

GILTI

Impact on U.S. Individual Shareholders of CFC's



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GILTI Overview

Global Intangible Low Tax Income

GILTI captures most non-Subpart F income of controlled foreign corporations (“CFC’s”.)

IRC § 951A

GILTI is taxable to U.S. shareholders on a current basis, similar to Subpart F.

GILTI rules are onerous for non-corporate shareholders of CFC’s.

962 Election: Individuals can elect quasi-corporate treatment, but questions remain.

CFC and U.S. Shareholder

A foreign corporation is a controlled foreign corporation (“CFC”) if more than 50% of the company, by vote or value, is owned by U.S. shareholders.

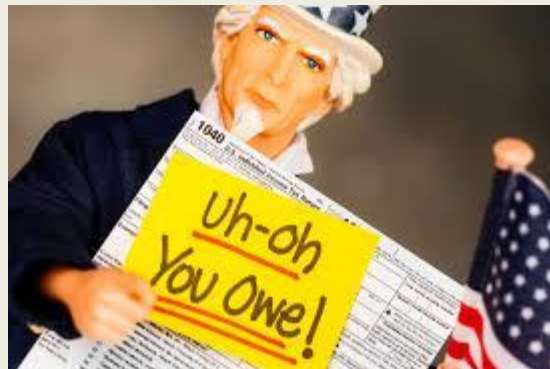
A U.S. shareholder is a U.S. person that owns, directly, indirectly or constructively, 10% or more of a foreign corporation.

A U.S. person is a U.S. citizen, a U.S. resident, a U.S. domestic corporation, or a U.S. domestic trust.

Note to U.S. Expats

U.S. citizens (including “accidental Americans”) and U.S. green card holders residing outside of the United States are U.S. tax residents, and thus are subject to the GILTI regime if they own shares of CFC’s. There is no de minimis rule and generally no exception for high-taxed income.

962 election generally cannot be made on an amended return. *But see* Dougherty v. Com’r, 60 T.C. 917 (1973) and GCM 36325.



GILTI Income Calculation

A U.S. shareholder of CFC's calculates GILTI in the aggregate for all CFC interests combined.

GILTI = Net CFC tested income minus deemed tangible income return

Net CFC tested income = aggregate of shareholder's pro rata share of tested income of each CFC over pro rata share of tested losses of all CFC's.

Rules in place coordinating with Subpart F to deny double benefit of tested losses.

Tested Income

Tested income = *all* income of the CFC, but *excluding* the following:

- Effectively connected income
- Subpart F income
- Subpart F income subject to high-tax exception
- Dividends from a related person (also excepted from Subpart F under look-through rule until 2020)
- Foreign oil and gas extraction income

minus properly allocable deductions.

CFC has a **tested loss** if properly allocable deductions exceed income.

Net Deemed Tangible Return

GILTI = Net CFC tested income minus net deemed tangible income return

Net deemed tangible income return = the excess of:

- 10% of the qualified business asset investment (“QBAI”) *over*
- Interest expense taken into account to the extent the such expense exceeds interest income included in CFC tested income.

QBAI = average adjusted tax bases in depreciable tangible property.

GILTI = Net CFC Tested Income – [(10% of QBAI) – interest expense]*

* If the amount of interest expense exceeds 10% of QBAI, deduction for 10% of QBAI is zero. See P. 644, FN 1539 of Conference Report, H.R. 1.

GILTI U.S. Corporations

U.S. corporations get deemed paid foreign tax credit under IRC § 960.

- Limited to 80% of foreign tax paid.
- Gross up of 100% of foreign tax under IRC § 78.
- Separate category of income and FTC.
- No carry-backs or carryovers of excess credits.

U.S. corporations benefit from a deduction of 50% of GILTI (reduced to 37.5% in 2026). IRC § 250(a)(1), (3).

Flat rate of 21% for U.S. corporations.

GILTI

U.S. Corporate Shareholder vs. U.S. Individual Shareholder

	Corporate Shareholder	Individual Shareholder
50% GILTI deduction	Yes	No
Deemed paid foreign tax credit	Yes (minimum foreign rate of 13.125% for 100% credit)	No
Tax rate on GILTI	10.5% (1/2 of 21% with 50% deduction)	37% (or lower marginal rate)

GILTI

U.S. Corporate Shareholder vs. U.S. Individual Shareholder

Between Subpart F income and GILTI, most income of CFC's will be taxable currently to individuals at their marginal rates.

962 election to the rescue? Partially



962 Election Basics

962 election in place since 1962 for Subpart F income, rarely used prior to 2018

Individual shareholders can elect to be taxed as a corporation with respect to Subpart F income and GILTI.

Year-to-year election. Permissible to elect in some years but not others.

Pay tax on GILTI at 21% corporate rate instead of 37% individual rate.

Deemed paid foreign tax credits for corporate tax (IRC § 960), with same limits as a corporate shareholder.

- Only 80% of taxes are creditable
- No carrybacks or carryforwards
- Separate basket for GILTI FTC

962 Election Basics (cont'd)

Previously taxed income (“PTI”) and increase in tax basis is created only to the extent of U.S. tax paid.

Distributions of prior GILTI in excess of U.S. tax paid will not be distributions of Previously Taxed Income (“PTI”) and thus will be taxable as dividends.

Prepare models:

- If CFC corporate tax rate is higher than United States corporate tax rate, likely that 962 should be elected.
- If CFC corporate is very low or zero, and non-qualified dividends will be paid to the U.S. individual shareholder in the foreseeable future, 962 likely should not be elected.

962 Election Questions

Will individuals making the 962 election be permitted to claim the 50% GILTI deduction? Under current regulations, most likely not.

Will dividends in excess of PTI paid from companies in non-treaty countries be qualified dividends (taxable at capital gains rates)? Not under current law.

How will states treat resident individuals who make the 962 election? If they ignore it, will they permit state adjustment to PTI and basis?

How does the direct foreign tax credit under IRC § Sec. 901, interact with the deemed paid credit under IRC § 960?

Strategy

Contribute Shares of CFC to U.S. Domestic C Corporation

Advantages as compared to 962 election:

- Deemed paid credits for foreign corporate taxes paid (same as 962 election)
- Tax rate on GILTI is 21% (same as 962 election)
- 50% GILTI deduction
- No U.S. tax on dividends paid from the foreign company in excess of PTI
- Qualified dividend rate on dividends paid to the individual (relevant if company located in a non-treaty country)
- Avoidance of state income tax on GILTI?

Strategy

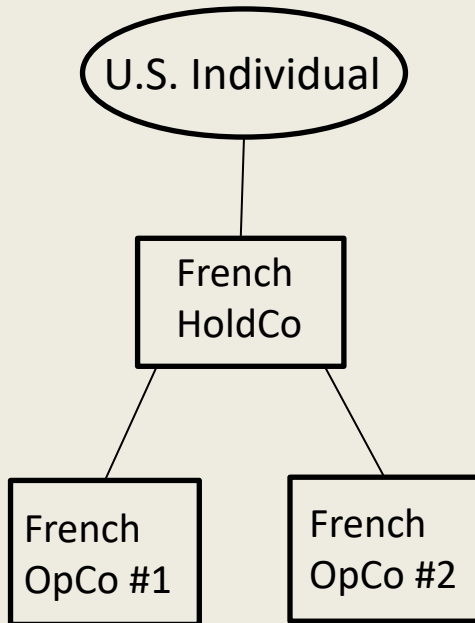
Contribute Shares of CFC to U.S. Domestic C Corporation

Disadvantages as compared to 962 election:

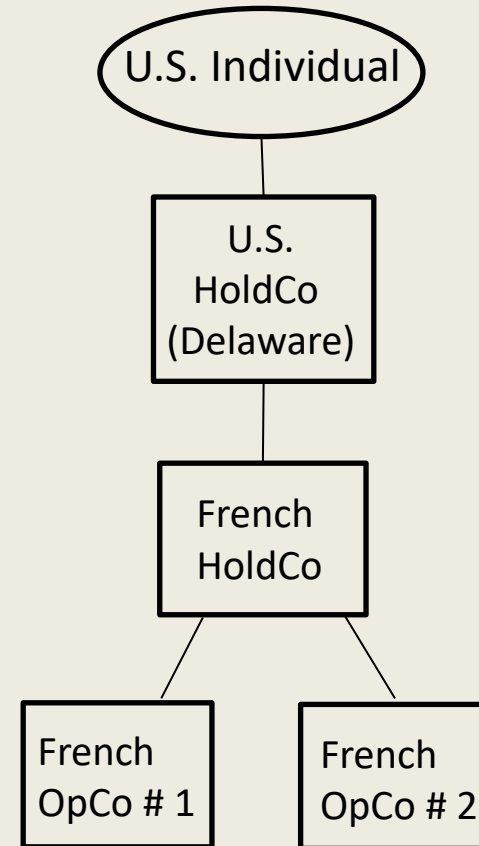
- Once CFC shares are contributed to a U.S. corporation, the individual is “stuck” with the C corporation structure. The 962 election is a year-to-year election.
- More compliance – IRC § 351 disclosures, corporate tax return required each year
- Management of personal holding company rules (IRC §§ 541 – 547)
- Elevated exposure to accumulated earnings tax (IRC §§ 531 – 537)
- Watch out for downward attribution
- Disallowance of direct foreign tax credits (IRC § 245A(d))?

Example

Before



After



Example

Example notes:

- U.S. HoldCo in Delaware or other state with no corporate tax.
- If exit plan is to sell the French group in a taxable transaction, the U.S. HoldCo structure could result in two levels of tax.
 - E&P treated as dividends under IRC § 1248 are not eligible for dividends received deduction under IRC § 245.
- All situations and scenarios should be modeled.

Thank You!

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