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# Looking Ahead: International Issues for Emerging from a Covid World

Barnes Dennig International Event  
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# Agenda

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- Greeting and Introduction
- Mergers and Acquisitions
- Global Workers
- How to replenish the funding after Covid-19 policies?



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# It's Poll Time!

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# Mergers and Acquisitions

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# Impact of Covid-19 on Mergers & Acquisitions

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- Significant slow-down of M&A deals worldwide in 2020, after onset of Covid-19 shut-down measures
  - Risk management concerns
  - Financial constraints – in-progress deals were dropped
  - Employee retention
- More robust activity in 2021 and 2022 due to:
  - Lower interest rates
  - Higher availability of financing options
  - Saturation or slow-downs in home market
  - Significant assistance provided by governments
- Post-COVID landscape opened opportunities to:
  - Make strategic acquisitions at lower costs
  - Acquire companies with accelerated growth potential
  - Expand into foreign markets or acquire foreign entities to resolve supply chain and labor issues

# Taxation of Outbound Restructurings/Transfers

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- Generally, transactions involving only U.S. entities can be structured to be tax-free, e.g. transfer of property to a corporation in exchange for stock in that corporation
- Tax-free treatment does not apply to transfers by U.S. person to a foreign corporation
  - Exception for outbound transfers of stock in a foreign corporation that is a party to a reorganization if the U.S. transferor enters into a Gain Recognition Agreement with the IRS
    - If substantially all of the assets are disposed of within 60 months of the initial transfer, the gain will be triggered (unless an exception applies)
    - Example:
      - Step 1: U.S. corporation directly owns foreign corporation (FC)
      - Step 2: U.S. corporation transfers stock of FC to U.S. subsidiary in exchange for stock of subsidiary
        - Can do this even if U.S. subsidiary was already wholly owned by U.S. corporation
      - Step 3: Gain is deferred if FC stock is not disposed of within 60 months
      - Note: FC stock can be transferred again within the 60 months as long as a new GRA is signed

# Issues Regarding Sale of Foreign Assets

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- The sale of a U.S. business can generally be structured as a stock sale, an asset sale, or a hybrid (i.e. a stock sale for legal purposes but treated as an asset sale for tax purposes through an F reorganization or an IRC Sec. 338 election).
- The buyer of assets which are used in the U.S. can take bonus depreciation in the year of the purchase, often making an asset purchase more desirable than a stock purchase for the buyer.
  - However, if assets are used outside the U.S., no bonus depreciation or accelerated depreciation is available. Therefore, if most of the purchased assets are outside the U.S., a stock deal could be more beneficial to both the buyer and the seller.
  - Asset deal could still make sense for purchase of foreign target if buyer wants to "restart" E&P
- Foreign jurisdiction may also tax the sale of the foreign assets
  - Tax treaty, if any, prevails
  - Foreign tax credits may be available to U.S. seller
- Exchange rate
  - Fixed assets reported on historical cost basis, so huge differences/fluctuations in exchange rate on sale date can significantly impact the gain or loss recognized

# Due Diligence Issues With Cross-border M&As

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- Unique risk factors
  - Complex tax laws of foreign jurisdictions
  - Accuracy of the financial statements of the foreign target, including ability to convert them to comparable GAAP basis financials; conversion of currency and language
  - Foreign government regulation of the product/industry
    - Intellectual property
    - Registration and certification of product
    - Annual filings
    - Anti-trust laws
  - Protection of IP
  - Ability to assess foreign target's market potential
  - Labor issues
  - Impact of time zones on meeting deadlines
  - Language barriers



# Labor Issues With Cross-border M&As

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- Unique labor issues
  - Foreign labor laws
  - Integration of existing employees/management
  - Language barriers
  - Transfer of existing employment liabilities
  - Determination of the employer entity
  - Taxation of employees
  - Integration of global HR policies
  - Cultural differences – communications, holidays, etc.
  - Labor unions, trade unions – some countries have a requirement to disclose and consult with workers before selling a business
  - Layoffs
    - Does the foreign jurisdiction allow layoffs due to acquisitions?
      - U.S. buyer may have to request a pre-closing layoff
    - Foreign severance pay requirements
    - Outplacement services
    - Some countries, e.g. France, do not recognize "at will" employment

# Other Issues With Cross-Border M&As

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- Integration – pre-closing research and post-closing speed are critical
- Local culture, customs, practices
- Protection of acquired, shared, or newly-developed IP
- Cash repatriation
- Global structuring
- Advisors – local legal, labor, accounting, and tax advisors are critical
  - No attorney/client privilege in many countries
- Political environment
  - Leveraging of political influence
  - In some countries, the government is required to be a JV partner for a foreign investor

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# Global Workforce

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# Remote Workers

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- Historically remote workers meant:
  - Short term – Less than a year
  - Long term – Temporary but longer than a year
  - Permanent
- Remote workers can now mean:
  - Working while on vacation
  - Domestically Remote
  - Internationally Remote
  - Hybrid Roles



# Considerations of Remote Workers

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- Payroll Considerations
  - How will you pay them?
  - Which company will pay them?
  - Withholding requirements?
- Immigration Considerations
  - Visa required?
  - Work permit required?
  - Language and skills required?
- Legal Considerations
  - Labor law
  - Minimum wages, overtime, etc.
  - Worker's compensation
  - Family and Medical Leave
- Tax Considerations

# Permanent Establishment

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- Permanent Establishment (PE) is a key concept in determining if a company has an income tax filing requirement in a country
- Generally defined based on if the corporation has a “fixed place of business” within a country, but...
- Questions to consider:
  - Can a remote worker create a PE?
  - Does the company track where employees are working remotely to be aware of the potential issues?
  - What activities is the remote worker doing?

# Employee or Contractor?

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	Employee	Contractor
<b>Control</b>	Company controls how, when and where work is performed.	Individual controls how, when and where work is performed based upon agreement with company.
<b>Compensation</b>	Paid a salary or hourly wage.	Paid a specific fee.
<b>Benefits</b>	Eligible for employment benefits.	Not eligible for employment benefits.
<b>Taxes</b>	Receive W-2 from company.	Receive 1099-NEC for US person or 1042-S for non-US person.

# How to determine if person is U.S. or non-U.S.?

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- A U.S. resident alien is treated as such if they:
  - Possess a U.S. green card (lawful permanent resident)
  - Satisfy the substantial presence test, or
  - Make a qualifying first-year election under IRC §7701(b)(1)-(4)
- A non-U.S. resident alien (NRA) individual is an individual who is neither a citizen nor a resident alien of the U.S. under IRC §7701(b)(1)(B).
- Company should request proof of status:
  - W-9 – Proof of U.S. Status
  - W-8 – Proof of Foreign Status (Different type of form based on type of entity)
  - 8233 – NRA certifying exemption from withholding on wages

# Substantial Presence Test

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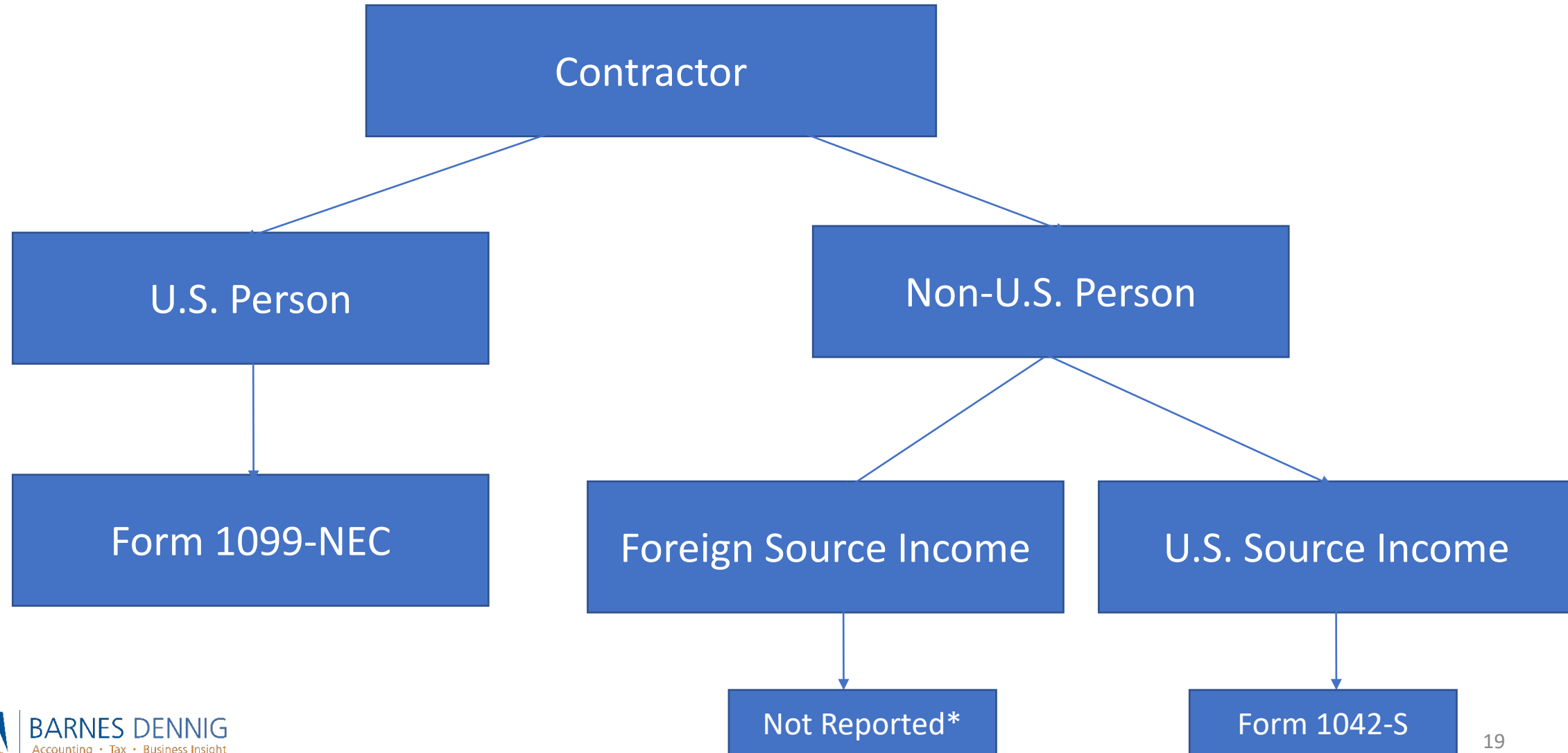
- An individual meets the substantial presence test if the individual:
  - Is physically present in the United States on at least 31 days during the current year, and
  - 183 days during the 3-year period during a three-year testing period by counting the following:
    - All the days present in current year
    - 1/3 of the days present during the first preceding year, and
    - 1/6 of the days present during the second preceding year
- Example

Individual A was physically present in the United States on 120 days in each of the years 2019, 2020, and 2021. To determine if they meet the substantial presence test for 2021, count the full 120 days of presence in 2021, 40 days in 2020 (1/3 of 120), and 20 days in 2019 (1/6 of 120). Because the total for the 3-year period is 180 days, they are not considered a resident under the substantial presence test for 2021.



# Form 1099-NEC or 1042-S?

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# Sourcing Rules - IRS

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Item of Income	Factor in Determining Source
Interest	Residence of payor
Dividends	Whether a U.S. or foreign corporation
Rent	Location of property
Royalties:	
Natural resources	Location of property
Patents, copyrights, etc.	Where property is used
Sale of real property	Location of property
Sale of personal property	Location of seller's tax home
Salaries, wages, other compensation	Where services performed
Business Income:	
Personal services	Where services performed
Sale of inventory - purchased	Where sold
Sale of inventory - produced	Where produced (allocation may be necessary)
Pension distribution attributable to contributions	Where services performed that earned the pension

# Income Tax – US Withholding Rules

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- Fixed Determinable Annual and Periodic (FDAP) - Flat 30% withholding on the gross income
- Effectively Connected Income (ECI) -- Taxed at graduated rates on Net Income
- Withholding exceptions do exist:
  - Payments of \$3,000 or less under IRC §861(a)(3)
  - Payments to NRAs in the U.S. under certain visas
  - Certain treaty exemptions

# Income Tax – Individual Filing Requirements

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- U.S. citizens and green card holders are required to file an annual U.S. income tax return
  - Must report worldwide income and gains
  - Does NOT matter where the individuals live or work
  - Files Form 1040
- Resident aliens are taxed the same as U.S. citizens and green card holders
  - Must report worldwide income and gains
  - Files Form 1040
- NRAs are taxed only on U.S. Source income
  - Files Form 1040-NR

# Social Taxes

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- Totalization Agreements – Agreements with certain countries for the purpose of avoiding double taxation of income with respect to social security taxes.
  - Employee must remain an employee of the home country and pay home country social taxes.
  - Any NRA who claims an exemption from U.S. Social Security Taxes and Medicare Taxes because of a Totalization Agreement must secure a Certificate of Coverage from the social security in their home country
  - Certificate of Coverage must be maintained by U.S. company to support no withholding of U.S. Social Security Taxes and Medicare Taxes
- Countries with Totalization Agreements

Australia	Czech Republic	Greece	Luxembourg	Slovak Republic	United Kingdom
Austria	Denmark	Hungary	Netherlands	South Korea	
Belgium	Finland	Ireland	Norway	Spain	
Canada	France	Italy	Poland	Sweden	
Chile	Germany	Japan	Portugal	Switzerland	



# Challenges to Global Workforce

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- Uniting the workers
- Standardizing benefits
- Resource limitations
- IT considerations
- Cost of compliance

# Benefits to Global Workforce

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- Larger pool of talent
- Meeting employee's requests
- Expand footprint of business
- Diverse ideas

# Retain Global Workforce

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# How to replenish the funding after COVID-19 policies?

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# Budget Deficits

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- Countries across the world provided funding to companies and individuals to survive the COVID-19 crisis
- U.S. alone
  - Payroll Protection Program Loans (PPP)
  - Employer Retention Credits (ERC)
  - Economic Impact Payments (EIP)
- Countries must rebalance tax systems and spending due to government budget deficits and debt
- High debt has been more manageable with lower interest rates
  - Inflation and increasing interest rates means debt needs to be re-evaluated

# Base Erosion and Profit Shifting "BEPS 2.0"

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- Domestic tax BEPS due to multinational enterprises exploiting gaps and mismatches between different countries' tax systems affects all countries.
- OECD/G20 are working together on the BEPS Framework. Over 135 countries and jurisdictions are implementing 15 Actions to tackle tax avoidance, improve coherence of international tax rules, ensure a more transparent tax environment and address the challenges arising from the digital economy.
- **Pillar 1:** Would expand a country's authority to tax profits from companies that make sales into their country but don't have a physical location.
  - Would require changes to tax treaties
- **Pillar 2:** Would implement a global minimum effective tax rate where multinational groups with consolidated revenue over €750m are subject to a minimum ETR of 15% on income arising in low tax jurisdictions.

# Inflation Reduction Act

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- Signed into law August 16, 2022
- Corporate Alternative Minimum Tax (AMT)
  - Based on book income rather than taxable income
  - Imposes a 15% tax on the excess of the corporation's adjusted financial statement income over its corporate AMT foreign tax credit for the year.
  - Applies only to large corporations (excludes S corporations) with average annual adjusted financial statement income of more than \$1 billion for three consecutive years, or for members of certain foreign-parented multinational groups, where combined annual adjusted financial statement income of all members of the group is \$1 billion for three consecutive years and the member has average annual adjusted financial statement income of more than \$100 million.
  - Effective for tax years beginning after December 31, 2022.

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# Questions?



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