



2024 **TAX STRATEGIST** WEBCAST SERIES

CROSS-BORDER

# International Tax, Transfer Pricing, and Customs and Trade Update

JUNE 26, 2024

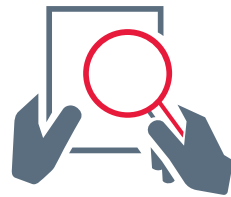
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# Learning Objectives



Identify the current landscape of international tax and transfer pricing, including U.S. customs and international trade and global VAT.



Describe expected international tax and transfer pricing developments in 2024.



Assess the impact the current and future landscape could have on global companies.

# With You Today



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# Agenda for Today

1

Proposed §987  
Regulations

2

Customs and  
International  
Trade Update

3

Importance of  
Value Added  
Tax/Goods and  
Services Tax

# Proposed §987 Regulations



# Background and Applicability Dates



# §987 Proposed Regulations

## OVERVIEW



- ▶ On November 9, 2023, the Treasury Department and the IRS issued proposed regulations under §987
- ▶ The 2023 proposed regulations retain the basic approach and structure of the 2016 final regulations, while expanding the scope of entities that are subject to §987, and providing
  - Simplifying elections
  - A new transition method
  - A new loss suspension rule
  - Retroactive applicability for certain QBU terminations
- ▶ If finalized, the 2023 proposed regulations would apply to taxable years beginning after December 31, 2024

# What to Do in 2024

## 2023 PROPOSED §987 REGULATIONS

- ▶ When finalized, the 2023 proposed regulations apply to taxable years beginning after December 31, 2024
- ▶ What methodology to apply in 2024?
  - **Alternative 1** - Taxpayers that had applied the 2016 final regulations for a taxable year ending before November 9, 2023, may use that methodology for taxable years beginning after December 7, 2016, and beginning on or before December 31, 2024.
  - **Alternative 2** - Taxpayers may adopt the 2023 proposed regulations early for taxable years beginning on or before December 31, 2024, and ending after November 9, 2023, provided they do so consistently.
  - **Alternative 3** - Taxpayers may rely only on the applicability date provisions in the 2023 proposed regulations and continue with their current method of complying with §987 (e.g., the 1991 proposed regulations) for taxable years beginning on or before December 31, 2024.



# What to Do in 2024



# What to Do in 2024

## 2023 PROPOSED §987 REGULATIONS

Determine if there have been (or will be) any section 987 terminations on or after November 9, 2023.

- ▶ The effective date of the proposed §987 regulations is immediate for any section 987 termination after November 9, 2023
- ▶ Gains would likely be taxed immediately while losses are suspended and, in some cases, may be lost

Determine if an “eligible pre-transition method” has been consistently applied prior to December 31, 2024.

- ▶ Eligible pre-transition method includes:
  - The 1991 proposed section 987 regulations
  - The 1991 proposed section 987 regulations computed on an earnings-only basis
  - Any other reasonable methodology that is generally similar to the 1991 proposed regulations

## What to Do in 2024

### 2023 PROPOSED §987 REGULATIONS

- ▶ If an eligible pre-transition method has **NOT** been consistently applied, then the amount of deemed termination gain or loss must be computed under the “simplified method” as of 12/31/2024.
  - The simplified method is generally applied as follows:
    - Determine the change in net value of the section 987 QBU based on the tax basis balance sheet for each year of the section 987 QBU’s existence
    - The cumulative change in net value is then adjusted for the amount of any section 987 gain or loss recognized before the transition date to determine the amount of deemed transition gain or loss
    - The source and character of section 987 gain or loss is determined under the asset method of Treas. Reg. §§1.861-9(g) and 1.861-9T(g)
    - Consider applying the 10-year amortization election (see below)
- ▶ If an eligible pre-transition method has been consistently applied:
  - Determine the amount of deemed termination gain or loss
  - The source and character of section 987 gain or loss is determined under the asset method of Treas. Reg. §§1.861-9(g) and 1.861-9T(g)
  - Consider the 10-year amortization election (see below)

# What to Do in 2024

PROP. TREAS. REG. §1.987-10

Determine whether your current method is an eligible method

Eligible Methods	Non-Eligible Methods
Earnings and capital method (e.g., method prescribed in the 1991 §987 proposed regulations)	Everything else
Earnings-only method	
Other reasonable methods	

Compute “deemed termination” pre-transition §987 gain or loss

- ▶ Either as a deemed remittance of all assets and liabilities of the §987 QBU to its owner under the pre-transition eligible methods, plus certain adjustments (OFCNV adjustments), or
- ▶ Under the method prescribed in Prop. Reg. §1.987-10(e)(3) for non-eligible methods

# What to Do in 2024

## PROP. TREAS. REG. §1.987-10

- ▶ Owner can either make a 10-year amortization election, or the default loss suspension rules apply

10-Year Amortization Election	No Election
Owner of a §987 QBU may make an election to recognize its pre-transition gain or loss ratably over 10 years	Pre-transition gain is treated as net accumulated unrecognized §987 gain
Certain liquidations or reorganizations will cause immediate recognition of pretransition gain, and elimination of pretransition loss	Pre-transition loss is treated as suspended §987 loss

- ▶ Determine the source and character of the pre-transition gain or loss (“initial assignment”) based on the asset method in §1.861-9(g)
- ▶ Determine OFCNV (defined below) on the last day of the preceding taxable year
  - Translating the QBU’s balance sheet items on the day before the transition date into the owner’s functional currency at the spot rate applicable to the day before the transition date
- ▶ Comply with the applicable reporting requirements
  - “§987 Transition Information” statement (description of each QBU, computation of pre-transition gain or loss, 10-year amortization election (if applicable), partnership information (if applicable))

# What to Do in 2025



# What to Do in 2025

## 2023 PROPOSED §987 REGULATIONS

- ▶ The 2023 Proposed Regulations require the application of the FEED method to determine section 987 computations
  - FEED is generally a balance sheet squeeze methodology that will require tax basis balance sheets for all section 987 QBUs
    - Consider accounting systems issues related to acquiring balance sheet information
- ▶ The 2023 Proposed Regulations contain elections designed to ease the compliance burden
  - 2025 compliance will require evaluating which elections make sense



# Key Elections

## CURRENT RATE ELECTION

- ▶ A current rate election (CRE) allows the QBU owner to treat all assets and liabilities that are properly reflected on the books of the §987 QBU as marked items
  - When translating the balance sheet items with a CRE, all items will be translated into owner's functional currency at the spot rate applicable on the last day of the relevant taxable year
  - When translating the P&L, all items will be translated into the owner's functional currency at the yearly average exchange rate for the taxable year
- ▶ Gains are recognized, but losses are suspended (recognized to the extent of gain with the same source and character)



# Key Elections

## ANNUAL RECOGNITION ELECTION

- ▶ An annual recognition election (ARE) allows the QBU owner to recognize its net unrecognized §987 gain or loss with respect to its §987 QBU on an annual basis
  - When translating the balance sheet item with an ARE, historic items will be translated at the historic exchange rate, while the marked items be translated at year-end spot rate
  - When translating the P&L, all items will be translated into the owner's functional currency at the yearly average exchange rate for the taxable year
- ▶ Current year gains and losses are recognized, but loss suspension rules may apply under certain circumstances

# §987 Proposed Regulations

## COMPARING THE ELECTIONS

	Current Rate Election	No Current Rate Election
Annual Recognition Election	<ul style="list-style-type: none"><li>▶ P&amp;L items are translated at annual average exchange rate; balance sheet items translated at year-end spot rate</li><li>▶ Generally larger §987 exposure (see Example)</li><li>▶ §987 gain/loss recognized every year (deferral rules do not apply, outbound loss rules do not apply, limited loss suspension rules may apply)</li></ul>	<ul style="list-style-type: none"><li>▶ P&amp;L items are translated at annual average exchange rate; balance sheets items are translated based on applicable rates for historic and marked items</li><li>▶ Generally smaller §987 exposure (see Example)</li><li>▶ §987 gain/loss recognized every year (deferral rules do not apply, outbound loss rules do not apply, limited loss suspension rules may apply)</li></ul>
No Annual Recognition Election	<ul style="list-style-type: none"><li>▶ P&amp;L items are translated at annual average exchange rate; balance sheet items translated at year-end spot rate</li><li>▶ Generally larger §987 exposure (see Example)</li><li>▶ §987 gain/loss recognized on remittance, but subject to deferral rules, and loss suspension rules (outbound loss rules do not apply)</li></ul>	<ul style="list-style-type: none"><li>▶ <b>Default FEEP Method</b></li><li>▶ P&amp;L items are translated at annual average exchange rate, but basis of historic assets and COGS is translated using historic rates; balance sheets items are translated based on applicable rates for historic and marked items</li><li>▶ Generally smaller §987 exposure (see Example)</li><li>▶ §987 gain/loss recognized on remittance, but subject to deferral rules, and outbound loss rules.</li></ul>

# §987 Proposed Regulations

## KEY ELECTIONS

Apply to all  
QBUs in the  
control group  
or consolidated  
group



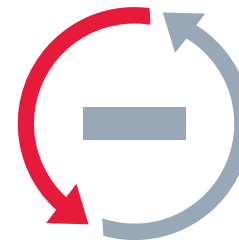
Is binding for  
five years



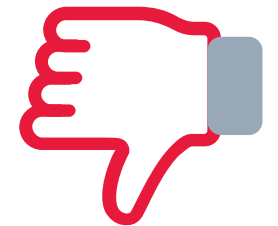
Can be revoked  
only with  
IRS consent  
(within five  
years)



Can be revoked  
without IRS  
consent  
(after five  
years)



Once revoked,  
a new election  
cannot be  
made for  
five years



# Customs and International Trade Update

HOT TOPIC

# Section 301 “China” Tariffs + Exclusions



# Results of Section 301 Tariff “Sunset Review”

- ▶ On May 13, 2024, the Office of the U.S. Trade Representative (USTR) announced the results of the Biden administration’s “sunset review” of the Section 301 China tariffs first imposed in 2018 by Trump.
- ▶ Section 301 of the Trade Act of 1974 allows the government to impose trade sanctions on foreign countries that violate U.S. trade agreements or engage in unfair trade practices that are “unjustifiable” or “unreasonable” and burden U.S. commerce.
- ▶ These are in addition to the Normal Trade Relations tariffs, antidumping/countervailing duties, and any other trade remedy tariffs (such as “safeguard tariffs” imposed under Section 201 of the Trade Act of 1974).
- ▶ The current Section 301 tariffs imposed in “four tranches,” which are levied at either 25% or 7.5%, will **ALL** remain in effect.
- ▶ Some existing tariffs will be increased, and new ones imposed for specific manufactured goods deemed “strategic” to U.S. interests. Administration is seeking comments (due June 28th) before final tariff rates/categories are announced.

# New Increased Tariffs for Specific Goods

Merchandise Class	Additional Duty Rate Increase
Battery parts (non-lithium-ion batteries)	Increase rate to 25% in 2024
Electric Vehicles	Increase rate to 100% in 2024
Facemasks	Increase rate to 25% in 2024
Lithium-ion electrical vehicle batteries	Increase rate to 25% in 2024
Lithium-ion non-electrical vehicle batteries	Increase rate to 25% in 2026
Medical gloves	Increase rate to 25% in 2026
Natural graphite	Increase rate to 25% in 2026
Other critical minerals	Increase rate to 25% in 2024
Permanent magnets	Increase rate to 25% in 2026
Semiconductors	Increase rate to 50% in 2025
Ship to shore cranes	Increase rate to 25% in 2024
Solar cells (whether or not assembled into modules)	Increase rate to 50% in 2024
Steel and aluminum products	Increase rate to 25% in 2024
Syringes and needles	Increase rate to 50% in 2024



# Section 301 Exclusions

On May 24, 2024, USTR announced the end of most of the remaining 429 product-specific Section 301 exclusions effective June 14th.

The cited reason was that *“public comments do not demonstrate that further extending the exclusion would aid efforts to shift sourcing out of China in the near term or do not demonstrate that products covered by the exclusion are unavailable outside of China.”*

Importers now have to go back to paying 25% or 7.5% *ad valorem* China tariffs in addition to the other duties that may apply (NTR, Section 232, etc.).

However, USTR is now soliciting comments (due June 28th) for establishing an exclusion process for machinery used in domestic manufacturing and for certain solar manufacturing equipment.



HOT TOPIC

# New Treasury Rule for EV Tax Credits



# Background

- ▶ On May 3, 2024, Treasury finally issued its long-awaited final rule on the \$7,500 tax credit for electric vehicles
- ▶ It specifically includes a more detailed process for automakers to **trace the battery supply chain** to qualify for the credit's domestic content requirements than the one that was originally proposed
- ▶ This kind of “tracing” is very similar to what occurs in the customs and trade world all the time for origin and free trade agreement qualification (**not to mention forced labor!**)
- ▶ NTO and the CITS team are collaborating with Earthstream to add this kind of tracing to their **mesur.io** software for our OEM clients and their downstream suppliers
- ▶ The final rule was published in the Federal Register on 05/06/2024 and is available online at
  - <https://federalregister.gov/d/2024-09094>
  - <https://govinfo.gov>

The screenshot displays the Federal Register website interface. At the top, there is a navigation bar with links for Sections, Browse, Search, Reader Aids, and My FR, along with a search box. The main header features the National Archives logo on the left, the text 'FEDERAL REGISTER The Daily Journal of the United States Government' in the center, and the National Archives and Records Administration seal on the right. Below the header, a blue banner contains a registered trademark symbol and the letter 'R'. The main content area displays the title of the document: 'Clean Vehicle Credits Under Sections 25E and 30D; Transfer of Credits; Critical Minerals and Battery Components; Foreign Entities of Concern'. Below the title, it states 'A Rule by the Internal Revenue Service on 05/06/2024'. A 'PUBLISHED DOCUMENT' tab is active, showing a 'Start Printed Page 37706' indicator. On the left side of the document view, there are icons for a menu, a speech bubble, and a comment icon. The document content shows 'AGENCY: Internal Revenue Service (IRS), Treasury.' and 'ACTION:'. On the right side, a 'DOCUMENT DETAILS' panel lists 'Printed version: PDF', 'Publication Date: 05/06/2024', and 'Agencies: Department of the Treasury, Internal Revenue Service'.

## Critical Minerals + Foreign Entities of Concern (FEOC)

- ▶ In performing the tracing test for domestic content, the final rule imposes a new “critical minerals” test for EV batteries which can be met by showing that the minerals were:
  - Extracted in the U.S.
  - Processed in the U.S. or in any country with which the U.S. has a free trade agreement in effect; or
  - Recycled in North America
- ▶ Automakers which meet this test receive a \$3,500 critical minerals credit towards the full \$7,500 vehicle credit
- ▶ The final rule excludes critical minerals sourced from “foreign entities of concern” (FEOC)
- ▶ FEOC comprise businesses with known ties to foreign governments deemed hostile to U.S. interests (currently China, Iran, North Korea, and Russia)
- ▶ Many of these FEOCs have ties to China, which dominates the EV battery supply chain

# EV Battery Components

In performing the tracing test for domestic content, the final rule also imposes a new “Battery Components” requirement to calculate the percentage of value of components.

They are only included in the calculation if they are:

- ▶ Manufactured in North America; or
- ▶ Assembled in North America

- ▶ The applicable percentage to receive an additional \$3,500 tax credit varies based on when the vehicle is placed in service:
  - ▶ Vehicles placed in service before January 1, 2024: 50%
  - ▶ Vehicles placed in service during calendar year 2024, 2025: 60%
  - ▶ Vehicles placed in service during calendar years 2026, 2027, and 2028, the applicable percentage is 70%, 80%, and 90%, respectively
  - ▶ Vehicles placed in service after December 31, 2028: 100%



# Domestic Content Calculations

The applicable percentage to satisfy the critical minerals test also varies based on when the vehicle is placed in service:

- ▶ Vehicles placed in service before January 1, 2024: 40%
- ▶ Vehicles placed in service during calendar year 2024, 2025, and 2026: 50%, 60%, and 70%, respectively; and
- ▶ Vehicles placed in service after December 31, 2026: 80%

The vehicle will qualify for the \$7,500 credit if the critical minerals and battery components tests are equal to or greater than the applicable percentages set forth above (as certified by the qualified manufacturer).

NEW CITS SERVICE OFFERING  
**Duty Drawback**



# What is Duty Drawback?

Duty Drawback is the refund of duties paid on imported merchandise which is exported unused or used to manufacture a product that is exported.

Drawback is allowable on 99% of the duties taxes and fees paid on imported merchandise which were imposed under federal law upon entry or importation

- ▶ Ordinary customs duties
- ▶ Marking Duties
- ▶ Internal Revenue Taxes
- ▶ Merchandise Processing Fees
- ▶ Harbor Maintenance Fees
- ▶ Section 301 "China tariffs"

**Not Eligible:** ADD/CVD or Section 232

## Major Types of Drawback

- ▶ Unused Direct Identification (1313(j)(1))
- ▶ **Unused Substitution (1313(j)(2))**
- ▶ Manufacturing Substitution (1313(b))
- ▶ Manufacturing Direct Identification (1313(a))

## Unused Substitution (1313(j)(2))

- ▶ Import & pay duty
- ▶ Substitute merchandise of the same 8-digit HTSUS (basket provisions not applicable)
- ▶ Unused in the U.S. (allowable operations)
- ▶ Exported or destroyed
- ▶ 5 years import to claim
- ▶ Lesser of rule required value of substitute merchandise
- ▶ First Filed Rule prevented claiming Direct ID and Substitution on same ES line item
- ▶ HTSUS is very important, so misclassification creates problems claiming drawback

# How to Get Started

## Combined Privilege Application

- ▶ One-time waiver of prior notice of intent to export (19 CFR § 190.36)
- ▶ Waiver of prior notice of intent to export (19 CFR § 190.91)
- ▶ Accelerated payment (19 CFR § 190.92)
- ▶ Applicable drawback provision(s)

## What constitutes a “complete” drawback claim?

- ▶ Drawback entry acceptance in ACE
- ▶ Mandatory documents into Document Image System (DIS), e.g., prior notice of intent to export, one-time waiver, Reconciliation (CATAIR Appendix G)

## Self-File

- ▶ Filer Code
- ▶ Letter of Intent
- ▶ Connection/Software

## Elements of a Duty Drawback Claim & Drawback Claim (Entry Summary) Transaction Input Structure Map

- |  |  |
|--|--|
| ▶ Drawback Entry #                     | ▶ Information on Exportation or Destruction  |
| ▶ Filing Port Code                     | ▶ Information on NAFTA/USMCA (if applicable) |
| ▶ Claimant ID #                        | ▶ Notice of Intent to Export or Destroy      |
| ▶ Drawback Provision                   | ▶ Quantity/Unit of measure                   |
| ▶ Drawback Claim Date                  | ▶ Duties, Taxes, and Fees Paid               |
| ▶ Total Drawback Amount Requested      | ▶ Entered Value per Unit                     |
| ▶ Import Entry Summary Line Level Data | ▶ Additional Requirements from the CATAIR    |

Name	Control ID
Drawback Entry Summary	10
Bond Information	31
Import Entry Summary Details	40
Import Classification	41
Import Quantity & UOM	42
Import Revenue Claimed	43
Exports	70
Export Descriptions	71
Revenue Subtotals	89
Revenue Totals	90



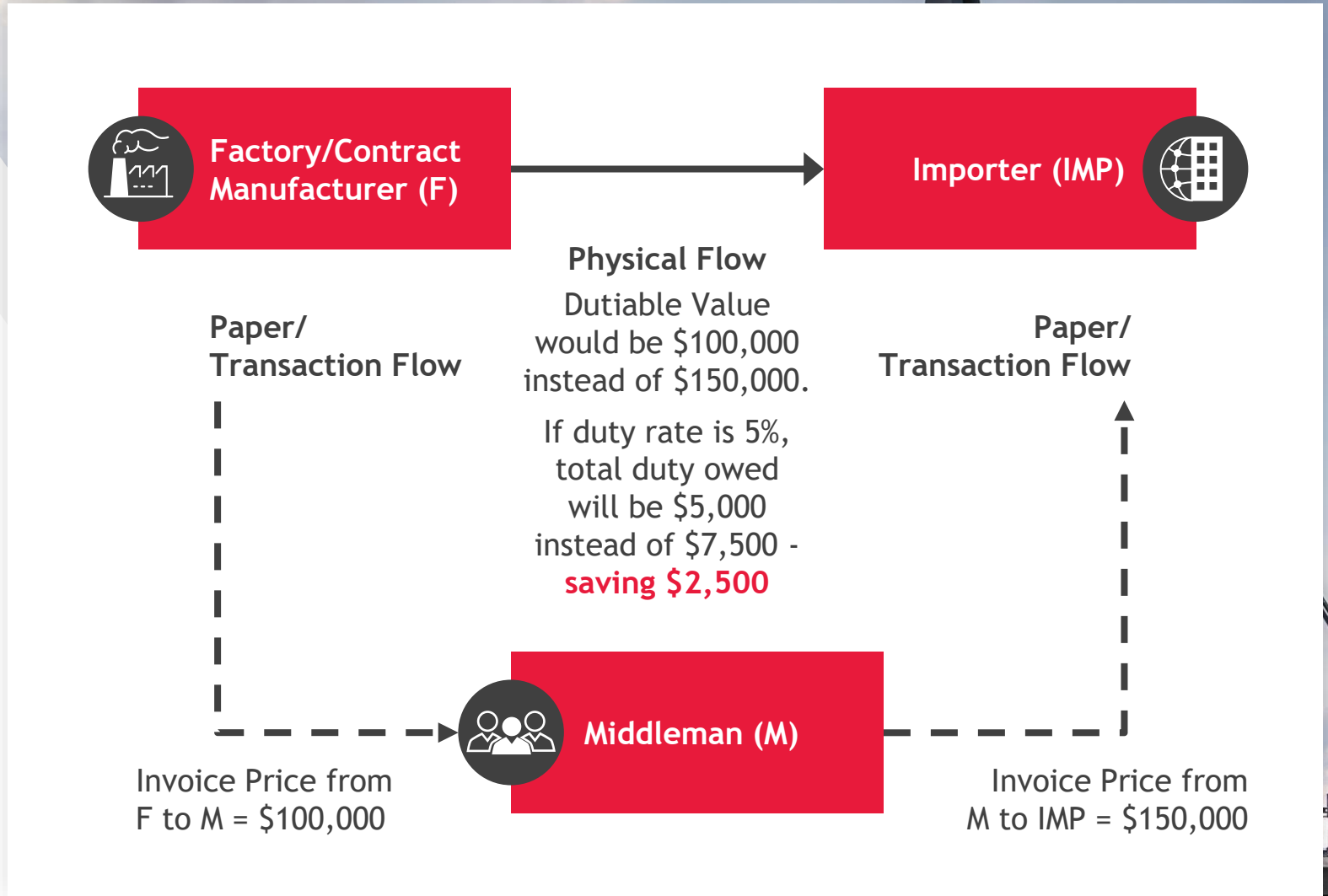
# First Sale Rule



# Customs Valuation: First Sale Rule (FSR)

- ▶ The First Sale Rule (FSR): FSR applies where merchandise is imported into the U.S. as a result of multiple sales prior to import. However, CBP normally now examines whether all sales are arm's length (including intercompany ones) before permitting use of FSR.
- ▶ FSR has three requirements:
  - A *bona fide* sale from the manufacturer to the middleman as well as from the middleman to the U.S. importer;
  - The merchandise was clearly destined for export to the U.S. at the time of the first sale; and
  - Both the first sale price and the second sale price were arm's length

# Customs Valuation: FSR Illustration



# Importance of Value Added Tax/Goods and Services Tax

# Overview



## COST

- ▶ VAT/GST (and other indirect taxes such as customs duties and excise taxes) are part of “**total tax liability**” and essential to a company’s planning and compliance activities.
- ▶ Not intended to be a costs to businesses, non-recoverable/non-reclaimed VAT/GST (e.g., incorrectly charged) is an above-the-line and often represent **cash savings and refund opportunities**.

## COMPLIANCE

- ▶ Any company engaging in business activities overseas likely incurs compliance and reporting obligations in an evolving regulatory and legal environment.
- ▶ VAT/GST is a whole of business tax - any changes in scope, rates, etc. has implications across the entire organization.

## MANAGEMENT

- ▶ People, processes, and technology all come together to manage global VAT/GST. Companies often do not have sufficient internal resources to manage calculation and determination, reporting and compliance obligations and leverage service providers to fill in the gaps.

## GLOBAL TREND OF E-INVOICING MANDATES

### Implications

- ▶ Global adoption of continuous transaction control (CTC) systems, including e-invoicing and digital reporting mandates is increasing
  - Over 30 jurisdictions have e-invoicing mandates, many G20 economies plan to implement in near future
- ▶ Businesses must ensure their transactions (including intercompany) comply with local VAT and invoicing requirements
- ▶ Non-compliance with CTC mandates can result in the rejection of invoices
  - Issues with customer deducting VAT incurred on purchases
  - Potential disallowance from deducting expenses for income tax purposes
- ▶ CTC mandates necessitate a strategic response from multinational enterprises
  - Comprehensive assessment of current processes
  - Implementation of global strategy
- ▶ CTC mandates tend to be expanded over time, making early compliance crucial
- ▶ Tax authorities leveraging data from CTC systems and AI tool to scrutinize transactions in real time
  - Increased automation of compliance processes
  - More scrutinizing of arm's-length pricing of intercompany transactions

# E-Commerce: Enforcement of Remote Seller Rules



Tax authorities using variety of methods to identify non-compliant remote sellers

Increased collaboration across borders between tax authorities

Wide range of enforcement measures used against non-compliant sellers

Notable increase in audit activities for registered remote sellers

**Thank You!**



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**CROSS-BORDER**

**Fall Planning  
Session**

September 25, 2024 / 1:00 PM ET

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