March 21, 2016

The American Institute of CPAs (AICPA) submits the below comments in response to the proposed regulations (REG-109822-15) published on December 23, 2015 regarding annual country-by-country reporting by United States (U.S.) persons that are the ultimate parent of a multinational enterprise (MNE) group. These comments were developed by the Base Erosion and Profit Shifting (BEPS) Task Force of the AICPA International Taxation Technical Resource Panel and approved by the AICPA Tax Executive Committee.

The AICPA respectfully requests that the Department of the Treasury (Treasury) consider the following recommendations:

1) Allow U.S. MNE groups to elect on a voluntary basis to apply the proposed regulations for tax years beginning on or after January 1, 2016 and before the effective date of the final regulations;

2) Clarify that a U.S. MNE group’s reporting is based solely upon its own annual accounting period and is not contingent on the timing of the annual accounting periods of its foreign constituent entities;

3) Clarify the classification of certain assets as tangible, intangible or cash equivalents;

4) Clarify issues related to the reporting of the number of full-time equivalent employees for each tax jurisdiction included on Form XXXX, Country-by-Country report;
5) Confirm the status of U.S. Possessions and Territories and whether their treatment as foreign jurisdictions is correct; and

6) Allow a National Security Exception for information contained in the required Country-by-Country reports.

**Detailed Recommendations and Analysis**

1. **Allow U.S. MNE groups to elect to apply the proposed regulations for tax years beginning on or after January 1, 2016 and before the effective date of the final regulations**

The AICPA recommends that the Treasury allow U.S. MNE groups that are required to submit country-by-country (CbC) reports to the Internal Revenue Service (IRS) under proposed regulations published December 23, 2015 (the “Proposed CbC Regulations”) to voluntarily elect to apply these regulations to tax years beginning on or after January 1, 2016 and before the effective date of the final regulations.

The Proposed CbC Regulations include an effective date of the first taxable year beginning after the rules are made final. This finalization will occur no earlier than sometime during calendar year 2016, meaning the earliest possible implementation of the CbC reporting requirement cannot occur prior to the 2017 calendar year for U.S. MNE groups with a calendar year end. Thus, the first CbC report filing for such U.S. MNE groups would not occur until sometime in 2018 (with the filing of the group’s 2017 U.S. tax return).

Numerous other countries around the world have announced their intentions, however, to implement the timing of the CbC reporting requirement recommended by the Organization for Economic Co-operation Development’s (OECD) BEPS project. The BEPS project recommends CbC reporting for taxable years beginning on or after January 1, 2016, with the first filing due by December 31, 2017.

Under the BEPS recommendations, if a particular country is not requiring multinational companies headquartered in its jurisdiction to submit CbC reports, then local reporting by a foreign subsidiary is potentially required.

The other OECD members have taken inconsistent approaches to this issue of non-conforming reporting year requirements. A few countries, such as Australia, have included provisions that may exempt U.S. MNE groups from needing to file 2016 CbC reports (for example, by tying the local CbC “piggyback” rule to the ultimate parent jurisdiction’s intention to implement CbC reporting and not to the effective date thereof). Others, such as France, have indicated that all companies must comply and submit a CbC report for calendar year 2016 and that they may not provide a transitional rule for delays in reporting implementation at the MNE group parent level.
Given the conflicting approaches taken by our trading partners on this issue and the comparatively delayed effective date for U.S. MNE groups’ CbC reporting in the United States, U.S. taxpayers could find themselves subject to multiple CbC report filing obligations in the interim transition periods. The CbC reports filed in those other jurisdictions would likely require preparation according to reporting requirements in those countries, and therefore under a different set of rules than those contained in the Proposed CbC Regulations, which will increase the administrative and compliance burden for those affected U.S. taxpayers. In addition, any local filing would probably fail to provide the same level of information privacy protections that inure to U.S. taxpayers under treaty-based exchange provisions and information exchange arrangements facilitated through Treasury and the IRS. In short, the potential inability of U.S. MNE groups to file in the U.S. for the 2016 taxable year presents the risks of unnecessary and costly duplicative filings and insufficient information safeguards. This result would undermine the extensive and careful work performed by Treasury over the course of the BEPS project to ensure that U.S. taxpayers are not unduly burdened or targeted by the project, and that U.S. taxpayers’ information is not inappropriately shared or put at risk.

Therefore, the AICPA requests that Treasury allow U.S. MNE groups that wish to voluntarily file for the 2016 calendar year to elect to apply the Proposed CbC Regulations and file CbC reports with the IRS for taxable years beginning on or after January 1, 2016 and before the effective date of the final regulations. In addition, we request that the IRS establish procedures to exchange these reports with applicable foreign tax authorities under the terms and conditions included in the proposed regulations published December 23, 2015.

2. Clarify that a U.S. MNE group’s reporting is based solely upon its own annual accounting period and is not contingent on the timing of the annual accounting periods of its foreign constituent entities

The proposed regulations contain the following effective date language:

“The rules of this section apply to taxable years of ultimate parent entities of U.S. MNE groups that begin on or after the date of publication of the Treasury decision adopting these rules as final regulations in the Federal Register and that include annual accounting periods determined under section 6038(e)(4) of all foreign constituent entities and taxable years of all domestic constituent entities beginning on or after the date of publication of the Treasury decision adopting these rules as final regulations in the Federal Register.”

Read literally, a reader might interpret the “and that include” language as a conjunctive requirement to the effective date of the final regulations. Under this interpretation, a U.S. MNE

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1 All section references in this letter are to the Internal Revenue Code of 1986, as amended, or the Treasury regulations promulgated thereunder.
group would not begin reporting until the first taxable year of the U.S. consolidated group that affirmatively includes a “pass-through” year-end of all of its foreign constituent entities.

The effective date provision seems intended to establish reporting for all of the majority-owned businesses whose taxable years are determined by the U.S. MNE group’s U.S. taxable year (for example, under section 898 for controlled foreign corporations and under section 706(b) for partnerships). For example, assuming the regulations are finalized on September 30, 2016, a calendar-year U.S. MNE group would file a report for its 2017 calendar year because its next taxable year after the finalization date begins on January 1, 2017. Assume, however, that the U.S. MNE acquires a foreign constituent entity (CFC1) with a year end of June 30 during the latter half of 2017. CFC1 is a specified foreign corporation, and therefore its annual accounting period under 6038(e)(4) is its U.S. taxable year as determined under section 898. Unless CFC1’s local accounting period is immediately required to conform to the U.S. MNE’s calendar year, CFC1’s local accounting and tax reporting would not close until June 30, 2018. Under the section 898 rules, CFC1’s taxable year for U.S. purposes also would not (absent a section 338 election) automatically conform to the U.S. MNE group’s calendar year; instead, CFC1 would complete its existing year ending June 30, 2018 and then have a short U.S. taxable from July 1, 2018 to December 31, 2018 to transition into its required U.S. taxable year.

In the foregoing example, the suggested literal reading of the Proposed CbC Regulations’ effective date would result in not requiring the filing of the entire U.S. MNE group’s CbC report for the 2017 year because this single, new addition to the U.S. MNE Group is not yet required to conform its accounting period to that of the U.S. MNE group. That is, because CFC1’s annual accounting periods are not included in the U.S. MNE group year ending December 31, 2017, the “and that include” language in the Proposed CbC Regulation arguably would eliminate the need for the U.S. MNE group to file a CbC report for its 2017 calendar year. This result is likely not the intention or desired outcome of Treasury.

To remove this ambiguity, we propose modifying the effective date language to clarify that a U.S. MNE group is required to file a CbC report for each of the ultimate parent’s U.S. taxable years beginning on or after the effective date in the final regulations and where such report includes (only) constituent entities whose accounting periods or taxable years, as applicable, end with or within the ultimate parent’s year. In the example described above, the initial reporting period which includes the CFC1 is calendar year 2018. As this result illustrates, this approach generally harmonizes the reporting required for the CbC report with the separate tax returns and informational forms (e.g., Form 5471, Schedule K-1) that are included with a U.S. consolidated group’s U.S. federal income tax return.

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3 See Treas. Reg. § 1.6038-2(e).
4 Longstanding proposed regulations under section 898 would allow earlier re-“testing dates” for 898 purposes in some contexts, but they are explicitly prospective in application.
3. Clarify the classification of certain assets as tangible, intangible or cash equivalents

The Proposed CbC Regulations require taxpayers to report the “Net book value of tangible assets other than cash or cash equivalents.” Under the BEPS recommendations, additional assets, including intangible property, are excluded from the definition of tangible assets. There are certain assets, however, that are not easily categorized as tangible, intangible or cash equivalents - an example of which is trade receivables. We request that Treasury provide an expanded definition of tangible assets to clarify the term’s scope and help avoid any misunderstanding on the information required on the CbC reports.

4. Clarify issues related to the reporting of the number of full-time equivalent employees for each tax jurisdiction included on Form XXXX, Country-by-Country report.

The AICPA recommends that Treasury provide further guidance and clarification related to the following issues connected to the reporting of the number of full-time equivalent employees:

a. For direct hires, how many hours of work is required to count as a full-time equivalent employee? Is it the traditional measure of 40 hours per week? The Affordable Care Act measure of 30 hours per week? Or some other measure?

b. May the hours of work considered to equal a full-time equivalent employee vary by entity based on local custom or law in foreign jurisdictions?

c. Please provide examples of what Treasury believes are reasonable methods for properly counting independent contractors as full-time equivalent employees.

d. Must the election to include independent contractors in the count of full-time equivalent employees apply to all jurisdictions/entities or may it vary based on differing employment situations in foreign jurisdictions as long as the election is applied consistently from year to year?

e. How should a MNE count workers hired through a temporary employment agency or leasing company?

f. How should a MNE count workers employed by independent subcontractors?

5. Confirm the status of U.S. Possessions and Territories and whether their treatment as foreign jurisdictions is correct

The Proposed CbC Regulations require taxpayers to report the tax jurisdiction of their constituent entities, as well as the jurisdiction where the constituent entity is organized or created (if different from the tax jurisdiction). The definition of a tax jurisdiction “is a country or a jurisdiction that is not a country but that has fiscal autonomy.” This “fiscal autonomy” concept is not further defined
and is not a commonly used term in the U.S. federal tax system. We therefore, request Treasury provide further detail as to its meaning. We also request that Treasury specifically address whether the U.S. possessions and territories (which are traditionally considered “foreign” for U.S. federal tax purposes) are included in CbC reports as separate jurisdictions or if entities organized therein are treated as United States constituent entities.

6. Allow a National Security Exception for information contained in the required Country-by-Country reports

The AICPA recommends that Treasury allow U.S. multinational companies who are required to submit CbC reports to the IRS under proposed regulations issued December 18, 2015 (REG-109822-15) to remove or provide in an alternative summary format, information which may have national security implications.

The proposed regulations “request comments with respect to the procedures that a U.S. person should be required to follow in order to demonstrate a national security reason to receive an exception from filing some or all of the information otherwise requested by Form XXXX, Country-by-Country report.”

The AICPA recommends that instead of requiring taxpayers to follow an annual procedure to request an exception, all activities performed under a U.S. government contract issued by a specified list of agencies and departments receive a blanket national security exception. A possible (non-inclusive) list would consist of The Department of Defense, Department of Homeland Security, Department of State and all U.S. intelligence agencies (such as the Central Intelligence Agency and the National Security Agency).

Alternatively, the AICPA recommends that the U.S. Government’s contracting officer, agency or department determine the exception at the outset of the contract. Even if a taxpayer is required to initiate the request, the national security exception should apply to all subsequent years for that contract(s) from the exception grant date going forward until the conclusion of that contract.

The AICPA believes that if an exception is granted for a contract, then no information directly related to that contract require reporting on Form XXXX, Country-by-Country report. We believe that even a small amount of information from these contracts would allow adverse parties and nation states to analyze and evaluate U.S. operations and capabilities.

The focus of the CbC report is to provide transparency of corporate activities to assist governmental bodies with assessing BEPS and transfer pricing audit risks. However, work performed by a contractor of a U.S. Government contract generally requires performance through a U.S. entity, or a branch of a U.S. entity when performed within a foreign jurisdiction. Frequently (but not always), such work performed outside of the U.S. is covered by a SOFA (a Status of Forces Agreement) or other diplomatic income tax exemption, and would not represent taxable income in the foreign jurisdiction. But even when such income is taxable in the foreign
jurisdiction, the U.S. Government requirement that such contractor activities are carried on through the branch of a U.S. entity would generally exclude such activities from the type that is the subject of the BEPS concerns. Therefore, we believe exempting these activities from the CbC report is an appropriate approach. If Treasury considers such an exception overly broad, then we recommend that information related to these contracts is aggregated and reported as U.S. activity. Alternatively, if Treasury believes that reporting these activities as U.S. activities would not be appropriate, then the AICPA recommends reporting only the country and gross revenue on Form XXXX, Country-by-Country report.

The AICPA suggests that in the interest of national security, the broadest possible exception is necessary - as opposed to limiting it solely to top-secret or secret activities. Information on activities as innocuous as providing food and lodging to personnel may allow third parties to determine not only a U.S. national security presence, but an approximate size of that presence within a country. Protecting data on these support activities is as important as top-secret and secret activities in terms of preventing adverse parties and nation states from gaining unnecessary access to this type of information.

The AICPA also notes that U.S. national security interests include work performed by U.S. contractors for U.S. alliances (such as NATO) and alliance partners, such as the U.K. Ministry of Defence. The AICPA recommends that the national security exception apply to the reporting of activities in support of such alliances and alliance partners.

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The AICPA is the world’s largest member association representing the accounting profession, with more than 412,000 members in 144 countries and a history of serving the public interest since 1887. Our members advise clients on federal, state and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America’s largest businesses.

We appreciate your consideration of these comments and welcome the opportunity to discuss these issues further. Please feel free to contact me at (801) 523-1051 or tlewis@sisna.com; Blake Vickers, Chair, AICPA International Taxation Technical Resource Panel, at (713) 753-5493 or blake.vickers@kbr.com; or Jonathan Horn, Lead Technical Manager – AICPA Tax Policy & Advocacy, at (202) 434-9204 or jhorn@aicpa.org.

Respectfully submitted,

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