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THE ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION

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US Tax Reform: Impact on Private Funds

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BACKGROUND ON US TAX REFORM

- Bill formerly known as the Tax Cuts and Jobs Act ("TCJA") signed December 22, 2017
- Comprehensive tax reform affecting virtually all taxpayers
- 7 weeks from start to finish
- Fast pace/process led to drafting errors, lack of clarity, gaps, overlaps and unintended consequences

THE AFTERMATH

- Congress will spend 2018 fixing these problems
  - Technical corrections
  - Legislative changes
- Treasury/IRS regulatory and guidance projects to interpret and implement
- This means risk and opportunity for you
  - Planning around the new law
  - Chances to clarify/shape
- Think outside the box!

MAJOR THEMES

- Most significant spread between corporate and individual rates since 1982
- Different tax treatment for taxpayers receiving the same or similar types of income
- Increased complexity in the Code for business taxpayers
- Significant variations in treatment of similar transactions from year to year built into the Act
- Major changes for foreign related transactions

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AGENDA

- Fund and Management Company Issues
  - Three-year holding period for long-term capital gains treatment for carried interests
  - Elimination of miscellaneous itemized deductions
  - 20% pass-through income deduction (new Section 199A)
  - One-time tax on accumulated foreign earnings
  - Limitation on deductibility of state and local taxes

AGENDA (CONTINUED)

- Portfolio Company and Investment Related Issues
  - New lower tax rate on US corporations
  - New limitations on interest deductibility
  - Full expensing for certain capital investments
  - Changes to rules relating to corporate net operating losses (“NOLs”)
  - Treatment of gain on sale of partnership interest by non-US partner
  - Changes to US “controlled foreign corporation” (“CFC”) rules
  - New participation exemption for dividends from foreign subsidiaries
  - Addition of “global intangible low-taxed income” (“GILTI”) to the US anti-deferral regime
  - Foreign-Derived Intangible Income (“FDII”)

Fund and Management Company Issues

NEW 3-YEAR HOLDING PERIOD FOR LONG-TERM CAPITAL GAINS TREATMENT FOR CARRIED INTERESTS

- TCJA imposes 3-year holding period requirement to treat capital gain derived from certain partnership profits interests as long-term capital gain
  - Consequence is short-term capital gain treatment, taxable at ordinary income rates
  - No grandfathering of existing interests
  - Prior to the change, the holding period requirement was one year
  - Applies to private equity and hedge funds, though with potentially limited practical effect

NEW 3-YEAR HOLDING PERIOD FOR LONG-TERM CAPITAL GAINS TREATMENT FOR CARRIED INTERESTS (CONTINUED)

- Affected profits interests include those transferred or held in connection with performance of substantial services in the trade or business of raising or returning capital and investing in, or disposing of, or developing, securities, commodities, debt instruments, options, derivatives, real estate held for investment, or any interest in a partnership to the extent of the partnership's interest in any of the foregoing assets
  - Generally does not apply to profits interests in operating companies
  - Applies to private equity and hedge funds, though with potentially limited practical effect

NEW 3-YEAR HOLDING PERIOD FOR LONG-TERM CAPITAL GAINS TREATMENT FOR CARRIED INTERESTS (CONTINUED)

- 3-year holding period appears to apply both with respect to asset sales at the partnership level as well as to direct sales of affected partnership interest
- Absent future administrative guidance to the contrary, a holder of a profits interest who is subject to the new rule and has held the profits interest for less than three years may nevertheless achieve long-term capital gain treatment with respect to allocations of capital gain from a partnership if the partnership's holding period for the sold asset is more than three years

NEW 3-YEAR HOLDING PERIOD FOR LONG-TERM CAPITAL GAINS TREATMENT FOR CARRIED INTERESTS (CONTINUED)

- Availability of long-term capital gains rates for qualified dividend income apparently unaffected
- Under special rule, partnership interest that otherwise would be subject to the three-year holding period requirement is excepted if held by a person employed by another entity that is engaged in a trade or business (other than one of the trades or businesses mentioned above) — e.g., an operating business — and provides services only to such other entity

NEW 3-YEAR HOLDING PERIOD FOR LONG-TERM CAPITAL GAINS TREATMENT FOR CARRIED INTERESTS (CONTINUED)

- Thus, in the private equity setting it appears that portfolio company executives or other employees may be able to receive a carried interest in an upper-tier partnership without triggering the three-year holding period requirement, notwithstanding that the partnership itself is engaged in a trade or business of investing
- Precise scope of this rule is uncertain
- Exceptions:
  - Interests held, directly or indirectly, by a corporation
  - Capital interests that provide a right to share in partnership capital commensurate with the amount of capital contributed or with the amounts included in income as compensation under Section 83

NEW 3-YEAR HOLDING PERIOD FOR LONG-TERM CAPITAL GAINS TREATMENT FOR CARRIED INTERESTS (CONTINUED)

- Under a plain reading of the statute, the first exception appears to encompass S corporations
  - IRS may take a position that S corporations are not eligible for the exception
- Currently it is unclear whether allocations of income, as opposed to contributions to capital, may give rise to a capital interest that would be eligible for the second exception
  - Plain language of the statute appears to focus solely on capital contributions

ELIMINATION OF MISCELLANEOUS ITEMIZED DEDUCTIONS

- Prior Law: individuals were permitted to deduct certain miscellaneous itemized deductions (e.g., investment management fees) to the extent that such deductions exceeded 2% of adjusted gross income
- TCJA: effective for tax years after December 31, 2017 and before January 1, 2026, miscellaneous itemized deductions, including investment management fees, no longer will be deductible for individuals, trusts, and estates

199A DEDUCTION: INTRODUCTION

- Potentially applies to income earned through partnerships (including LLCs taxed as partnerships), S corporations and sole proprietorships
  - The deduction is allowed to itemizers and non-itemizers alike
  - Sunsets at the end of 2025
- For purposes of this presentation, we assume a taxpayer does not have cooperative dividends, REIT dividends, or publicly traded partnership income, though the deduction potentially applies to such income as well

199A DEDUCTION: INTRODUCTION (CONT'D)

- The potential Section 199A deduction with respect to any "qualified trade or business" of the taxpayer generally is equal to the lesser of:
  - (1) 20 percent of the taxpayer's "qualified business income" with respect to such qualified trade or business; or
  - (2) The greater of:
    - 50 percent of the W-2 wages with respect to the qualified trade or business; or
    - The sum of 25 percent of the W-2 wages with respect to the qualified trade or business, plus 2.5 percent of the unadjusted basis immediately after acquisition of all qualified property
- Subject to overall cap of 20 percent of (i) taxable income over (ii) net capital gain

199A DEDUCTION: QUALIFIED TRADE OR BUSINESS

- Includes any trade or business, unless a specific exception applies
- Exceptions:
  - Specified Service Trade or Business. Generally excludes any trade or business involving the performance of services in the fields of health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any other trade or business where the principal asset of the trade or business is the skill of one or more of its employees or owners (other than architecture and engineering) (a “specified service trade or business”)
  - Employees. Excludes the trade or business of performing services as an employee
  - Investment Management, Trading and Dealing. Excludes trades or businesses that involve the performance of services that consist of investing, investment management, trading, or dealing in securities, partnership interests or commodities
- Notwithstanding the general exception, a specified service trade or business may be a qualified trade or business with respect to a taxpayer if the taxpayer’s taxable income is less than $415,000 (in the case of a joint filer) or $207,500 (in the case of a single filer)
  - Phase-outs are applied, however, as the taxpayer’s taxable income rises above $315,000 to $415,000 (in the case of a joint filer) or $157,500 to $207,500 (in the case of a single filer)

199A DEDUCTION: QUALIFIED BUSINESS INCOME

- Generally determined as the net amount of items of income, gain, deduction, and loss that are "effectively connected" with the conduct of a qualified trade or business in the United States
  - Note: generally intended to incentivize conduct of business activity in the US
  - Although beyond the scope of this presentation, care must be taken to structure foreign operations tax efficiently and may involve a different choice of entity than for US operations
  - Section 199A imports concepts of Code Section 864(c) (part of the "inbound" international tax rules) to determine whether income is effectively connected with a qualified trade or business
- Excludes most passive-type income
  - Capital gain or loss, dividends, interest (other than properly allocable to a trade or business (e.g., a lending business)), commodities gains, foreign currency gains, income from notional principal contracts, any amount received from an annuity (other than in connection with a trade or business), and any item of deduction or loss properly allocable to any of the foregoing
  - Notably, does not exclude rental income
- Also excludes reasonable compensation and guaranteed payments

199A DEDUCTION: W-2 WAGES

- Generally includes wages properly reportable on Form W-2 to the extent such wages are properly allocable to qualified business income
- To qualify as W-2 wages for purposes of Section 199A, the wages must be reflected on a Form W-2 or Form W-2c within 60 days of the due date of Form W-2 with the Social Security Administration (i.e., generally within 60 days of January 31st of the taxable year following the year in which the wages are paid)
- Issues may arise for pass-through businesses with profits interest holders that have historically reported compensation income to such holders as wages on Form W-2 rather than as guaranteed payments on Form K-1
  - Unlocking the Section 199A deduction may require restructuring of profits interest arrangements so that sufficient W-2 wages may be paid at the operating entity level
- Each partner in a partnership or shareholder in an S corporation takes into account such person's "allocable share" of the W-2 wages for purposes of computing such person's deduction under Section 199A

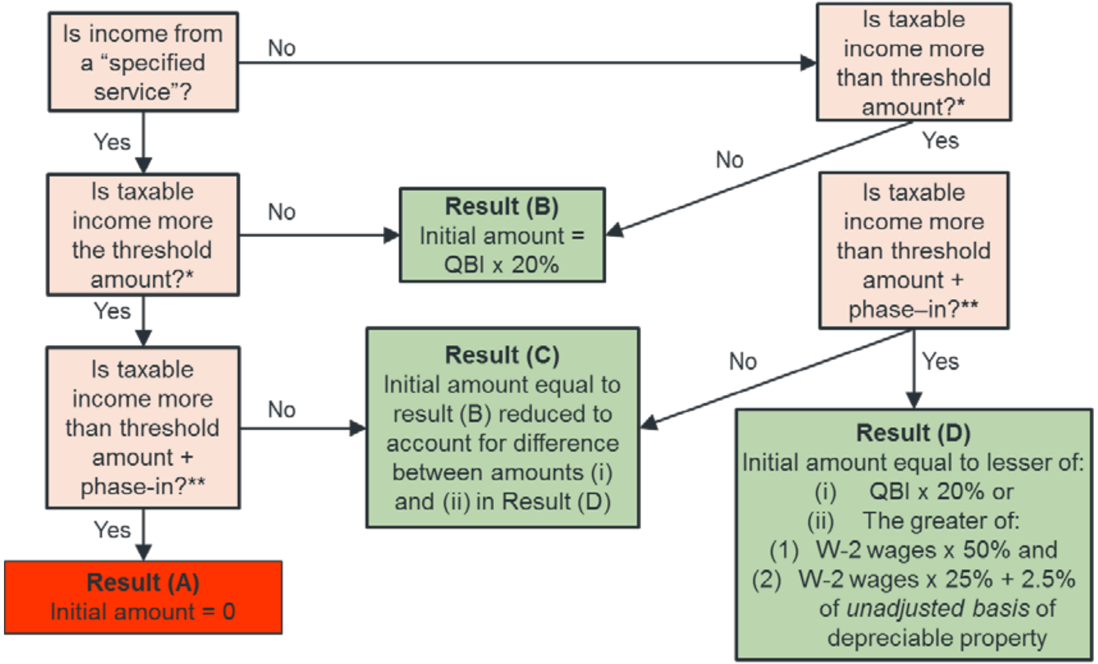
199A DEDUCTION: QUALIFIED PROPERTY

- Generally includes the depreciable tangible property held by and available for use in the qualified trade or business at the close of the taxable year and used in the production of qualified business income during such year
- The unadjusted tax basis of such property may be used to support a Section 199A deduction generally for the later of 10 years from the date the property was first placed in service or the last day of the last full year of the recovery period for such property under Code Section 168 (MACRS)
- The addition of the qualified property concept in Section 199A was added in Conference and apparently is designed to benefit the real estate industry, though the provision potentially benefits capital-intensive operating businesses as well

199A DEDUCTION: SIGNIFICANCE OF THRESHOLD AMOUNTS

- Generally, if taxable income is below the applicable threshold amounts:
  - 199A deduction may be available with respect to a specified service trade or business; and
  - W-2 and/or qualified property conditions do not apply
- Threshold amounts are inflation-adjusted and currently are $315,000 for joint filers and $157,500 for single filers
- Phase-in of limits applies as the taxpayer’s taxable income rises above $315,000 to $415,000 (in the case of a joint filer) or $157,500 to $207,500 (in the case of a single filer)

SECTION 199A DEDUCTION: BASIC DECISION TREE



* Threshold Amount is $315,000 of taxable income if filing jointly and $157,00 in all other cases

** Phase-In is $100,000 of taxable income if filing jointly and $50,000 in all other cases

Note: deduction subject to overall cap of 20 percent of (i) taxable income over (ii) net capital gain

ONE-TIME TAX ON ACCUMULATED FOREIGN EARNINGS

- TCJA imposes one-time transition tax on certain post-1986 deferred foreign earnings through a deemed repatriation of such earnings
- Any 10 percent United States shareholder (by vote) of foreign corporation as of December 31, 2017 must include in income for taxable year 2017 its proportionate share of the foreign corporation's undistributed earnings if such foreign corporation is a CFC or is a foreign corporation with at least one 10 percent US corporate shareholder
- Tax Rates:
  - For corporate shareholders, 15.5 percent for earnings invested in cash or cash equivalents and 8% for earnings invested in non-cash assets
  - For individuals, 17.5 percent for earnings invested in cash or cash equivalents and 9.05% for earnings invested in non-cash assets

ONE-TIME TAX ON ACCUMULATED FOREIGN EARNINGS (CONT'D)

- Election to pay the tax without interest over eight-year period with significant back-loading (i.e., 8 percent in each of the first five years, 15 percent in the sixth year, 20 percent in the seventh year, and 25 percent in the eighth year)
- Applies to post-1986 E&P of the foreign corporation, other than ECI (and to the extent not otherwise previously taxed), as of November 2, 2017 and December 31, 2017, whichever is greater
  - An E&P deficit from one CFC may be used by a United States shareholder to offset E&P from another CFC
  - E&P deficits are also shared within an affiliated group

ONE-TIME TAX ON ACCUMULATED FOREIGN EARNINGS (CONT'D)

- Mainly aimed at ending deferral of the taxation of offshore earnings of multinational corporations
- However, may result in phantom income (i.e., income without a related cash distribution) for, e.g., US investors in a US fund where the fund held shares of a foreign corporation amounting to a 10 percent voting interest as of December 31, 2017, even if such investors' indirect interests in the foreign corporation were below 10 percent as of such time

LIMITATION ON DEDUCTIBILITY OF STATE AND LOCAL TAXES

- TCJA significantly limits an individual's ability to deduct state and local taxes through 2025
- TCJA permits deductions of up to $10,000 for income, property and sales taxes
  - $10,000 cap does not apply to property and sales taxes that are attributable to the individual's trade or business or Section 212 investment activity

Portfolio Company and Investment Related Issues

LOWER CORPORATE TAX RATE

- Tax rate on US corporations reduced from 35% to 21% effective for taxable years beginning after December 31, 2017
- Even lower rates apply to certain types of foreign derived income of US corporations (as discussed below)
- Purpose of lower rates is to limit expatriation transactions and attract new investment to the United States

NEW LIMITATIONS ON INTEREST DEDUCTIBILITY

- Old section 163(j) (so-called “earnings stripping rules”) repealed
  - Under prior law, US corporations owned by foreign entities the interest expense of which exceeded 50% of EBITDA could deduct interest paid to related foreign persons only if their debt to equity ratio was less than 1.5 to 1
- New 163(j) introduces substantial limitations on deductibility of business interest that apply in domestic and international situations alike (and apply both to pass-throughs and corporations)
- Potentially far broader application of new limitations on interest deductibility as compared with old rules
- No grandfathering of existing debt

NEW LIMITATIONS ON INTEREST DEDUCTIBILITY (CONTINUED)

- Under the TCJA, deduction for business interest generally limited to the sum of (1) business interest income for such year, plus (2) 30% of "adjusted taxable income" ("ATI") for such year
- ATI generally is taxable income, computed without regard to:
  - (1) any item of income, gain, deduction, or loss that is not properly allocable to a trade or business;
  - (2) any business interest or business interest income;
  - (3) the amount of any net operating loss ("NOL") deduction under Section 172; (4) the amount of any deduction under Section 199A; and
  - (5) in the case of taxable years beginning before January 1, 2022, any deduction allowable for depreciation, amortization, or depletion
- Prior to 2022, ATI approximates EBITDA; after 2022, ATI approximates EBIT

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APPLICATION OF NEW LIMITATIONS ON INTEREST DEDUCTIBILITY TO PASS-THROUGHS

- 30% cap applies at the entity level
- Excess ATI allocated to the partners for purposes of computing partner-level ATI
- Increase in basis upon disposition for excess business interest previously incurred but suspended

CARRYOVER OF UNUSED INTEREST DEDUCTIONS

- Disallowed interest may be carried over indefinitely
- Treated as incurred in the next year
- Not part of NOL deduction (and therefore not subject to 80% limitation, discussed below)
- Subject to limitation after sale of the business under Section 382
- Excess business interest allocated from a partnership may be used only to offset future excess taxable income above the 30% cap allocated from that partnership in future years

EXCEPTIONS TO INTEREST DEDUCTION LIMITS

- Electing real estate businesses
- Small businesses (average gross receipts in the prior 3 years of $25 million or less)
- Farming businesses
- Motor vehicle, boat and farm equipment dealers (for floor plan financing interest)

RATIONALES AND IMPLICATIONS

- Revenue raiser to pay for the reduction in corporate rates
- Belief that equity financing is more stable
- Reduces ability of financial buyers to acquire companies (i.e., may negatively impact LBOs)
- Will provide advantage to business entities with substantial capital
- Could cause highly-leveraged business to experience increase in effective tax rate relative to prior law, despite lowering of rates
- US corporations, regardless of whether they are foreign-controlled, are now subject to the limitations on interest deductibility under Section 163(j)
- Although real estate companies are not subject to the 30% limitation, such companies remain subject to the arm’s-length requirement and general debt-equity principles
- May be possible to structure around interest limitations through use of economically equivalent alternatives to the extent not treated as debt for US tax purposes (e.g., sale-leasebacks)
- Debt financing may continue to be desirable notwithstanding new limitations, e.g. for withholding tax reasons
- Together with the BEAT (discussed below), may incentivize multinationals to move debt to foreign affiliates

FULL EXPENSING FOR CERTAIN CAPITAL INVESTMENTS

- Section 179 has been permanently amended to allow small businesses to expense up to $1 million per year of certain depreciable tangible property purchased for use in the active conduct of a trade or business ($500,000 under prior law)
- More broadly (but subject to sunset as described below), Section 168(k), which provides for bonus depreciation on tangible personal property where 179 does not apply, also has been amended to allow for increased depreciation deductions. This benefit varies by year in which the property is place in service
  - Through 2022, 100% of the cost of tangible personal property (whether new or used) may be deducted as bonus depreciation in the year such property is placed in service
  - This percentage is reduced by 20% every 2 years until 2027, when the benefit terminates
  - Any cost not recovered by bonus depreciation is written off under the regular MACRS system

FULL EXPENSING FOR CERTAIN CAPITAL INVESTMENTS (CONT'D)

- Application of provision to used property may result in greater desire for asset acquisitions by buyers (particularly for capital-intensive businesses), though in many cases a significant portion of the purchase price will be allocated to goodwill and other intangible assets, the cost of which is not eligible for immediate expensing
- Taxpayers may elect out of bonus depreciation on a class of property basis each year that such property is placed in service
- Consider the interaction of the NOL rules, the interest deduction limits, and the new expensing rules (e.g., taxpayers with NOLs that will not initially benefit from such immediate deductions may choose to make such elections)

CHANGES TO RULES RELATING TO CORPORATE NOLS

- Prior Law:
  - NOLs could be carried back 2 years and carried forward 20 years
  - Generally could be used as a deduction against 100% of a corporation's regular taxable income
- TCJA:
  - NOLs may be used to shelter only 80% of taxable income in taxable years after 2017
  - NOLs may not be carried back beginning in 2018
  - NOLs may be carried forward indefinitely
  - Changes are effective for NOLs arising in taxable years after December 31, 2017, i.e., older NOLs not subject to these rules
- Note: elimination of NOL carryback may impact ability to monetize transaction tax deductions in M&A setting

TREATMENT OF GAIN ON SALE OF PARTNERSHIP INTEREST BY NON-US PARTNER

- Historical IRS position: Non-US partners subject to tax on gain from sale of partnership interest as "effectively connected income" ("ECI") to the extent of gain inherent in partnership assets used in US trade or business
- Historical IRS position recently overturned in *Grecian Magnesite Mining, Industrial & Shipping Co., SA v. Commissioner*, 149 T.C. 3 (2017)
- TCJA legislatively overturns Grecian Magnesite
- Under TCJA, gain on disposition of partnership interest subject to U.S. tax to the extent attributable to the partnership's assets used in a US trade or business (consistent with historical IRS position)
- TCJA includes new withholding feature
  - Transferee required to withhold 10% of amount realized if any portion of gain is attributable to a U.S. trade or business unless transferor certifies that it is US person
  - If transferee fails to withhold, partnership must withhold from distributions to transferee

CHANGES TO US CFC RULES: INTRODUCTION

- Under prior law and the TCJA, a CFC is any foreign corporation owned more than 50% (by vote or value) by "United States shareholders" on any day during the taxable year of the foreign corporation
- The TCJA broadens application of the CFC rules in several ways, including by expanding the definition of "United States shareholder" and eliminating the requirement that a foreign corporation be a CFC for an uninterrupted period of 30 days during the taxable year as a prerequisite to the application of Subpart F income inclusions
- Section 956 not repealed

CHANGES TO US CFC RULES: DEFINITION OF "UNITED STATES SHAREHOLDER"

- Prior Law: any U.S. person who owns 10% or more of the vote of stock of the foreign corporation
- TCJA: any U.S. person who owns 10% or more of the vote *or value* of stock of the foreign corporation
- TCJA also expands constructive ownership to attribute ownership from foreign persons to US persons (downward attribution rules), thus potentially creating CFCs where none previously existed (particularly in the brother-sister setting where a foreign parent owns both US and foreign subsidiaries)
- Effect of these changes is to significantly expand the scope of the CFC rules

CHANGES TO US CFC RULES: 30-DAY REQUIREMENT REPEALED

- Prior Law: Subpart F income inclusion required for each United States shareholder who owns (directly or indirectly) stock on the last day of the tax year in a foreign corporation only if such foreign corporation is a CFC for <u>an uninterrupted period of 30 days or more</u> during the tax year
- TCJA: Subpart F income inclusion for each United States shareholder who owns (directly or indirectly) stock on the last day of the tax year in a foreign corporation that is a CFC <u>at any time</u> during the tax year

NEW PARTICIPATION EXEMPTION FOR DIVIDENDS FROM FOREIGN SUBSIDIARIES

- TCJA provides US corporate shareholders of a “specified 10 percent owned foreign corporation” with 100 percent dividends received deduction for the foreign-source portion of the dividends received from such corporation
- Effect is to exempt such dividends from the US federal income tax base – i.e., the exemption moves the US tax system closer to a “territorial” system
- One-year holding period generally is required (expressed as 365 days over a two-year period)
- Foreign tax credits not allowed for exempt portion of any dividend

NEW PARTICIPATION EXEMPTION FOR DIVIDENDS FROM FOREIGN SUBSIDIARIES (CONT'D)

- "Specified 10 percent owned foreign corporation" generally is any non-US corporation that has at least one US corporate shareholder that owns at least 10 percent of the stock of the non-US corporation (excluding a passive foreign investment company that is not also a CFC)
- Participation exemption applies to distributions from CFC to the extent earnings attributable to such distribution do not otherwise constitute Subpart F income or GILTI (or were includible previously under Section 956)
- Basis of stock of specified 10 percent owned foreign corporation must be reduced by the exempt portion of dividend for purposes of determining loss with respect to later sale or disposition of such stock

NEW PARTICIPATION EXEMPTION FOR DIVIDENDS FROM FOREIGN SUBSIDIARIES (CONT'D)

- The "foreign-source portion" of dividend is determined based on following ratio:

$$\frac{undistributed\ foreign\ earnings\ of\ the\ foreign\ corporation}{total\ undistributed\ earnings\ of\ the\ foreign\ corporation}$$

- Limitations:
  - Not available for "hybrid dividends" – *i.e.*, an amount received from a CFC, which receives a deduction (or other tax benefit) against any non-US income tax on account of the dividend
  - Not available for GILTI
  - Not available for gains realized on the sale of stock of a non-US corporate subsidiary except in case of CFC to the extent that gain is treated as dividend under Section 1248
    - May encourage 338 elections for sales of non-US subsidiary stock, but impact of GILTI rules must be considered

GLOBAL INTANGIBLE LOW-TAXED INCOME

- TCJA adds new Section 951A, which effectively expands CFC anti-deferral regime to include a new class of income known as GILTI
- GILTI is new type of income that may be taxed to US shareholders of a CFC in a manner similar to the taxation of Subpart F income
- Generally, GILTI includes all net operating income (taking into account allocable interest deductions) of a foreign corporation not otherwise taxed to US shareholders in excess of a 10 percent return on the adjusted cost basis of the tangible assets of the company used in the production of such operating income

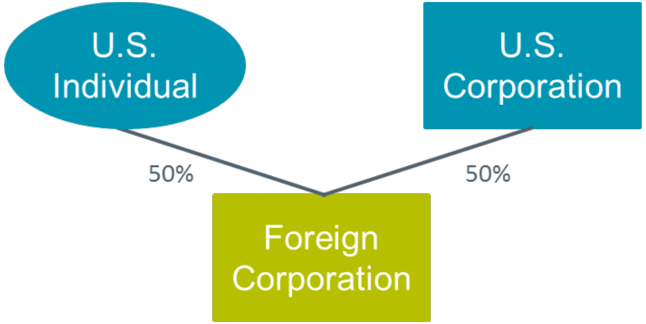
GLOBAL INTANGIBLE LOW-TAXED INCOME (CONT'D)

- Corporations (excluding S corporations): effective tax rate of 10.5% (rising to 13.25% in 2026)
- Individuals (including income earned by individuals through pass-throughs): regular rates apply (currently a maximum rate of 40.8%, taking into account 3.8% Medicare tax)
- Individuals subject to GILTI should consider whether election under Section 962 may be available and beneficial with respect to GILTI
- Tax-exempt organizations do not appear to be subject to tax on GILTI unless such income also is UBTI
- US corporate shareholder is eligible for indirect foreign tax credit of 80% of the foreign taxes paid with respect to GILTI
- As noted above, the participation exemption does not apply to GILTI

GLOBAL INTANGIBLE LOW-TAXED INCOME (CONT'D)

- GILTI provisions could apply to a domestic fund (e.g., a private equity fund) that holds more than 50% of the stock of a non-US corporation, and also could apply to a domestic fund holding 10% or more (by vote or value) of the stock of a non-US corporation if after accounting for other US shareholder groups such non-US corporation were a CFC
  - Fund would be required to include on the K-1s of the investors and general partners of the fund their allocable share of the non-US corporation's GILTI on an annual basis
- Non-US vehicle (e.g., a Cayman Islands limited partnership) may still result in CFC (and GILTI inclusion), but likelihood would be lower
- Fund managers should consider (1) whether any of their fund investments are in CFCs; (2) if a fund does have investments in CFCs, whether tax distribution provisions will be triggered if the fund has any GILTI that is allocated to its investors or managers; and (3) whether restructuring may be desirable to avoid the GILTI rules

GILTI EXAMPLE



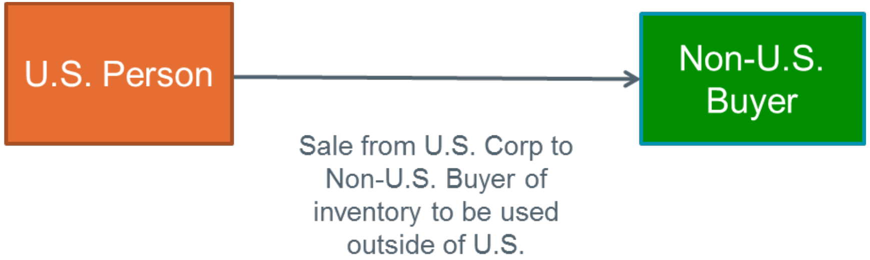
		U.S. Corporations			U.S. Individuals*	
Per U.S. Shareholder through CFC		**Prior Tax**	**Current Tax**		**Prior Tax**	**Current Tax**
Passive Income (capital gains, dividends)	$ 40.00	$ 14.00	$ 8.40		$ 15.84	$ 14.80
Gross Income from Sales to Unrelated Buyer	$ 50.00		$ 5.25			$ 18.50
Active Royalties (IP owned by CFC)	$ 50.00		$ 5.25			$ 18.50
Services Income (non-Subpart F)	$ 50.00		$ 5.25			$ 18.50
Total	$ 190.00	**$ 14.00**	**$ 24.15**		**$ 15.84**	**$ 70.30**

* Individual subject to tax at 37% rate, no 3.8% Medicare tax

FOREIGN DERIVED INTANGIBLE INCOME

- As a complement to the GILTI rules, and with an emphasis on incentivizing US companies to maintain onshore operations, the TCJA added the FDII regime
- Includes 13.125% tax rate (increased to 16.41% in 2026) for a US corporation's FDII
- FDII calculated in a similar fashion to GILTI, generally income related to services provided and goods sold by a US corporation to foreign customers

FDII EXAMPLE



		U.S. Corporation		U.S. Individual*	
FDII (U.S. taxpayer earning directly)		Prior Tax	Current Tax	Prior Tax	Current Tax
Passive Income (capital gains, dividends)	$ 40.00	$ 14.00	$ 8.40	$ 8.00	$ 8.00
Gross Income from Sales to Non-U.S. Buyer	$ 50.00	$ 17.50	$ 6.56	$ 19.80	$ 18.50
Active Royalties (IP used abroad)	$ 50.00	$ 17.50	$ 6.56	$ 19.80	$ 18.50
Services Income (non-U.S. recipient)	$ 50.00	$ 17.50	$ 6.56	$ 19.80	$ 18.50
Total	$ 190.00	**$ 66.50**	**$ 28.09**	**$ 67.40**	**$ 63.50**

* Individual subject to tax at 37% rate, no 3.8% Medicare tax

COMPARISON OF GILTI AND FDII OUTCOMES

		U.S. Corporations		U.S. Individuals*	
GILTI + Sub F (per U.S. Shareholder through CFC)		Prior Tax	Current Tax	Prior Tax	Current Tax
Passive Income (capital gains, dividends)	$ 40.00	$ 14.00	$ 8.40	$ 15.84	$ 14.80
Gross Income from Sales to Unrelated Buyer	$ 50.00		$ 5.25		$ 18.50
Active Royalties (IP owned by CFC)	$ 50.00		$ 5.25		$ 18.50
Services Income (non-Subpart F)	$ 50.00		$ 5.25		$ 18.50
Total	$ 190.00	$ 14.00	**$ 24.15**	$ 15.84	**$ 70.30**
FDII (U.S. taxpayer earning directly)		Prior Tax	Current Tax	Prior Tax	Current Tax
Passive Income (capital gains, dividends)	$ 40.00	$ 14.00	$ 8.40	$ 8.00	$ 8.00
Gross Income from Sales to Non-U.S. Buyer	$ 50.00	$ 17.50	$ 6.56	$ 19.80	$ 18.50
Active Royalties (IP used abroad)	$ 50.00	$ 17.50	$ 6.56	$ 19.80	$ 18.50
Services Income (non-U.S. recipient)	$ 50.00	$ 17.50	$ 6.56	$ 19.80	$ 18.50
Total	$ 190.00	$ 66.50	**$ 28.09**	$ 67.40	**$ 63.50**

* Individual subject to tax at 37% rate, no 3.8% Medicare tax

Thank you!

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