24 January 2020

Global Tax Alert

Report on recent US international tax developments - 24 January 2020

NEW! EY Tax News Update: Global Edition

EY's new Tax News Update: Global Edition is a free, personalized email subscription service that allows you to receive EY Global Tax Alerts, newsletters, events, and thought leadership published across all areas of tax. Access more information about the tool and registration here.

Also available is our EY Global Tax Alert Library on ey.com.

The United States (US) Internal Revenue Service (IRS or Service) has finalized regulations that deny nonrecognition treatment to contributions of appreciated property by US persons to certain partnerships with related foreign partners. More specifically, the IRS on 17 January issued final regulations (TD 9891) under Internal Revenue Code[1] Section 721(c), which provide that if a US person transfers certain appreciated property to a partnership with a related direct or indirect foreign partner, the general nonrecognition rule of Section 721(a) does not apply unless the partnership adopts the remedial allocation method and meets certain other requirements. The final regulations further provide that a segment of a tax year resulting from a change in the partners' interests in the partnership, accounted for under the interim closing method in the Section 706 regulations, is treated as a "taxable year" for purposes of applying the consistent allocation method.

The final Section 721(c) regulations, which replace temporary regulations (TD 9814) issued in January 2017, do not materially change the rules in the temporary Section 721(c) regulations. The final rules cause gain recognition with respect to certain property contributed to partnerships. Gain recognition can occur either at the time of contribution or upon later, and perhaps unforeseen, events. The regulations also create significant complexity and administrative burden, and limit flexibility to conduct transactions (including distributing property from a partnership) in the future.

EY

Building a better working world

An IRS official this week commented on last week's IRS announcement offering limited relief from double taxation in regard to the Section 965 transition tax. The official was quoted as saying the announcement is an example of the Service willing to consider — and possibly offer — relief for "one-off, taxpayer-specific issues," and that the Service is interested in hearing about unintended consequences from the application of IRS guidance. While the IRS official said the announcement was "intentionally cryptic," a Treasury official later elaborated that the repatriation relief is meant to be seen as offered on a case-by-case basis and not based on a certain set of guidelines that taxpayers must meet. The IRS will listen to the taxpayer's particular circumstances and determine whether the taxpayer merits double taxation relief, he said.

The IRS official also indicated that the Service soon will be issuing the first quarterly update to the 2019-2020 priority guidance plan. He said the update will include projects resulting from 2019 legislation, including last summer's *Taxpayer First Act* and legislation enacted just before the end of last year.

US government officials this week also offered some insights into upcoming international guidance. In regard to the Section 245A dividends received deduction (DRD), an IRS official was quoted as saying that final Section 245A regulations — that follow temporary regulations issued in June 2019 (TD 9865) — would be issued before general proposed regulations on the DRD. A Treasury official this week was also quoted as saying the Government is considering making changes to the temporary DRD regulations in respect of the "extraordinary reduction closing-the-books election," and that those regulations could be finalized by early spring.

The IRS official also declined to take a position on whether Treasury and the IRS should adopt an expansive approach with respect to DRD eligibility for dividends from lower-tier specified foreign corporations, saying the Government is still considering whether to extend the deduction to the CFC (controlled foreign corporation) level, as opposed to it being only applicable to domestic corporations. He noted that determining eligibility in this regard could present a problem.

Another Treasury official was quoted this week as saying that final Section 163(j) business interest deduction limitation regulations will be released with newly proposed regulations that will address issues not covered by the coming final regulations. The proposed regulations under Section 163(j) have not been sent to the Office of Management and Budget's (OMB) Office of Information and Regulatory Affairs for review, which may delay the release of the final interest limitation regulations (which have been at the OMB since mid-December 2019).

The US and France reportedly have reached agreement to defuse the ongoing dispute over France's enactment of a Digital Services Tax (DST) last July, and thereby possibly avert a trade war. According to press reports, France will suspend collection of the 3% DST and, in turn, the US will not impose retaliatory tariffs of up to 100% on approximately US$2.4 billion of French goods. No action by either side will be taken through the end of 2020 in the hopes of reaching a multilateral digital tax agreement.

In the meantime, US Treasury Secretary Steven Mnuchin this week was quoted as saying that the United Kingdom and Italy may face retaliatory US tariffs if they continue with their own, respective, digital services taxes. The US Government's position is that unilateral digital services taxes are discriminatory against US companies.

Endnote

1. All "Section" references are to the Internal Revenue Code of 1986, and the regulations promulgated thereunder.

For additional information with respect to this Alert, please contact the following:

Ernst & Young LLP, International Tax and Transaction Services, Washington, DC

- Arlene Fitzpatrick arlene.fitzpatrick@ey.com
- Joshua Ruland joshua.ruland@ey.com

EY | Assurance | Tax | Transactions | Advisory

About EY
EY is a global leader in assurance, tax, transaction and advisory services. The insights and quality services we deliver help build trust and confidence in the capital markets and in economies the world over. We develop outstanding leaders who team to deliver on our promises to all of our stakeholders. In so doing, we play a critical role in building a better working world for our people, for our clients and for our communities.

EY refers to the global organization, and may refer to one or more, of the member firms of Ernst & Young Global Limited, each of which is a separate legal entity. Ernst & Young Global Limited, a UK company limited by guarantee, does not provide services to clients. For more information about our organization, please visit ey.com.

© 2020 EYGM Limited.
All Rights Reserved.

EYG no. 000371-20Gbl

1508-1600216 NY
ED None

This material has been prepared for general informational purposes only and is not intended to be relied upon as accounting, tax, or other professional advice. Please refer to your advisors for specific advice.

ey.com