



5x5 series: Insights and actions

FDII issues and potential opportunities

Foreign Derived Intangible Income (FDII) is a category of income for US corporations that was introduced under the TCJA. The section 250 deduction provides an effective tax rate of 13.125% on US income derived from both sales of general property or intangible property to foreign parties for foreign use and the provision of a service to a foreign person, or with respect to property not located within the US, in order to support the policy goals of increasing exports of US goods and services and encouraging US companies to locate more intangible assets in the US. Subsequent regulations and legislative proposals present a complex series of issues for US corporations to analyze, but the analysis is an investment that may reveal the potential to reduce cash taxes.

5 insights you should know

The continued evolution of global and US tax legislation may impact FDII posture (e.g., section 174 mandatory capitalization, decrease to the section 250 deduction after 2025, Pillar Two, local country tax rate increases).

Some supply chain structures produce income that is taxed at the US rate of 21%, while others produce income that may qualify as FDDEI (which may be taxed at a lower rate).

The final FDII regulations require that a corporation's deductions are allocated and apportioned to gross DEI and gross FDDEI under the rules of §§ 1.861-8 through 1.861-14T and 1.861-17 by treating section 250(b) as an operative section described in § 1.861-8(f).

Consider impact and ability to reduce cash taxes through the acceleration of income or other methods changes and elections.

Certain transactions are subject to specific substantiation requirements in order to qualify for a FDII deduction. Taxpayers who do not substantiate their deduction are not entitled to a FDII deduction (zero deduction).

5 actions to take now

- 1 Analyze impact of evolving tax legislation.** Consider impact of mandatory R&E capitalization, future decrease to section 250 deduction, and potential for increased preference towards FDII due to global tax landscape changes.
- 2 Analyze supply chain structure.** Modifying contracts or the supply chain structure, in alignment with business objectives, may qualify some income for FDDEI treatment and save cash tax.
- 3 Analyze expense allocation and apportionment methodologies.** Consider completing a detailed review of expense allocation and apportionment methodologies and ensure consistency with other calculations, including FTC calculations. Analyze R&E allocation and apportionment methodology to ensure conformity with complex guidance in § 1.861-17.
- 4 Accelerate FDII qualifying income with FDII-eligible prepayments.** Prepaying FDII-eligible income that otherwise would be reduced by the section 250 deduction limitation: consider the effect of certain prepaid income on expense allocation and apportionment. Consider method changes and elections impact to section 250 profile in current year and in the future.
- 5 Establish systems and processes.** Transactions occurring on or after 1/1/2021 must be properly substantiated; therefore, taxpayers should have systems and processes in place to extract or collect the data as part of the compliance process.

Connect with us

Jennifer Voorhees
Tax Partner
Deloitte Tax LLP

Gretchen Sierra
Tax Principal
Deloitte Tax LLP

This publication contains general information only and Deloitte is not, by means of this publication, rendering accounting, business, financial, investment, legal, tax, or other professional advice or services. This publication is not a substitute for such professional advice or services, nor should it be used as a basis for any decision or action that may affect your business. Before making any decision or taking any action that may affect your business, you should consult a qualified professional advisor. Deloitte shall not be responsible for any loss sustained by any person who relies on this publication.

As used in this document, "Deloitte" means Deloitte Tax LLP, a subsidiary of Deloitte LLP. Please see www.deloitte.com/us/about for a detailed description of our legal structure. Certain services may not be available to attest clients under the rules and regulations of public accounting. The services described herein are illustrative in nature and are intended to demonstrate our experience and capabilities in these areas; however, due to independence restrictions that may apply to audit clients (including affiliates) of Deloitte & Touche LLP, we may be unable to provide certain services based on individual facts and circumstances.

Copyright © 2024 Deloitte Development LLC. All rights reserved.