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## Final, Temporary Regulations Address Post-Inversion Tax Avoidance Deals

The IRS issued final regulations (T.D. 9812 at <http://www.stradley.com/~media/Files/Publications/2017/01/TD9812.pdf>) that identify certain stock of a foreign corporation that is disregarded in calculating ownership of the foreign corporation for purposes of determining whether it is a surrogate foreign corporation. The regulations also provide guidance on the effects of transfers of stock of a foreign corporation after the foreign corporation has acquired substantially all of the properties of a domestic corporation or of a trade or business of a domestic partnership. The final regulations adopt, with changes, proposed regulations (REG-135734-14) issued in 2016. The corresponding temporary regulations (T.D. 9761) are removed. See our prior coverage here. The temporary regulations contain rules related to definitions and disregarding certain stock attributable to passive assets and certain distributions.

In response to comments submitted on the proposed regulations, the IRS and the Treasury Department made certain modifications to the proposed regulations. For example, the IRS and the Treasury Department have determined that transfers of stock of a foreign acquiring corporation in exchange for intercompany obligations generally do not present opportunities to inappropriately reduce the “ownership fraction.” Accordingly, the final regulations exclude from the definition of nonqualified property an obligation owed by a member of the expanded affiliated group if the holder of the obligation immediately before the domestic entity acquisition and any related transaction (or its successor) is a member of the expanded affiliated group after the domestic entity acquisition and all related transactions.

The Treasury Department and the IRS agree that nonqualified property generally should not include an obligation owed by a person who is only a de minimis former domestic entity shareholder or former domestic entity partner. Also, nonqualified property should not include an obligation owed by a person who, before and after the domestic entity acquisition, owns no more than a de minimis interest in any member of the expanded affiliated group. Therefore, the final regulations are modified to provide a de minimis rule for a less than 5 percent ownership interest. Nevertheless, the anti-abuse rule in Section 7874(c)(4) may still apply to disregard transfers of stock in exchange for such obligations. (Section references are to the Internal Revenue Code of 1986, as amended.)

The Treasury Department and the IRS refused to make certain modifications out of concerns about undue complexity and administrative burdens. For example, a look-through approach, under which stock acquisitions would be treated similar to asset acquisitions, would be the preferable approach for harmonizing the treatment, in contrast to the comments’ recommendation to treat certain asset acquisitions similar to stock acquisitions. However, the final regulations do not implement this approach due to the aforementioned concerns. Similarly, another comment recommended that if the final regulations retain different treatment for stock and asset acquisitions, working capital of a foreign target corporation should be excluded from the definition of nonqualified property. But again, the Treasury Department and the IRS have



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determined that providing special rules that exclude working capital from the definition of nonqualified property would result in undue complexity and administrative burden. The final regulations also include certain clarifications. Stock of the foreign acquiring corporation included in the numerator of the ownership fraction is in all cases also included in the denominator of the fraction. Also, the definition of nonqualified property is clarified to provide that an interest in a partnership is nonqualified property only to the extent it is a marketable security or avoidance property. The Treasury Department and the IRS are concerned that the reference in the temporary regulations to Treasury Regulations Section 1.752-1(a)(4)(ii) to define an obligation may cause confusion when applied outside of a partnership setting. The final regulations thus remove the reference to Section 1.752-1(a)(4)(ii) and provide that an obligation for purposes of the disqualified stock rule includes any fixed or contingent obligation to make payment or provide value (such as through providing goods or services).

The final regulations generally apply to domestic entity acquisitions completed on or after Sept. 17, 2009, to the extent described in Notice 2009-78 (2009-40 IRB 452), ([https://www.irs.gov/irb/2009-40\\_IRB/ar09.html](https://www.irs.gov/irb/2009-40_IRB/ar09.html)). The final regulations generally apply with respect to the remainder of the proposed rules in the 2014 proposed regulations to domestic entity acquisitions completed on or after Jan. 16, 2014. However, see Treasury Regulations Section 1.7874-4(k) for certain rules that apply only to domestic entity acquisitions completed on or after the publication

of Notice 2015-79 (2015-49 IRB 775) (<https://www.irs.gov/pub/irs-drop/n-15-79.pdf>) or the final regulations, as applicable. Similar to the 2014 temporary regulations, the final regulations provide that taxpayers may elect to apply all the rules contained in these final regulations to domestic entity acquisitions completed on or after Sept. 17, 2009, and before Jan. 13, 2017 (the transition period), if the taxpayer applies all of the rules consistently to all domestic entity acquisitions completed during the transition period.

### Members of Some Religious Sects Are Exempt From FICA, SECA Taxes

In responding to an inquiry from Sen. Pat Toomey, the IRS summarized the requirements to be met by a religious sect or subdivision in order for a member of the sect or subdivision to qualify for an exemption from either Self-Employment Contributions Act (SECA) tax or Federal Insurance Contributions Act (FICA) tax (Info 2016-0084 at <https://www.irs.gov/pub/irs-wd/16-0084.pdf>).

### IRS Releases Publication on Tax-Sheltered Annuity Plans

The IRS has released Publication 571 (rev. January 2017) (<https://www.irs.gov/pub/irs-pdf/p571.pdf>), Tax-Sheltered Annuity Plans (403(b) Plans) for Employees of Public Schools and Certain Tax-Exempt Organizations, which explains the tax rules that apply to Section 403(b) tax-sheltered annuity plans.

### IRS Updates Publication on Unrelated Business Income of Exempt Organizations

The IRS has released Publication 598 (rev. January 2017) (<https://www.irs.gov/pub/irs-pdf/p598.pdf>), Tax on Unrelated Business Income of Exempt Organizations, explaining which organizations are subject to the tax on unrelated business income, what the requirements are for filing a return, what an unrelated trade or business is, and how to figure unrelated business taxable income.

### Cambodia-U.S. FATCA Agreement Available

The text is available of the agreement (<https://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Agreement-Cambodia-9-14-2015.pdf>) signed by Cambodia and the United States to facilitate implementation of the information reporting and withholding tax provisions of FATCA.