] The Department will provide separate guidance regarding the General Corporation Tax, Banking Corporation Tax, and Unincorporated Business Tax.

Taxpayers must use Finance Memorandum 16-2 (01/26/2016), Direct and Indirect Attribution of Interest Deductions Under the Business Corporation Tax (Corporate Tax of 2015). Finance Memorandum 18-11, Impact of IRC § 163(j) Limitation on Interest Attribution, and this Finance Memorandum when determining the amount of interest deductions directly or indirectly attributable to the IRC § 965(a) inclusion amount.

- If the stock of a foreign corporation that generates the IRC § 965 inclusion amount is business capital, then the stock is considered exempt CFC stock for purposes of Finance Memorandum 16-2 and no modifications to the Finance Memorandum 16-2 attribution methodology are necessary.

- If the stock of a foreign corporation that generates the IRC § 965(a) inclusion amount is investment capital, the stock is not considered exempt CFC stock used in Step 3(C) of Finance Memorandum 16-2. Rather, such stock is included in the indirect attribution formula for investment capital computed in Step 3(D) of Finance Memorandum 16-2.

The IRC § 965(a) inclusion amount is not included in the numerator or denominator of the business allocation percentage (BAP).

The IRC § 965(a) inclusion amount is disregarded for purposes of the "principally engaged" test used to determine a taxpayer's, or combined group's, eligibility for preferential rates and amounts available to manufacturers.

Taxpayers that have an underpayment of estimated tax penalty related to the addback of interest deductions attributable to their IRC § 965(a) inclusion amount (or the 40% safe harbor election attributable to their IRC § 965(a) inclusion amount) on their 2017 New York City Business Corporation Tax return may request a penalty abatement if they receive a bill for that penalty.[4] There is no penalty relief for tax years after 2017.

[IRC § 965; Administrative Code §§ 11-652(5-a)(b), 11-652(8)(b)(20), 11-676(3)]

Foreign-derived intangible income (FDII) deduction

For federal tax purposes, a U.S. domestic corporation taxed as a C corporation[5] is allowed to deduct a portion of its income derived from serving foreign markets. For purposes of Subchapter 3-A, New York City decouples from the federal FDII deduction for tax years beginning on or after January 1, 2017.

[IRC § 250(a)(1)(A); Administrative Code § 11-652(8)(b)(21)]

[4] *See* Finance Memorandum 18-4 for information on how to apply for an abatement of underpayment penalties.
[5] See Ad. Code section 11-652(Real estate investment trusts (REITs) and regulated investment companies (RICs) are not eligible for the deduction allowed under IRC § 250 related to FDII.

Global intangible low-taxed income (GILTI)

For federal tax purposes, a U.S. shareholder of any CFC is required to include in gross income its GILTI, which is the excess of a U.S. shareholder's net CFC tested income for the tax year over the U.S. shareholder's net deemed tangible income return for the tax year.[6] A U.S. domestic corporation taxed as a C corporation [7] is allowed a deduction for a portion of its GILTI.[8] GILTI includes amounts earned directly by the U.S. shareholder as well as distributive shares of GILTI from flow-through entities.

Treatment of GILTI Income Under the Business Corporation Tax[9]

Net GILTI income, which is the GILTI recognized under IRC § 951A less the allowable IRC § 250(a)(1)(B)(i) deduction, is included in ENI under Subchapter 3-A. IRC § 78 dividends attributable to GILTI are not included in ENI. Taxpayers are required to attach a copy of their federal or pro-forma Form 8992, Form 8993 and Schedule I-1 of Form 5471, along with accompanying worksheets used to compute GILTI and, where applicable, FDII amounts, to their New York City tax return.

In computing the separate taxable income of combined group members to be reported on Form NYC-2-A/BC, members must compute their GILTI inclusion in accordance with the provisions of the Internal Revenue Code that govern the computation of taxable income for separate return purposes, but subject to United States Treasury Regulations section 1.1502-12(s). Members must compute their GILTI deduction in accordance with proposed section 1.1502-50(b) before the date of publication of the Treasury decision adopting those rules as final regulations in the Federal Register, and in accordance with the final regulations thereafter.

If the stock of a foreign corporation that generates GILTI is business capital, net GILTI income needs factor representation in the BAP in order to properly reflect the taxpayer's business income and capital in the City. Such net GILTI income must be included in the denominator but not the numerator of the BAP. Taxpayers must report this amount in the *Everywhere* column of Form NYC-2.5 or Form NYC-2.5A, Line 53 *Discretionary Adjustments*, and attach a statement to the return indicating the GILTI amounts included on this line.

If the stock of a foreign corporation that generates GILTI is investment capital, only the net GILTI income may be deducted as investment income in the computation of business income. Such net GILTI amount, like all other income from investment capital, is not included in the numerator or denominator of the BAP.

The net GILTI amount is disregarded for purposes of the "principally engaged" test used to determine a taxpayer's, or combined group's, eligibility for preferential rates and amounts available to manufacturers.

[IRC §§ 250(a)(1)(B) and 951A; Administrative Code §§ 11-652(8)(b)(2), 11-652(8)(a)(2-a)]

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[6] *See* IRC § 951A

[7] REITs and RICs are not eligible for the deduction allowed under IRC § 250 related to GILTI.

[8] *See* IRC § 250(a)(1)(B).

[9] As REITs and RICs are not allowed the IRC § 250 deduction related to GILTI, these entities must use GILTI, as opposed to the net GILTI income, when following the instructions in this section.