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IRS Announces Guidance on Withholding for Partnership Interests That Are Not Publicly Traded

The IRS released Notice 2018-29, 2018-16 IRB 1 (<https://www.irs.gov/pub/irs-drop/n-18-29.pdf>), announcing that the Treasury Department and the IRS intend to issue regulations under new Section 1446(f) regarding the disposition of a partnership interest that is not publicly traded. (Section references are to the Internal Revenue Code of 1986, as amended.) In general, Section 1446(f)(1) provides that if any portion of the gain on any disposition of an interest in a partnership would be treated under Section 864(c)(8) as effectively connected with the conduct of a trade or business within the United States, then the transferee must deduct and withhold a tax equal to 10 percent of the amount realized on the disposition. Section 864(c)(8) provides that gain or loss from the sale, exchange or other disposition of a partnership interest by a nonresident alien or foreign corporation is effectively connected with the conduct of a trade or business in the United States to the extent that the person would have had effectively connected gain or loss had the partnership sold all of its assets at fair market value. The Treasury Department and the IRS have determined that until regulations, other guidance, or forms and instructions have been issued under Section 1446(f), transferees required to withhold under Section 1446(f)(1) must use the rules in Section 1445 and the regulations thereunder for purposes of reporting and paying over the tax, except as otherwise provided in the notice. The notice also provides exceptions to the withholding, including the transferee's receipt of a certification of non-foreign status, a certification that the transferor had less than 25 percent effectively connected taxable income in three prior taxable years, a certification of no realized gain, or a certification from a partnership of less than 25 percent effectively connected gain under Section 864(c)(8).

IRS Issues Guidance on the Limitation of Business Interest

Notice 2018-28, 2018-16 IRB 1 (<https://www.irs.gov/pub/irs-drop/n-18-28.pdf>), announces that the Treasury Department and the IRS intend to issue proposed regulations providing guidance to assist taxpayers in complying with Section 163(j), which was amended by the Tax Cut and Jobs Act (TCJA) to provide new rules limiting the deduction of business interest expense for taxable years beginning after Dec. 31, 2017. For any taxpayer to which Section 163(j) applies, Section 163(j)(1) now limits the annual deduction for business interest expense to the sum of (1) the taxpayer's business interest income (as defined in Section 163(j)(6)) for the taxable year; (2) 30 percent of the taxpayer's adjusted taxable income (as defined in Section 163(j)(8)) for the taxable year; and (3) the taxpayer's floor plan financing interest (as defined in Section 163(j)(9)) for the taxable year.

The Treasury Department and the IRS intend to issue regulations clarifying that taxpayers with disqualified interest disallowed under prior Section 163(j)(1)(A) for the last taxable year beginning before Jan. 1, 2018, may carry such interest forward as business interest to the taxpayer's first taxable year beginning after Dec. 31, 2017. The regulations will also clarify that business interest carried forward will be subject to potential disallowance.

The regulations are expected to clarify that, solely for purposes of Section 163(j), in the case of a taxpayer that is a C corporation, (1) all interest paid or accrued by the C corporation on indebtedness of such C corporation will be business interest within the meaning of Section 163(j)(5), (2) all interest on indebtedness held by the C corporation

that is includable in the gross income of such C corporation will be business interest income within the meaning of Section 163(j) (6), and (3) the disallowance and carryforward of a deduction for a C corporation's business interest expense under Section 163(j) will not affect whether or when such business interest expense reduces earnings and profits of the payor C corporation. The regulations will also clarify that the limitation in Section 163(j) (1) on the amount allowed as a deduction for business interest applies at the level of the consolidated group (as defined in Treasury Regulation Section 1.1502-1(h)). The regulations will also address business interest income and floor plan financing of partnerships, partners, S corporations and S corporation shareholders.

IRS Announces Section 965 Guidance

The IRS has issued Notice 2018-26, 2018-16 IRB 1 (<https://www.irs.gov/pub/irs-drop/n-18-26.pdf>), announcing that the Department of the Treasury (Treasury Department) and the IRS intend to issue regulations in connection with Section 965, which was amended by the TCJA. The notice also announces relief from estimated tax penalties in connection with the amendment of Section 965 and the repeal of Section 958(b)(4) by the TCJA.

Section 965(a) provides that for the last taxable year of a deferred foreign income corporation (DFIC) that begins before Jan. 1 (such year of the DFIC, the "inclusion year"), the subpart F income of the corporation (as otherwise determined for such taxable year under Section 952) shall be increased by the greater of (1) the accumulated post-1986 deferred foreign income of such corporation determined as of Nov. 2, 2017, or (2) the accumulated post-1986 deferred foreign income of such corporation determined as of Dec. 31, 2017 (each such date, a "measurement date," and the greater of the accumulated post-1986 deferred foreign income of the corporation as of the measurement dates, the "Section 965(a) earnings amount"). The Section 965(a) earnings amount is not subject to the rules or limitations in Section 952 and is not limited by the accumulated earnings and profits of the DFIC as of the close of the inclusion year. Section 965(b)(1) provides that if a taxpayer is a United States shareholder with respect to at least one DFIC and at least one E&P deficit foreign corporation, then the portion of the Section 965(a) earnings amount which would otherwise be taken into account under Section 951(a)(1) by a United States shareholder with respect to each DFIC (the "Section 965(a) inclusion amount") is reduced by the amount of such shareholder's aggregate foreign E&P deficit that is allocated to such DFIC.

Among the numerous announcements in the Notice, the Treasury Department and the IRS intend to issue regulations providing that – solely for purposes of determining whether a foreign corporation is a specified foreign corporation within the meaning of Section 965(e)(1)(B) – stock owned, directly or indirectly, by or for a partner (tested partner) will not be considered as being owned by a partnership under Sections 958(b) and 318(a)(3) (A) if such partner owns less than 5 percent of the interests in the partnership's capital and profits. Additionally, the Treasury



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Department and the IRS intend to issue regulations providing the applicable dates for determining a specified foreign corporation's "final cash measurement date," "second cash measurement date" and "first cash measurement date," and that a United States shareholder takes into account its pro rata share of the cash position of a specified foreign corporation as of any cash measurement date of the specified foreign corporation on which such shareholder is a United States shareholder of such specified foreign corporation, regardless of whether such shareholder is a United States shareholder of such specified foreign corporation as of any other cash measurement date, including the final cash measurement date of such specified foreign corporation.

The regulations are also expected to provide that, for purposes of determining a specified foreign corporation's post-1986 earnings and profits as of the measurement date on Nov. 2, 2017, any foreign income tax (as defined in Section 901(m)(5)) that accrues (1) within the specified foreign corporation's U.S. taxable year that includes Nov. 2, 2017, and (2) after Nov. 2, 2017, but on or before Dec. 31, 2017, will be allocated between the respective portions of the foreign tax base on which the accrued foreign taxes are determined that are attributable to the part of the U.S. taxable year ending on Nov. 2, 2017, and the part of the U.S. taxable year beginning after Nov. 2, 2017. The regulations will also include an anti-avoidance rule and rules related to certain election, reporting and payments. Finally, the notice describes instances when the IRS will provide penalty relief under Sections 6654 and 6655 from tax liability under Section 965.

IRS Updates FAQs and System User Guide for Qualified Intermediaries and Withholding Foreign Partnerships and Trust

The IRS updated the FAQs (<https://www.irs.gov/businesses/corporations/qi-system-faqs>) and System User Guide (<https://www.irs.gov/pub/irs-pdf/p5262.pdf>) regarding its Qualified Intermediary (QI), Withholding Foreign Partnership (WP), Withholding Foreign Trust (WT) System Application and Account Management System, on which users can apply to become a QI, WP or WT, or renew or terminate an existing QI, WP or WT agreement and manage their QI, WP or WT information online.