

Monthly US Tax Bulletin

February 2026



Welcome to the February edition of Grant Thornton Bharat's US Tax Bulletin, a monthly guide to keep you informed of key developments across the federal, state, and local tax landscape. In an environment marked by regulatory shifts, economic uncertainty, and increasing complexity, staying informed is crucial to making strategic, compliant decisions. This newsletter is designed to deliver timely, relevant, and actionable insights to help you navigate the evolving tax landscape with confidence.

This edition features curated updates on recent legislative changes, IRS enforcement priorities, and emerging trends. Whether you are navigating corporate tax reform, assessing cross-border implications, or managing compliance challenges, we aim to support your efforts with clarity and precision.

The most notable federal tax updates this month include the OECD's 5 January 2026 package, which introduces the new Side-by-Side arrangement, exempts U.S. MNEs from the Income Inclusion Rule (IIR) and the Undertaxed Profits Rule (UTPR), while adding key safe harbours and guidance to simplify Pillar Two compliance and strengthen global coordination. IRS Notice 2026-11 provides interim guidance on key Section 168(k) bonus-depreciation elections, introduces alternative 40% or 60% options, expands eligible property, and offers greater flexibility for taxpayers until final regulations are issued. The IRS's updated FAQs in Fact Sheet 2025-09 clarify the amended Section 163(j) rules by reinstating the Adjusted Taxable Income (ATI) addbacks for depreciation, amortisation, and depletion, and expanding floor plan financing interest to cover trailer and camper financing. The IRS has opened a 90-day public comment period on proposed updates to the Voluntary Disclosure Practice, introducing a streamlined penalty framework and requiring taxpayers to file all delinquent returns, pay all liabilities within three months of conditional approval, and comply with a six-year disclosure period to avoid potential civil or criminal penalties. The One Big Beautiful Bill Act (OBBBA) repeals the Section 898(c)(2) one-month deferral election, requiring affected foreign corporations to align their year end with their majority U.S. shareholders. Notice 2025-72 explains how taxpayers must allocate foreign income taxes to a short transition year after the repeal of the one-month deferral rule, including Section 987 transition rules. The OBBBA updates §162(m) by applying the USD 1 million executive-compensation deduction limit on a consolidated controlled-group basis, ensuring all entities in the group are treated as a single employer and preventing avoidance through compensation shifting.

Several states have introduced notable tax changes this month. Maryland has decoupled from OBBBA provisions by retaining 60-month Research and Experimental (R&E) amortisation, requiring recomputation of §163(j) interest limits, and disallowing special depreciation for qualified production property beginning in 2025. Texas will start applying current federal tax rules, except for certain items that continue to reference the 2007 Internal Revenue Code when calculating the franchise tax, beginning in 2026. At the same time, the state will align its Cost Of Goods Sold (COGS) depreciation and gross receipts' computations with the amounts reported on the federal return. The California State Controller's Office (SCO) is encouraging businesses with past due unclaimed property obligations to participate in the Voluntary Compliance Programme (VCP). This programme provides eligible holders with a 12% interest waiver, provided they meet the programme's requirements and submit all necessary VCP documentation within the prescribed deadlines. Pennsylvania's Act 45 of 2025 decouples the Corporate Net Income Tax (CNIT) from key OBBBA provisions by requiring the five-year amortisation of all R&E costs, disallowing federal §168(n) Qualified Production Property (QPP) expensing, and applying pre-2025 Section 163(j) interest-limitation rules through proforma federal reporting.

We recognise that tax considerations are integral to broader business strategy. As such, we remain committed to helping you align your tax planning with your organisational objectives, ensuring you are well-positioned to respond to both immediate developments and long-term regulatory shifts.

We trust this edition provides a valuable perspective on the evolving tax and compliance landscape. As we continue to monitor developments at the federal and state levels, our goal is to keep you informed with timely, actionable insights.

Happy reading!



Lloyd Pinto
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A.

Key developments under US federal laws

Organisation for Economic Co-operation and Development (OECD) finalises Side by Side arrangement under Pillar Two, offering major relief for U.S. multinationals

The OECD released a landmark package of administrative guidance on 5 January 2026, establishing the Side by Side (SbS) arrangement under the Pillar Two global minimum tax framework. The package endorsed by the OECD/G20 Inclusive Framework marks a significant political and technical shift in how Pillar Two applies to U.S.-headquartered multinational groups.

Under the new SbS arrangement, U.S.-parented multinational groups will be exempt from the Income Inclusion Rule (IIR) and the Undertaxed Profits Rule (UTPR), recognising that the existing U.S. minimum tax regimes achieve comparable outcomes. This exemption applies to fiscal years beginning on or after 1 January 2026, ensuring continuity after the transitional UTPR safe harbour expires at the end of 2025.

Although the arrangement prevents other jurisdictions from imposing top up tax under the IIR or UTPR, Qualified Domestic Minimum Top Up Taxes (QDMTTs) remain fully applicable, and U.S. MNEs must still comply with the GloBE Information Return (GIR) reporting compliance for 2024 and 2025 (with 2024 filing due as early as June 2026).

The OECD's 5 January 2026 release also included detailed administrative guidance featuring several key measures:

- A permanent simplified Effective Tax Rate (ETR) Safe Harbour, applicable from 2027 (or 2026 if adopted in earlier years).
- A one year extension of the transitional CbCR Safe Harbour, now covering 2027.
- A new substance based tax incentive safe harbour.
- Two Side by Side safe harbours (SbS Safe Harbour and Ultimate Parent Entity (UPE) Safe Harbour), offering meaningful compliance simplifications for eligible MNE groups.
- GIR reporting for 2024 due as early as June 2026.

Together, these measures are intended to increase stability, reduce administrative complexity, and support global coordination as jurisdictions continue implementing the global minimum tax.

[\[OECD/Newsroom/2025/Press Release dt. 5 January 2025, side-by-side arrangement\]](#)

IRS issues interim guidance on full first-year depreciation under OBBBA

The IRS has released Notice 2026-11, giving interim guidance on how taxpayers may make key elections under Section 168(k). This includes the Section 168(k)(5) election, which allows taxpayers to claim 100% bonus depreciation for specified plants when they choose to apply this special rule. It also covers the Section 168(k)(7) election, which permits taxpayers to elect out of bonus depreciation for an entire class of property, offering greater flexibility in tax planning.

In addition, the notice outlines the Section 168(k)(10) election that allows taxpayers to claim:

- 40% bonus depreciation for general property, or
- 60% for long-production-period property and certain aircraft instead of the standard 100% for their **first tax year** ending after 19 January 2025,

The notice further adds qualified sound recording productions to the list of eligible property, treating them as acquired when principal recording begins and placed in service upon initial release. Taxpayers may rely on this interim guidance until final regulations are issued, provided they apply it consistently to all qualifying property. The revised framework offers greater flexibility, permanent incentives, and expanded eligibility, particularly benefiting industries such as manufacturing, agriculture, and the music and entertainment sectors. With 100% bonus depreciation now made permanent, businesses can accelerate deductions, enhancing cash flow and investment planning.

[\[Notice 2026-11\]](#)



IRS releases updated guidance on business interest deduction limitations

The Internal Revenue Service has released updated **Frequently Asked Questions in Fact Sheet 2025-09** that provide enhanced clarity on the recent amendments to Section 163(j), which address the limitations on the deduction of business interest expense following the changes introduced by the OBBBA. There are effective changes from tax years **beginning after 31 December 2024**.

- The taxpayer once again adds back depreciation, amortisation, and depletion when computing the Adjusted Taxable Income (ATI), reinstating a more favourable calculation method.
- Expanded the definition of floor plan financing interest to include the interest on financing for trailers and campers used for temporary living, such as recreational, seasonal, or camping, so long as they are designed to be towed by or attached to a motor vehicle.

Effective changes for tax years beginning after 31 December 2025

- Section 163(j) interest expense now clearly includes interest incurred and capitalised during the year, except for amounts capitalised under Sections 263(g) (interest on straddle transactions) and 263A(f) (capitalisation of construction-period interest).
- Subpart F income, GILTI inclusions, Section 78 gross-ups for deemed paid foreign tax credit, and related deductions are excluded from the ATI to ensure consistent treatment for U.S. shareholders.

[IR-2025-126, Dec. 23, 2025, Fact Sheet 2025-09]

IRS seeks public comment on Voluntary Disclosure Practice proposal

The IRS has opened a 90-day public comment period, ending 22 March 2026, for proposed updates to its Voluntary Disclosure Practice (VDP), including a more streamlined penalty framework. Taxpayers receiving conditional approval must, within three months, file all required amended or delinquent income tax, international information returns, and Foreign Bank Account Report (FBAR), and pay all taxes, penalties, and interest; and execute all required agreements. The disclosure period is six years, and non-compliant taxpayers will be referred for criminal prosecution.

The penalty framework under this proposal is outlined below:

- **Delinquent returns:** Only failure-to-file penalties apply.
- **Amended returns:** A 20% accuracy-related penalty applies.
- **FBARs:** Penalties apply per year, subject to inflation adjustments.
- **International information returns:** Penalties up to USD 10,000 per return, per year.

Taxpayers must electronically file **Form 14457**, identifying all non-compliant years and describing willful conduct. Once pre-cleared, they receive a conditional approval and must file all returns and pay all amounts due within three months, then submit a signed closing agreement and FBAR, as applicable. Failure to comply may result in rescission and potential civil and criminal penalties. The final procedures are expected to take effect six months after publication.

[IR-2025-124]

IRS announces transition rules for foreign tax allocation, and Section 987 pre-transition amounts

The OBBBA repealed the one-month deferral election under Section 898(c)(2). This election allowed many specified foreign corporations to use a non-calendar year that ended one month earlier than the year of their majority U.S. shareholder (for example, 30 November vs. 31 December). Foreign corporations that previously relied on the one-month deferral must now align their taxable year with the year-end of the majority U.S. shareholders. For most affected entities, this shift creates a one-month 'first required year' during the transition.

The IRS released Notice 2025-72, which provides guidance following the repeal of the one month deferral election under Section 898(c)(2). The notice establishes a structured system for allocating foreign income taxes so that they properly align with the income for Subpart F, GILTI, earnings and profits, and Section 960 deemed paid purposes. It also provides that taxpayers electing amortisation must recognise the pre-transition Section 987 gain or loss ratably over 120 months, starting with the first applicable tax year, treating any prior short year as a whole 12-month period, effective for taxable years beginning after 30 November 2025. The notice offers an administrable method for allocating certain foreign income taxes between the shortened 'first required year' and the subsequent taxable year.

[Notice 2025-72]

Comprehensive expansion of §162(m) and new aggregation rule introduced

Under the existing §162(m), public companies are prohibited from deducting compensation exceeding **USD 1 million** paid to “covered employees,” which has, since 2016, included the CEO, CFO, and the following three highest-paid officers, along with any individuals who were covered employees in prior years. Beginning in **2027**, the rule expands further to include the **next five highest-paid employees across the entire group**, regardless of title.

The **OBBBA** introduces a significant modification to the executive compensation rules under **§162(m)** by establishing a new **entity aggregation framework for publicly held corporations**.

A **foreign affiliate** is treated as publicly held for §162(m) purposes only if it meets SEC registration or reporting requirements and is part of an affiliated group that includes a publicly held corporation. In such cases, the affiliated group rules may also be subject to the §162(m) framework.

The new OBBBA framework is designed to prevent companies within the same corporate group from avoiding the USD 1 million deduction cap by distributing compensation across multiple entities. It accomplishes this by treating all controlled-group members as a single employer, applying the USD 1 million deduction cap on a consolidated basis, and allocating the permitted deduction proportionately among paying entities. The OBBBA ensures that the limitation is enforced consistently across the entire corporate group. Overall, the OBBBA amendments ensure that the §162(m) deduction limit applies on a **consolidated, group-wide basis**, effectively closing a longstanding planning gap and strengthening the integrity of the executive compensation deduction rules.

[House of Representatives (H.R. 1), eas, 1 July 2025]

B.

Key developments under U.S. state laws

Maryland decouples from key federal provisions under the OBBBA

Maryland has chosen to **decouple** from several federal-level provisions of the OBBBA [PL 119 21], which are as follows:

- **Full expensing of domestic research or experimental expenditures** under the IRC §174A permits immediate expense for domestic research and experimental (R&E) expenditures. However, Maryland retains the 60-month amortisation requirement, necessitating pro forma federal returns and Form 500DM adjustments when federal expensing is taken. If the taxpayer elects 60-month amortisation on the federal return, no pro forma return and Maryland decoupling adjustment are required.
- **Modification of limitation on business interest** must be recomputed by deducting depreciation and amortisation in the adjusted taxable income instead of earnings before interest, tax, depreciation, and amortisation (EBITDA). This results in a lower allowable interest deduction compared to federal rules, and the difference is reconciled on Form 500DM.

- **Special depreciation allowance for qualified production property under IRC §168(n)**, allowing complete expense of qualified production property that would otherwise be depreciated as per the IRS rules. Maryland has decoupled from this provision for tax years beginning in 2025, requiring an additional modification for any special depreciation claimed under this section.

[Maryland Tax Alert Effective 6 January 2026]



Texas updates franchise tax rules to align with current federal law for 2026 reporting

The state of Texas has issued important guidance outlining changes to how businesses must calculate their franchise tax, effective for the 2026 reporting period. Texas will no longer rely on the outdated 2007 federal tax rules for most items sourced from the federal income tax return. Instead, businesses will now apply current federal tax law when determining the majority of federal based inputs for the franchise tax calculation.

Items continuing to follow 2007 federal provisions:

Certain components will still be governed by the 2007 version of the Internal Revenue Code (IRC), as these provisions are referenced explicitly under Texas law. These include:

- IRC Section 78 – foreign tax credit gross up amounts
- IRC Sections 951–964 – Subpart F income calculations

These are contrasted with foreign royalties and foreign dividends, which do follow current federal law because they are not tied to older IRC references.

Cost of Goods Sold (COGS) Depreciation is used to calculate COGS. Texas will use the federal depreciation amounts reported on a business's federal tax return, including any applicable bonus depreciation. To ease the transition to this approach, businesses may take a one-time adjustment on the 2026 report to reconcile any differences between prior Texas and federal depreciation. Any unused portion of this adjustment may be carried forward.

Gross receipts used for apportionment will align with the amounts reported on the federal income tax return, except in specific instances where Texas law requires a different treatment.

[Texas Comptroller of Public Accounts STAR System, 19 December 2025, 202512012M]

California's Voluntary Compliance programme offers interest relief for holders of past due unclaimed property

The California State Controller's Office (SCO) is urging businesses with past due unclaimed property to participate in the Voluntary Compliance Programme (VCP), which enables eligible holders to become compliant and receive a waiver of the 12% annual interest typically imposed on late-reported property. Unclaimed property refers to inactive financial assets that have been inactive for three years and does not include real estate.

VCP eligibility

To qualify for this programme, holders must meet all of the following conditions: not be currently undergoing an unclaimed property examination or involved in any civil or criminal investigation, must have no outstanding interest assessments from the past five years, and must not have received a VCP interest waiver within the previous five years, except in limited circumstances.

The eligible holders can receive the interest waiver, subject to satisfying the requirements, such as complete the required SCO training (two employees, or one in the case of a sole proprietor), conduct a thorough review of their books and records to identify potential unclaimed property, issue due diligence notices to property owners, file a notice report within the assigned timeframe, respond to any owner inquiries that arise, and ultimately submit the remit report and transfer the applicable property by the designated deadline.

To participate in the Voluntary Compliance programme, holders must submit a completed and signed VCP 01 application to the Controller's office. The office will review the submission, determine eligibility, and notify the applicant of approval or denial. Approved holders will receive an enrollment confirmation and the VCP-02 requirements schedule with all due dates.

[California Voluntary Compliance program]



Pennsylvania's Act 45 reshapes its Corporate Net Income Tax framework

Act 45 of 2025 decouples the state Corporate Net Income Tax (CNIT) from specific federal provisions approved in federal H.R. 1 (P.L. 119-21 One Big Beautiful Bill). The general guidance for corporate taxpayers is as mentioned below:

- **Research & experimentation (R&E) expenditures:** Corporate taxpayers must now add back federal deductions for both domestic and foreign R&E, then deduct the expense for Pennsylvania purposes over the taxable year until the full amount of the original cost has eventually been deducted. The federal bill permits small businesses (generally those with average annual gross receipts of USD 31 million or less – per IRC Section 448(c)) to apply the immediate deduction for domestic R&E for tax years 2022 to 2024. The federal bill permits all other businesses to elect to deduct the remaining domestic R&E for tax years 2022 to 2024 in 2025 or split between 2025 and 2026. Act 45 does not allow these deductions. Instead, any remaining domestic or foreign R&E costs from 2022–2024 that were not amortised for federal purposes must be amortized for Pennsylvania tax at 20% per year over five years, starting in 2025.

- **Depreciation of Qualified Production Property (QPP):** Corporate taxpayers must add back federal Section 168(n) deductions for the QPP and instead compute the Pennsylvania depreciation under the standard IRC §167– §168 rules. This requirement is effective immediately, meaning particular fiscal year 2024 filers may need to incorporate the QPP adjustments when preparing their 2024 Pennsylvania returns.
- **Interest expenses:** Act 45 requires that taxable income, as defined under Section 401(3) of the Tax Reform Code of 1971, be computed as if IRC Section 163(j) applied in the form it was in effect on 31 December 2024. No corresponding adjustments will be made on RCT 101. Instead, taxpayers must reflect the required Section 163(j) adjustment on a pro forma Form 1120 and submit it with the return.

[Corporate Net Income Tax (CNIT) provisions, Act 45 of 2025]



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