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State and Local Tax Update HLB North American Tax Conference

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About Green Hasson Janks

At Green Hasson Janks, we believe that collaboration is the foundation for success. We work as a business advocate for our clients – providing personalized service and building long-term relationships to help position our clients for the future.

- Accountants and Business Advisors since 1953
- Named a “2012 Best of the Best” firm by Inside Public Accounting
- Named “Best Places to Work” by the Los Angeles Business Journal 2008, 2009 , 2011, 2012 and 2013
- Named a “Beyond the IPA 100 Firm” by Inside Public Accounting
- Named a “Fastest-Growing” firm in the 2012 and 2011 Beyond the IPA 100 rankings
- Named “Beyond the Top 100: Firms to Watch” and “Top Firms: West” in the 2013 Accounting Today Top 100 Firms
- Ranked 20th largest CPA firm in Los Angeles County 2012
- Diverse firm of 12 partners and approximately 100 staff

Agenda

1. California Water's-Edge Election
2. Recent Landmark Decisions/Legislation

Water's-Edge Election – General Requirements

- California by default requires filing on a worldwide unitary combined reporting basis with option of making a water's-edge election
- Election must be made on an original timely filed return (FTB Form 100W).
- Election is in affect for an 84 month period (7 Full Tax Years)
- After initial 84 month period has expired, election is on a year by year basis
- Taxpayer must elect back into a worldwide filing – 84 months
- Election is generally limited to U.S. Domestic entities with exceptions
- Entities eligible to make a water's-edge election include:
 - C Corporations
 - S Corporations

Water's-Edge Election – Determination

- Who should be included in water's-edge filing?
- What are the financial projections (e.g. income and apportionment) for the next 7 years?
- What are the future plans for the business domestic vs. foreign?
- Are there any plans to repatriate cash to the US during the next 7 years?
- Companies should model out tax impact of election based on the best available information
- Important to understand the mechanics of filing on a worldwide vs. water's-edge basis

Water's-Edge Election – Who is Included?

- Two Criteria for inclusion in water's-edge combined report
 - Must be a unitary member
 - Must meet one of the four fully inclusion tests or two of the partial inclusion tests

Water's-Edge Election – Who is Included? (cont.)

- Fully included members:
 - Foreign Sales Corporations (“FSC”)
 - Corporations regardless of where incorporated with 20% or more average apportionment factors in US.
 - Corporations incorporated in the US
 - Export Trade Companies (“ETC”)
- Partially Included Members:
 - Controlled Foreign Corporations with Subpart F Income (IRC Section 952)
 - Foreign corporations with US Source Effectively Connected Income (“ECI”) – Treaty based protection does not apply

Water's-Edge Election – Traps for the Unwary

- Dividends paid within a particular year
 - Full elimination if dividends are paid from earnings that were included in the combined report
 - 75% DRD if dividends are paid from other earnings
 - For partially included members, dividends paid in a particular year are first deemed paid from earnings included in combined report
- Dividends paid from prior year earnings (“LIFO” Approach)
 - Dividends are deemed first paid out of current year earnings and then prior year earnings in reverse chronological orders subject to either full elimination or 75% DRD

Water's-Edge Election – Traps for the Unwary (cont.)

- Transfer pricing issues when a member joins or leaves water's-edge combined report
- FDAP Income no longer includable in return as of February 2007
- Foreign investment interest offset
- Corporate partners are required to include income from foreign partnerships to the extent the corporate partner is included in the combined report

Landmark Decisions/Legislation

- Gillette v. FTB
 - California Court of Appeals held that Multistate Tax Compact is binding
 - Taxpayers should consider filing protective refund claims for prior years
 - California has repealed MTC election prospectively
 - California Supreme Court has granted certiorari

Landmark Decisions/Legislation (cont.)

- Nortel Networks, Inc. v. SBE
 - Written software agreements meeting certain criteria are exempt from sales/use tax
 - Prewritten software may be exempt from sales/use tax regardless of how delivered if the software meets the definition of a Technology Transfer Agreement (“TTA”)
 - A “TTA” is defined as any agreement under which a person who holds a patent or copyright interest assigns or licenses to another person the right to make and sell a product or use a process that is subject to the patent or copyright interest

Landmark Decisions/Legislation (cont.)

- Oregon “Tax Haven” Legislation
 - For tax years beginning on or after January 1st, 2014, entities incorporated in certain “Tax Haven” jurisdictions must be included in the Oregon consolidated return if they meet certain unitary characteristics

Landmark Decisions/Legislation (cont.)

- Repeal of California Enterprise Zone Credit
 - Enterprise Zone Credit Program (“EZ”) repealed as of January 1st, 2014
 - Taxpayers will have until January 1st, 2015 to claim EZ credits for employees hired prior to January 1st, 2014
 - EZ credits not utilized as of January 1st, 2015 can be carried forward for 10 years

Landmark Decisions/Legislation (cont.)

- Repeal of California Enterprise Zone Credit (continued)
 - New Hiring Credit implemented as of January 1st, 2014
 - 35% of wages paid in first five years up to \$56,000
 - Wages must be between 150% and 300% of the California hourly minimum wage
 - Businesses not eligible include retailers, food service, casinos and temp agencies
 - Eligible employees must have received the federal earned income credit, be a veteran, been long term unemployed or must have been incarcerated
 - Credit must be requested within 50 days of employment and claimed on an original filed return

Landmark Decisions/Legislation (cont.)

- Repeal of California Enterprise Zone Credit (continued)
 - Partial Sales/Use Tax Exemption as of January 1st, 2014
 - Exemption on approx. 1/2 of the sales/use tax due on qualified manufacturing and R&D equipment
 - Exemption not available for financial institutions and agricultural taxpayers
 - Exemption applies to assets purchased between July 1st, 2014 and December 31, 2018 with certain exceptions

Questions?

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Akash Sehgal leads the firm’s state and local tax practice with a focus on multistate income and franchise tax, sales and use tax and credits and incentives. He has over fifteen years of state and local tax experience with two Big 4 firms in Los Angeles and Seattle.

Akash assists his clients on complex state and local tax issues related to transactional planning, mergers and acquisitions, general day-to-day consulting and compliance. He has significant experience dealing with state tax issues in California, Oregon, Idaho and Washington and local city taxes including the Los Angeles City Business Tax. He is a frequent speaker for a variety of tax associations including Tax Executive Institute (“TEI”) and the Council on State Taxation (“COST”).

Akash has a Bachelor of Science degree in accounting from California Polytechnic University, Pomona.