



TaxNewsFlash

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Observations about Notice 2018-31: Country-by-country reporting by “specified national security contractors”

The IRS on March 30, 2018, released an advance copy of Notice 2018-31 concerning national security considerations with respect to country-by-country (CbC) reporting.

In general, [Notice 2018-31](#) [PDF 21 KB] modifies the CbC reporting requirement for specified national security contractors and states that the IRS and Treasury intend to modify the CbC regulations to reflect the modified guidance.

The following discussion offers some observations and potential actions for taxpayers to consider. Read an initial report about Notice 2018-31 in [TaxNewsFlash](#).

Overview of Notice 2018-31

A U.S. multinational enterprise (MNE) group is a “specified national security contractor” if more than 50% of the U.S. MNE group’s annual revenue—determined in accordance with U.S. GAAP in the preceding reporting period—is attributable to contracts with the U.S. Defense Department or other U.S. government intelligence or security agencies.

U.S. MNE groups that qualify as specified national security contractors may provide Form 8975 and related Schedules A (collectively “Form 8975”) as follows:

- Complete Form 8975 with a statement at the beginning of Part II (Additional Information) that the U.S. MNE group is a specified national security contractor;
- Complete one Schedule A for the United States with aggregated financial and employee information for the entire U.S. MNE group in Part I (Tax Jurisdiction Information) and only the ultimate parent entity (UPE) information in Part II (Constituent Entity Information); and

- Complete one Schedule A for the Tax Jurisdiction “Stateless” with zeroes in Part I (Tax Jurisdiction Information) and only the UPE’s information in Part II (Constituent Entity Information).

No other Schedules A or additional information is required to be presented on the Form 8975.

A specified national security contractor may file an amended U.S. federal return and attach an amended Form 8975, prepared in accordance with Notice 2018-31, in order to supersede an already-filed Form 8975. To prevent the original CbC reports from being exchanged, any amended forms are to be filed by April 20, 2018, if filing on paper, or May 25, 2018, if filing electronically.

KPMG observation

Taxpayers that qualify as national security contractors should carefully weigh the pros and cons of filing (or amending) a CbC report prepared in accordance with this new guidance. The desire to protect potentially sensitive data coupled with the ability to file a significantly simplified CbC report may prove to be an attractive option for many taxpayers, but they should understand the potential risks of filing such a report.

Most notably, Notice 2018-31 only protects U.S. MNE groups that qualify as national security contractors from being subjected to penalties for failure to file (or for filing a substantially incomplete form) in the United States. A CbC report filed in accordance with Notice 2018-31 will not necessarily satisfy CbC obligations in other countries.

As a general matter, the only exception to the requirement to file a CbC report found in the OECD’s base erosion and profit shifting (BEPS) Action 13 final guidance is the consolidated revenue reporting threshold (e.g., \$850 million for U.S. MNE groups). The guidance makes it clear that if an MNE group does not meet the revenue threshold set by the UPE’s home country, reporting will not be required in any jurisdiction. Apart from this allowance, however, there are no other universally accepted exceptions from reporting.

Indeed, the supplemental OECD CbC guidance clearly implies that there are situations when reporting would not be required in the UPE’s home country, but would nevertheless be required at the local country level. In such cases, the OECD recommends that the home country accept a voluntary filing to prevent the need to file the CbC at the local level.

As indicated above, the guidance provided by Notice 2018-31 is not binding on any other tax jurisdiction. The obligation to submit a CbC report in a particular jurisdiction is a requirement at the local country level. A taxpayer generally is only relieved of that filing obligation to the extent the local tax authorities are able to get a copy of the CbC report from the UPE’s home country (or surrogate filing jurisdiction) via an automatic exchange. To the extent a local tax jurisdiction receives a CbC report that is not

prepared in accordance with BEPS Action 13, there is a likelihood that the local CbC requirement will not have been satisfied.

Thus, taxpayers that file CbC reports in the United States in accordance with Notice 2018-31 are potentially subjecting themselves to penalties in other jurisdictions—as no other jurisdiction has signaled an intent to accept U.S. national security concerns as a valid exception from filing.

To date, China is the only other jurisdiction to include a similar exception in their CbC regulations, though it is not clear that this exception extends to local Chinese subsidiaries of foreign MNE groups (i.e., that exception might only apply to Chinese MNE groups).

Accordingly, unless the OECD formally “blesses” the guidance in Notice 2018-31—which tax professionals do not think appears likely—it’s likely that filing a CbC report in accordance with Notice 2018-31 will not satisfy a U.S. MNE group’s CbC obligations in other jurisdictions.

To the extent a U.S. MNE group decides that the benefits outweigh the risks and decides to file a CbC report in accordance with Notice 2018-31, particular care should be paid to the timing of filing such a report. Given the May 25, 2018 due date for amended returns (April 20, 2018 if filing on paper), it’s likely that the IRS has not yet exchanged CbC reports with any tax jurisdiction.

Thus, if a U.S. taxpayer files an amended CbC report by the prescribed due date, it is doubtful that any of the previously filed data will be provided by the IRS to any other tax authority. Note that while the taxpayer’s data will remain secure, the taxpayer will still have to contend with the risks described above.

Taxpayers who choose to file amended returns in accordance with Notice 2018-31 should also be aware of any potential consequences associated with filing an amended return. Unlike Rev. Proc. 2017-13—which effectively allowed U.S. MNEs to file amended returns in order to submit CbC reports past the statutory due date of the return itself without affecting the statute of limitations—Notice 2018-31 provides no such guarantee.

If, on the other hand, a taxpayer has either already filed on a surrogate basis in another location, or has filed a CbC report locally, there is almost no chance of being able to recall that return. Similarly, if a taxpayer has already filed in the United States and decides not to amend this year (e.g., CY2016), but wishes to file in accordance with Notice 2018-31 in a subsequent year (e.g., CY2017), the taxpayer should be aware that the proverbial “cat is out of the bag”—foreign tax authorities either already have the taxpayer’s data or will get it in due course.

By filing what is tantamount to a “zero return” in a subsequent period, taxpayers may be opening themselves up to a barrage of local country “information document requests” (known in the United States as “IDRs”—on multiple fronts. A tax authority

that has received a full CbC report for Year 1 but then receives a CbC report for Year 2 based on Notice 2018-31 won't be too happy.

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