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# Washington Dispatch

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## Tax treaties

### **US treaty negotiations with Israel, Switzerland set to start, pending treaties require TCJA updates**

The US Government is set to begin negotiations with Israel and Switzerland to update the existing bilateral tax treaties with those countries. A Treasury official recently was quoted as saying that those discussions will begin very soon; the Swiss treaty was signed in 1996, the Israeli accord in 1975 and will require a full revision.

The official said the proposed treaties with Vietnam and Poland, signed in 2015 and 2013, respectively, require updates to reflect the *Tax Cuts and Jobs Act* (TCJA). Negotiations are taking place with Vietnam for targeted reservations, and tax treaty negotiations with Romania and Norway reportedly are near completion. Neither the Romanian nor Norwegian treaties have been signed and will require targeted reservations to reflect the TCJA.

The Treasury official further indicated he was optimistic the Senate would give its advice and consent to the proposed US-Chile tax treaty before the end of the year, noting that targeted reservations to that accord have been drafted and are with the Chileans for approval.

## Treasury and IRS news

### **PTEP regs coming in Q1 2023, Section 367(d) guidance possible this year**

A Treasury official offered insights in mid-September in regard to some eagerly anticipated pending international tax regulations projects.

Long-awaited and long-delayed proposed regulations on previously taxed earnings and profits (PTEP) will likely not be released in 2022 as had been hoped. A senior Treasury official said the coming PTEP regulations - over 200 pages - are now expected to be released in the first quarter of 2023. The official was quoted as saying the proposed rules would address the application of Section 959(b) in situations in which there are multiple shareholders that do not have pro rata shares of existing PTEP accounts.

The Treasury official further noted that it is possible the Government will release regulations under Section 367(d) in 2022 that deal with the situation when intangible property is transferred from the US and then repatriated. Treasury also reportedly is looking to quickly finalize proposed regulations under Section 1256 that were issued in July 2022.

## **Congress passes CR to fund government; little action expected until after mid-term elections**

Congress passed a continuing resolution (CR) to extend federal government funding beyond 30 September 2022 and into December, hours before the fiscal year deadline. The House and Senate adjourned and will not return to session until after the November mid-term elections.

After the midterm elections, and before the December expiration of the just-passed CR, Congress is expected to try to assemble a year-end bill that could address tax and possibly retirement issues, in addition to government funding that could extend through the remainder of the fiscal year.

House Republican leaders on 23 September also unveiled their "Commitment to America" platform, a blueprint of post-election Republican priorities if Republicans take control of the House in January following the November mid-term elections.

In regard to taxation, the plan is anchored in ensuring that the TCJA tax rates (i.e., individuals and small business) remain permanent. Preview documents called for continuing "proven pro-growth tax policies that increase take-home pay, reduce the cost of living, boost local businesses, and encourage innovation."

In a related action, Rep. Vern Buchanan (R-FL), one of three members vying for the Ways and Means chairmanship in the next Congress should Republicans take control of the House, introduced the *TCJA Permanency Act* (H.R. 8913) to make permanent the 2017 tax cuts for individuals and small businesses.

High on the list of priorities coming out of Treasury will be guidance on the *Inflation Reduction Act's* new corporate alternative minimum tax (CAMT). The official said there are myriad outstanding issues related to the provision and that guidance will be released in tranches. He noted that while the CAMT provision is domestic, it has numerous international tax implications that will need to be addressed. Treasury has broad regulatory authority and will initially address basic questions, the official said, including: the scope of the CAMT, i.e., those that are covered by the provision, what is an applicable corporation, issues in the foreign-owned context, and what income should be included in the base.

### **Treasury and IRS to issue proposed regulations on application of noncompulsory payment regs to certain amended Puerto Rico tax decrees**

The US Government announced in [Notice 2022-42](#) that they plan to issue proposed regulations amending the Section 901 regulations on the application of the noncompulsory payment regulations to certain amended Puerto Rico tax decrees. Taxpayers can rely on the notice pending the issuance of the regulations.

The forthcoming proposed regulations would provide that foreign income tax paid or accrued to Puerto Rico under an existing tax decree amended on or before 31 December 2022, would not be treated as noncompulsory amounts under Reg. Section 1.901-2(e)(5). In particular, the forthcoming proposed regulations would not consider amending an existing tax decree under *PR Act 52-2022* as

increasing a taxpayer's Puerto Rico income tax liability over time for purposes of Reg. Section 1.901-2(e)(5), solely because of any difference in the Puerto Rico income tax liability under the existing tax decree and the amended tax decree.

The taxpayer, however, must have its existing tax decree amended on or before 31 December 2022, and "the taxpayer's Puerto Rico income tax liability under the amended tax decree in each [tax] year [must be] less than the amount of income tax the taxpayer would have owed to Puerto Rico under Puerto Rico's generally applicable income tax laws in the absence of any tax decree in the [tax] year."

Notice 2022-42 provides that no inference as to the application of the noncompulsory payment regulations in any other context should be drawn from the notice.

The forthcoming proposed regulations would apply to tax years ending on or after 11 October 2022, which is the date the notice will be published in the Internal Revenue Bulletin.

Notice 2022-42 does not eliminate completely the need to undertake an analysis of the noncompulsory payment rules under Reg. Section 1.901-2(e)(5). Taxpayers must still analyze whether entering into a new agreement would cause their tax liability to exceed their tax liability as determined under Puerto Rico's generally applicable tax laws.

Furthermore, under Reg. Section 1.901-2(e)(5), the analysis must be on a separate entity by separate entity basis, which means that in the case of a US-based company with a controlled foreign corporation (CFC) in Puerto Rico, the noncompulsory payment rules must be applied to the US entity and the CFC separately.

### **EY comments on Inflation Reduction Act's CAMT**

EY has commented to Treasury on the *Inflation Reduction Act's* enactment of the corporate alternative minimum tax (CAMT) in a 15 September 2022 letter. EY writes that it has become clear that "book income (i.e., income or gain reflected on a corporation's US GAAP financial statements) resulting from transactions intended to qualify for tax-free treatment under Internal Revenue Code sections 355 and 361 (i.e., Section 355 Separations) should be excluded from the calculation of adjusted financial statement income ("AFSI") for purposes of the CAMT." The firm writes that this position is consistent with the purpose underlying Section 355, the correct implementation of the new CAMT, and "how book income from extraordinary transactions such as Section 355 Separations are generally viewed and treated in the marketplace."

EY notes "there is clear regulatory authority for achieving this outcome and allowing corporations to continue traditional transactional planning that is critical to achieving optimal business success." Therefore immediate guidance is needed that "excludes book income from Section 355 Separations (as well as other acquisitive and restructuring transactions that Congress intended to treat as tax-free) from AFSI, while the broader issues raised by the CAMT continue to be studied and addressed over time."

## IRS Chief Counsel memo clarifies process for determining assessment statute expiration date in multi-year Section 332 liquidation

An IRS Chief Counsel memorandum ([AM 2022-002](#), dated 2 September 2022) concluded that the IRS should not only rely on Form 952 when determining the Assessment Statute Expiration Date (ASED) for a multi-year Section 332 liquidation, but should thoroughly review all the information filed by the parent and subsidiary to identify the tax year in which the first distribution was made.

The memo was written in response to an LB&I Workflow Coordination Liaison request about how to determine the ASED if the parent has not yet filed its return for its third tax year beginning after the end of the tax year of the first liquidating distribution. The memo says the IRS should assume that the ASED is the earliest possible date and adjust that date later if it receives information from the fourth year after the first distribution.

The memo also clarifies that the ASED is the same for all tax years during which the parent received a liquidating distribution from the subsidiary and for which it filed Form 952.

Sometimes it is not clear when the subsidiary made its first distribution, according to the memo, but it is the understanding of Chief Counsel that “the current practice is to treat the taxable year for which the initial Form 952 was filed as the year of the first liquidating distribution.” The memo recommends modifying that practice by thoroughly reviewing all the information filed by the parent and subsidiary to identify the tax year in which the first distribution was made. Specifically, the IRS should review (i) Form 952; (ii) Form 966, *Corporate Dissolution or Liquidation*; (iii) when the first distribution was made; (iv) each statement the parent filed with its income tax returns; and (v) the events that occurred before the liquidation plan was formerly adopted.

The memo also specifies who may execute Form 952 on behalf of the parent for each tax year.

Chief Counsel Memo AM 2022-002 reminds taxpayers that filing Form 952 is a specific requirement for Section 332 treatment for a complete liquidation under the multi-year alternative under Section 332(b)(3). Failure to file Form 952 may result in the IRS denying nonrecognition treatment to a complete liquidation that would otherwise have qualified under Section 332.

The Memo provides a useful overview of the ASED’s mechanics when a Form 952 is filed. Moreover, the Memo provides specific guidance on who has signatory authority to execute a Form 952. The Memo should be read in conjunction with the IRS’s Internal Revenue Manual Section 25.6.22.6.2.3.1.

In addition, the Memo usefully reiterates the IRS’s positions with respect to busting Section 332 liquidations, the timing of the plan of liquidation adoption and the continuation of consolidated group membership in financially stressed situations.

## Transfer pricing news

### Sixth Circuit rules in favor of Eaton in appeal from Tax Court regarding APA cancellation

The Sixth Circuit Court of Appeals on 25 August 2022 held in [Eaton Corp. & Subs. v. Commissioner](#) that the IRS had the burden of proving that there were grounds to cancel the Advance Pricing Agreements (APAs) under generally applicable contract-law principles and the IRS failed to meet that burden.

The Sixth Circuit also held the IRS could not impose Section 6662 penalties on Eaton Corporation’s (Eaton) self-reported adjustments. Eaton was thus eligible to claim relief from double taxation under Revenue Procedure 99-32.

The Sixth Circuit’s opinion likely has limited applicability to other taxpayers. The Sixth Circuit relies on Eaton’s unique facts within the confines of the APAs and the APA Revenue Procedures in effect during the years at issue.

### FinCEN issues final rule on beneficial ownership information reporting requirements

Treasury’s Financial Crimes Enforcement Network (FinCEN) on 28 September 2022 issued a [final rule](#) requiring certain entities to file reports with FinCEN that identify two categories of individuals - (1) beneficial owners of an entity and (2) individuals who have who have filed an application with specified governmental authorities to create the entity or register it to do business. The new regulations implement section 6403 of the *Corporate Transparency Act*, enacted in 2021.

Although the IRS very rarely cancels an executed APA, taxpayers must be careful not to apply the conclusions in this case to any scenario in which an APA is cancelled. The facts underlying each APA stand on their own. Even when a taxpayer makes a mistake that is discovered in an APA annual report, it is often able to agree to a resolution with the IRS while keeping the APA intact. This ruling, however, confirms that APAs are binding under contract-law principles and the IRS has the burden of proof to show the grounds supporting an APA cancellation.

## OECD developments

### OECD holds public consultation meeting on Progress Report on Amount A of BEPS Pillar One

On 12 September 2022, the OECD held a public consultation meeting on the [Progress Report on Amount A of BEPS Pillar One](#), which had been released by the OECD Secretariat on 11 July 2022 in connection with the ongoing OECD/G20 BEPS 2.0 project. The Progress Report describes the proposed design for Amount A, reflecting the mechanics for the new nexus and profit allocation rules being developed under Pillar One with the aim of providing market jurisdictions with a greater share of the taxing rights over global business income.

During the public consultation, three panels discussed key elements of the proposed design for Amount A, including the marketing and distribution profits safe harbor, the approach for eliminating double taxation with respect to Amount A and other aspects of the rules.

Comments from the OECD Secretariat acknowledged that there is work still to be done, including, in particular, more work on revenue sourcing, the design of the marketing and distribution profits safe harbor and the design of the elimination of double taxation rules.

The importance of the commitments with respect to unilateral measures and the need for workable tax certainty processes was also stressed. At the same time, the Co-Chairs of the Tax Force on the Digital Economy emphasized the deadline for reaching signature of the Pillar One Multilateral Convention by mid-2023, which will require that the work advance quickly.

### OECD's Pascal Saint Amans to leave post

Pascal Saint-Amans, Director for the OECD Centre for Tax Policy and Administration, announced on 5 September 2022 that he will be leaving his position at the end of October after 15 years in the post.

### OECD considering two permanent safe harbors for Pillar Two GloBE rules

An OECD official in September 2022 was quoted as saying the organization is considering two permanent safe harbors with respect to the BEPS 2.0 Pillar Two global minimum tax rules (GloBE). The OECD reportedly is considering simplified calculations of the income tax base and effective tax rate, respectively.

EY submitted extensive [comments](#) on the Amount A Pillar One Progress Report. (Earlier, the OECD released the [public comments](#) it had received on the Progress Report.) According to the comment letter submitted by EY, applying the complex mechanics for Pillar One that have been specified to date, it becomes clear that the overall result would be that a relatively small number of mature market jurisdictions would gain additional taxing rights, with the bulk of jurisdictions around the world likely receiving little benefit or seeing a reduction in their taxing rights. This outcome is largely due to the formulaic approach used to determine Amount A.

### OECD publishes Manual on Bilateral APAs

The OECD on 28 September 2022 published its [Bilateral Advance Pricing Arrangement Manual](#) as part of the ongoing tax certainty work of the OECD's Forum on Tax Administration. The Manual was approved by the Inclusive Framework on BEPS and all members of the OECD Forum on Tax Administration.

The Manual is intended to provide an effective guide on Bilateral Advance Pricing Agreements (BAPAs) for both tax administrations and taxpayers, setting out the objectives of BAPAs and obstacles currently faced, 29 Best Practices for engaging in BAPAs and providing practical resources (sample BAPA timelines, template agreements, etc.). The Best Practices do not impose a set of binding rules upon jurisdictions, nor provide or mandate a single and uniform BAPA process for all jurisdictions. Rather, they seek to:

- ▶ Increase transparency and collaboration between competent authorities and taxpayers
- ▶ Ensure symmetries in requested information between competent authorities
- ▶ Mitigate delays created by differences in individual jurisdiction's BAPA processes
- ▶ Ensure realistic expectations as to the resources requirements and expected timeframes

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