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IRS Issues Final Regulations That Exclude Corporate US Shareholders From Application of Section 956

The IRS has issued final regulations (T.D. 9859, https://www.govinfo.gov/content/pkg/FR-2019-05-23/pdf/2019-10749.pdf) that reduce the amount determined under Section 956 for certain domestic corporations that own (or are treated as owning) stock in foreign corporations. Under the regulations, neither an actual dividend to a corporate U.S. shareholder nor such a shareholder's amount determined under Section 956 will result in additional U.S. tax. (Section references are to the Internal Revenue Code of 1986, as amended.)

Section 956 was enacted to prevent taxpayer workarounds on earnings repatriations that were essentially equivalent to a dividend and would have been subject to tax except that they were done through an investment of earnings in U.S. property. Because of the 2017 Tax Cuts and Jobs Act, there was disparate treatment between dividends and Section 956 inclusions. Section 245A provides for a participation exemption system for a U.S. shareholder domestic corporation through a dividends received deduction from a 10%-owned foreign corporation and would not account for a Section 956 inclusion that is not a dividend. Similar to the proposed regulations, the final regulations provide that, like dividends to corporate shareholders, tentative Section 956 inclusions will not result in U.S. tax.

The final regulations make two changes to the proposed regulations. They provide an ordering rule to address situations in which a controlled foreign corporation has prior-year earnings and profits under Section 959(c)(1) (i.e., a Section 956 inclusion) and current-year earnings and profits under Section 959(c)(3) that would not result in an inclusion under subpart F of the global intangible low-taxed income provision. The new ordering rule would treat a hypothetical distribution as first coming out of Section 959(c)(2) earnings and profits (i.e., subpart F inclusion) and then out of Section 959(c)(3) earnings and profits (i.e., other earnings and profits). The final regulations also address circumstances involving domestic partnerships that might have partners that are domestic corporations, U.S. individuals or other persons. The rule provides that a Section 956 inclusion is reduced by the amount that a domestic corporate partner would have been entitled to as a Section 245A deduction on such a distribution, with the remaining amount allocated to the partners in proportion to net income that would come from a hypothetical distribution.

Court of Appeals Holds ERISA Trusts Are Trusts Under Related Party Rules

The U.S. Court of Appeals for the Tenth Circuit, affirming a Tax Court holding, has held in *Petersen* (May 15, 2019, https://www.ca10.uscourts.gov/opinions/17/17-9003.pdf) that an ERISA trust – an employee stock ownership plan (ESOP) in the case decided by the Court of Appeals – holding stock of an S corporation was a trust for purposes of Section 267(c) and that the stock was thus deemed to be held by the trust's beneficiaries, i.e., the ESOP participants.

IRS Rules Stock Redemption Not Essentially Equivalent to a Dividend

The IRS issued Private Letter Ruling 201918009 (https://www.irs.gov/pub/irs-wd/201918009.pdf) finding that a corporation's redemption of a shareholder's stock was not essentially equivalent to a dividend under Section 302(b)(1). Therefore, the amount paid will be treated as a distribution in exchange for the stock redeemed.

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IRS Rules Employee Stock Compensation Not Second Class of Stock

The IRS issued Private Letter Ruling 201918013 (https://www.irs.gov/pub/irs-wd/201918013.pdf), in which it concluded that an S corporation's employee stock compensation plan did not create a second class of stock. The transfer and repurchase restrictions on the plan's shares were disregarded when determining whether the shares awarded under the plan had identical rights to other stock issued by the S corporation.

Senate Finance Committee Task Forces to Review Tax Extenders

Senate Finance Committee Chairman Charles Grassley (R-Iowa) announced (https://www.finance.senate.gov/chairmans-news/grassley-on-launch-of-bipartisan-taskforces-to-resolve-temporary-tax-policy) on May 16 the formation of task forces to examine temporary tax provisions commonly known as extenders to determine ways to provide more long-term certainty for most of the provisions and possibly phase out others. The task forces will look at temporary tax provisions that expired or will expire between Dec. 31, 2017, and Dec. 31, 2019. The committee members will be divided into six groups: workforce and community development, health, energy, business cost recovery, and a combined group consisting of individual, excise and other temporary policies. Grassley said that there will also be a separate group to look at whether there is a core package of tax relief provisions that should be available when natural disasters strike.

IRS' Large Business and International Division Launches Large Corporate Compliance Program

The IRS announced (IR 2019-95, https://www.irs.gov/newsroom/lbi-announces-large-corporate-compliance-program) that it has made "a key advancement in how it identifies its biggest and most complex large corporations." Specifically, the IRS' Large Business and International Division (LB&I) has instituted a new application of data analytics for determining the population of such corporate taxpayers. The program, named the Large Corporate Compliance (LCC) program, covers compliance oversight for LB&I's largest corporate taxpayers and replaces the Coordinated Industry Case program. As described by IRS, the LCC utilizes automatic application of the large-case pointing criteria to determine the LCC population. Such criteria include gross assets and gross receipts. Previously, this was done on a "manual, localized basis," the agency said. IRS further stated: "Automated pointing allows a more objective determination of the taxpayers that should be part of the population. After the population is determined, data analytics is used to identify the returns that pose the highest compliance risk. The LCC program further improves LB&I's ability to efficiently focus its resources on noncompliance."

Virginia Issues Guidelines for Remote Sellers and Marketplace Facilitators

The Virginia Department of Taxation has issued guidelines (https://townhall.virginia.gov/L/GetFile.cfm?File=C:%5CTownHall%5Cdocroot%5CGuidanceDocs_Proposed%5C161%5CGDoc_TAX_2059_20190507.pdf) for new economic nexus laws requiring remote sellers and marketplace facilitators who sell or facilitate sales to Virginia customers to register for the collection of sales and use tax. Under the new laws, remote sellers or marketplace facilitators have economic nexus in Virginia if they sell or facilitate the sales of more than $100,000 in annual gross retail sales or have 200 or more transactions with Virginia customers annually. Remote sellers and marketplace facilitators meeting these requirements must register to collect Virginia sales and use tax beginning July 1. The guidelines will help facilitate the new laws and will become effective on June 27; however, taxpayers are permitted to rely on the guidelines prior to this effective date. The guidelines will be published in the May 27 edition of the Virginia Register and be followed by a 30-day public comment period; those wishing to comment are encouraged to do so beginning May 27 and ending June 26.

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