TREASURY DEPARTMENT PROVIDES DETAILS OF THE OBAMA ADMINISTRATION'S TAX CHANGE PROPOSALS AFFECTING MULTINATIONAL CORPORATIONS

On May 4, 2009, the Obama Administration released a summary of its tax change proposals. On May 11, 2009, the Treasury Department issued the General Explanations of the Administration's Fiscal Year 2010 Revenue Proposals (the "Green Book") to provide the details of the proposed changes. The proposed changes summarized below, if enacted, would have a profound adverse impact on U.S. multinational companies. These changes would generally be effective for taxable years beginning after December 31, 2010.

- *Deferral of Expense Deduction*. Under current law, a U.S. corporation generally may deduct expenses allocated to foreign sources before repatriating and paying U.S. taxes on the associated foreign earnings. The Obama Administration's proposal would require a U.S. corporation to defer deductions (other than research and development expenses) allocated or apportioned to foreign earnings until the associated earnings are repatriated. This proposal was previously introduced in 2007 by House Ways and Means Chairman Charles Rangel (H.R. 3970). If enacted, it could severely limit the benefits of keeping earnings offshore.

- *Foreign Tax Credits*. Under current law, a U.S. corporation is not required to aggregate foreign taxes and earnings and profits of all of its foreign subsidiaries. The Obama Administration's proposal would require both computations be made on a consolidated basis in determining available foreign tax credits, thus largely eliminating the benefits of repatriating highly taxed foreign earnings while keeping other foreign earnings offshore. A similar provision was also in H.R. 3970. Further, the proposal would prevent the separation of creditable foreign taxes from the associated foreign income. Such inappropriate separation could occur, for example, by having a foreign group of entities that are characterized in the United States differently from the treatment in foreign jurisdictions. This proposed change is similar to that in a proposed Treasury regulation issued in 2006. In addition, under the proposal, certain taxpayers subject to foreign levy (such as levy imposed only on oil income) may not be able to claim credit for the levy if the foreign country has no generally imposed income tax.

- *Check-the-Box Election*. Under the entity classification rules, a wholly owned foreign entity can be disregarded for U.S. tax purposes by making a check-the-box election. The Green Book states that this election has been used to migrate foreign earnings to low-tax jurisdictions, thereby avoiding current income inclusion by the U.S. parent company. Under the Obama Administration's proposal, generally a second- or lower-tier wholly owned foreign entity may be treated as a disregarded entity only if the single owner and that entity are created or organized in the same foreign country. The change would treat single-member entities that had made the check-the-box election prior to 2011 as being converted into corporations.

The Obama Administration's proposals described in the Green Book are far-reaching. It is difficult to predict what measures would eventually be enacted as proposed by the Administration.

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