

FOREIGN-DERIVED INTANGIBLE INCOME



What is the Foreign-Derived Intangible Income Deduction (FDII)?

- The FDII was introduced in the Tax Cuts and Job Act in 2017
- It is an incentive for US C-corporations to generate revenue from serving foreign markets and applies a preferential tax rate to eligible income
- How to calculate the FDII Deduction:

$$\text{FDII Deduction} = \left(\frac{\text{Deemed Intangible Income (DII)}}{\text{DEI} - 10\% \text{ return on U.S. assets}} \right) \times \left(\frac{\text{Foreign Derived Deduction Eligible Income (FDDEI)}}{\text{U.S. Export Income} - \text{Allocated U.S. Deductions}} \right) \times 37.5\%$$
$$\text{FDII Deduction} = \left(\frac{\text{Deemed Intangible Income (DII)}}{\text{DEI} - 10\% \text{ return on U.S. assets}} \right) \times \left(\frac{\text{Deduction Eligible Income (DEI)}}{\text{U.S. Gross Income} - \text{U.S. Deductions}} \right) \times 37.5\%$$

What kind of income qualifies?

- Don't let the name fool you! Eligible income need not be generated from intangible assets
- This deduction is applicable to sales of most any product or service, wherein the buyer is foreign
- More specifically, the sale must meet 2 conditions:
 - The sale must be to a foreign buyer
 - The product or service must be used outside of the U.S.

The Benefits of Taking Advantage of the FDII

- FDII represents a 37.5% deduction against taxable income
- For U.S. exporters, this essentially brings the Effective Tax Rate (ETR) down to 13.125% on foreign sales of products, royalties and services
- For those already applying for the R&D tax credit, **a significant portion** of the FDII application process and **data gathering** is identical to the R&D application process, making it much easier to qualify and **apply for this deduction and save both on the research credit claim as well as on the FDII deduction.**

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How Anchin Can Help

- Proving that you are eligible for the FDII is more difficult than it may seem
 - Deep understanding of multiple complex technical nuances is necessary in order to yield the largest allowable benefit
 - FDII eligibility and filing may intersect with numerous areas of tax law
 - Properly documenting additional data and making changes to contract language and invoices at the point of sale can be extremely cumbersome
- Anchin's team is experienced in the calculation of tax incentives and deductions, documentation of qualification for tax incentives and deductions and support throughout an IRS or state audit.

Your To-Do List

1. Check to see if you are eligible for the deduction
2. Ensure that you are prepared for an audit and have the required documentation
3. Evaluate your operating/sales structure to see if there are additional benefits that can be obtained by routing transactions differently
4. Build templates to document and quantify the relevant data and information in a proactive fashion.

If you are interested in taking advantage of this lucrative deduction, reach out to **Yair Holtzman, Gwayne Lai** or your **Anchin Relationship partner**.



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