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# Washington Dispatch

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## Legislation

### Senate Finance Committee approves US-Taiwan tax bill

The Senate Finance Committee approved the *US-Taiwan Expedited Double Taxation Relief Act* in a unanimous 27-0 vote, following committee consideration in an Executive Session held on 14 September 2023.

Under the bill, income from US sources earned or received by qualified residents of Taiwan would be entitled to certain benefits. Those benefits include: reduced tax rates for income otherwise subject to 30% gross basis withholding tax; taxation of income effectively connected with a US permanent establishment; and certain preferential treatment of wages earned by qualified residents.

Finance Committee Chairman Ron Wyden (D-OR) and Ranking Member Mike Crapo (R-ID) released a discussion draft in July with leaders of the House Ways & Means Committee, which may consider a bill on the issue but has not announced plans. With no announced plans for consideration by the Ways and Means Committee, it is unclear when a bill on the issue could be considered by the full House. Both the House and Senate would need to pass the same bill for it to become law with the President's signature. Moreover, the proposed rules become applicable only if reciprocal provisions apply to US persons with respect to income sourced in Taiwan.

### Congress passes CR to fund government until 17 November, avoiding a government shutdown

Congress on 30 September 2023 passed a continuing resolution (CR) to prevent a government shutdown and fund the government through 17 November along with health and other programs. President Biden signed the bill into law several hours before the midnight deadline, setting spending at FY 2023 levels for the duration of the CR.

Separately, the Senate Foreign Relations Committee on 13 July approved the *Taiwan Tax Agreement Act* (S. 1457), a bill to authorize the President to negotiate and enter into a tax agreement with Taiwan to relieve double taxation. At the Senate Finance Committee Executive Session on 14 September, Senator Crapo said he is confident there will be an appropriate path forward for each committee, a point that was echoed by Chairman Wyden.

Michael Plowgian, Deputy Assistant Treasury Secretary for International Tax Affairs, confirmed that a tax information exchange agreement with Taiwan is currently being negotiated.

### Senate Finance Committee holds hearing on IRS Chief Counsel pick

Margorie Rollinson, President Biden's pick to become IRS Chief Counsel and Treasury Assistant General Counsel, testified at her Senate Finance Committee confirmation hearing on 28 September 2023. Rollinson spent most of her career at EY, retiring as EY Deputy Director of National Tax, and has held several senior positions at the IRS including Associate Chief Counsel (International).

International tax was one area of focus for committee Republicans during the confirmation [hearing](#). Ranking Member Mike Crapo (R-ID) said the Administration "invited foreign governments to pursue new discriminatory taxes against our companies in the form of the Undertaxed Profits Rule (UTPR), a surtax which also likely violates our existing bilateral tax treaties." According to Senator Crapo, a collateral consequence was that "Treasury must now exhaust precious resources issuing regulations to attempt to mitigate the double taxation it created by unilaterally committing to a global tax deal that undermines U.S. interests."

The timing for further action on the Rollinson nomination is not clear at this time.

## House Republicans want countries to delay BEPS Pillar Two, adopt GILTI-like regime

US House Republican tax lawmakers reportedly want countries to delay their implementation of BEPS Pillar Two, while also urging nations to adopt rules similar to the US Global Intangible Low-taxed Income (GILTI) regime. According to a press report released in mid-September, the focus has moved from the OECD to getting countries on board to adopt something akin to GILTI.

US House Ways and Means Committee Chairman Jason Smith (R-MO) along with committee members recently met with OECD Secretary-General Mathias Cormann in Paris, explaining the serious concerns with respect to the BEPS 2.0 project in the US Congress.

Chairman Smith told European officials that the US already has a global minimum tax – the GILTI regime – and does “not object to others implementing their own GILTI-type taxes.” However, the Chairman warned that the US “will not suddenly repeal our proven system in favor of an untested regime with substantial complexity and uncertainty.”

The Ways and Means delegation also told OECD officials of their strong objection to “discriminatory digital services taxes that countries have targeted at U.S. companies.”

The Chairman singled out the Pillar Two Undertaxed Profits Rule (UTPR) as particularly problematic, saying: “If countries move forward with the UTPR surtax, we will continue to aggressively pursue tax and trade countermeasures.” Last May, Chairman Smith, along with all committee Republicans, introduced the *Defending American Jobs and Investment Act*, which, if enacted, would impose reciprocal tax measures on multinational companies from countries that “try to use the UTPR to tax U.S. workers and productivity for their own gain.”

According to a Ways and Means [committee press release](#), there is also a concern that the global tax system is “headed for more, not fewer, disputes among countries.”

## Treasury and IRS news

### IRS publishes additional interim guidance clarifying CAMT

The IRS on 12 September 2023 published [Notice 2023-64](#), providing further interim guidance that clarifies certain provisions of the corporate alternative minimum tax (CAMT), enacted under the *Inflation Reduction Act of 2022*. The IRS also announced that it plans to issue proposed regulations that are consistent with the guidance in the Notice and previously issued interim guidance in Notice 2023-7 and Notice 2023-20.

The latest Notice indicates that proposed regulations are anticipated to be effective for taxable years beginning on or after 1 January 2024 and that Taxpayers may rely on the interim guidance issued in Notice 2023-64 (and prior interim guidance issued in the Notices) for taxable years beginning before that date. As the proposed regulations are not anticipated to be retroactive, Taxpayers are expected to apply reasonable interpretations of the statute and the Notices for taxable years beginning before 1 January 2024.

Among the highlights in Notice 2023-64:

#### Definition of “Taxpayer”

Notice 2023-64 defines “Taxpayer” as any entity identified in Section 7701 and the regulations thereunder (including a disregarded entity (DRE) under Reg. Section 301.7701-3), regardless of whether the entity meets the Taxpayer definition in Section 7701(a)(14). Presumably, the clarification that a DRE can be a separate “Taxpayer” for CAMT purposes is to accommodate the Section 56A(c)(6) adjustment.

#### Taxpayer’s AFS determination

Section 56A provides that an adjusted financial statement (AFS) with respect to any tax year means the AFS as defined in Section 451(b)(3) or as specified in regulations or other guidance.

The guidance in Notice 2023-64 expands the definition of AFS provided in Section 451(b)(3) and underlying regulations to include certain unaudited external financial statements and a Taxpayer’s federal income tax return. This expanded definition confirms that every Taxpayer is intended to have an AFS for CAMT purposes and, therefore, have adjusted financial statement income (AFSI).

## Determining AFSI

In general, AFSI means the Taxpayer's financial statement income (FSI) for such tax year, adjusted as provided in Section 56A or regulations or other guidance issued under Section 56A. Notice 2023-64 clarifies that a Taxpayer otherwise may not make any adjustments to FSI in determining AFSI.

The Notice defines FSI generally as the net income or loss of the Taxpayer set forth on the income statement included in the Taxpayer's AFS for the tax year. The Notice clarifies that FSI does not include amounts reflected elsewhere in the Taxpayer's AFS, including in equity accounts such as retained earnings and other comprehensive income.

## AFSI and foreign corporations

Section 56A(c)(4) provides that, in determining the AFSI of a foreign corporation, the principles of Section 882 (i.e., the rules for determining income effectively connected with a US trade or business) apply (ECI Adjustment). Notice 2023-64 clarifies that if a foreign corporation qualifies for and claims the benefits of the business profits provisions of an applicable income tax treaty, the principles of those treaty provisions apply in determining the foreign corporation's AFSI.

Notice 2023-64 clarifies the interaction of the controlled foreign corporation (CFC) Pro Rata Share Adjustment and the ECI Adjustment, providing that if a CFC is an applicable corporation, the CFC's net income for purposes of the CFC Pro Rata Share Adjustment is reduced by the amount of CFC's AFSI (i.e., the amount subject to CAMT at the CFC level).

## CAMT Foreign Tax Credit (FTC)

The CAMT FTC may reduce the CAMT (if the Taxpayer chooses to credit foreign income taxes for regular US federal income tax purposes).

Creditable foreign income taxes paid or accrued by CFCs are limited to 15% of the Taxpayer's pro rata share of its CFCs' income. Creditable foreign income taxes paid or accrued by domestic corporations are not limited.

The Notice clarifies that a foreign income tax is eligible to be claimed as a CAMT FTC in the tax year in which it is paid or accrued for Federal income tax purposes by the applicable corporation or a CFC, provided the foreign income tax has also been "taken into account" on the AFS of the applicable corporation or CFC.

Importantly, consistent with the required adjustment to AFSI, the Notice provides that a foreign income tax is "taken into account" on an AFS for CAMT FTC purposes if any journal entry has been recorded in the journal used to determine the amounts on the Taxpayer's AFS (or an AFS that includes the Taxpayer) for any year to reflect the income tax.

## IRS announces intent to issue proposed regulations for Section 174, would affect cost sharing arrangements

Treasury and the IRS issued [Notice 2023-63](#) (Notice) on 8 September 2023, describing rules that the IRS is considering for inclusion in proposed regulations under Section 174, as amended by the *Tax Cuts and Jobs Act* (TCJA). The guidance also covers the treatment of SRE expenditures (a new term replacing the term "research or experimental expenditures") under Section 460, as well as the application of Section 482 to cost-sharing arrangements that involve SRE expenditures.

The proposed regulations would be effective for tax years ending after 8 September 2023.

Section 174(a)(2) requires taxpayers to charge SRE expenditures to a capital account. Taxpayers must amortize the expenditures over five years (15 years if the SRE expenditures relate to foreign research within the meaning of Section 41(d)(4)(f)), beginning with the midpoint of the tax year in which taxpayers pay or incur the SRE expenditures. Section 174, as amended, applies to SRE expenditures paid or incurred in tax years beginning after 31 December 2021.

Among other things, Notice 2023-63 addresses the effect of Section 174 on Reg. Section 1.482-7 cost sharing arrangements and provides interim guidance to taxpayers on proposed regulations that will revise Reg. Section 1.482-7(j)(3)(i).

Per the Notice, Treasury and the IRS anticipate issuing proposed regulations that will replace the current regulatory text with rules providing that cost sharing payments owed to a participant reduce (1) the category of intangible development costs (IDCs) borne directly by that participant that must be charged to a capital account; and (2) the category of IDCs borne directly by that participant that are not described in the Notice and are deductible.

The Notice also illustrates the ordering principle of how cost sharing payments from the payor reduce the payee's IDC.

Taxpayers subject to the cost sharing rules under Section 482 should review Notice 2023-63 and assess whether the anticipated revisions to Reg. Section 1.482-7(j)(3)(i) align with how they are capitalizing IDCs under Section 174.

### **US Government considering extension of temporary FTC relief, guidance on taxes paid under BEPS Pillar Two**

An IRS official in September 2023 indicated that the government is considering extending the temporary foreign tax credit relief provided in [Notice 2023-55](#) to assist fiscal-year taxpayers. Notice 2023-55, released in July 2023, announced temporary relief for taxpayers seeking a foreign tax credit by deferring key components of Reg. Sections 1.901-2 and 1.903-1, which were issued in December 2021 (TD 9959, 87 FR 276).

A Treasury official was also quoted as saying the government plans to issue foreign tax credit guidance this year to address taxes paid under BEPS 2.0 Pillar Two. Specifically, Treasury hopes to issue rules on the Pillar Two income inclusion rule, undertaxed profits rule and qualified domestic minimum top-up taxes before year-end.

### **IRS official offers international regulatory update**

An IRS official in mid-September 2023 provided an update on the status of various pending international tax guidance. According to the official, proposed previously taxed earnings and profits (PTEP) regulations are "highly unlikely" to be released in 2023. The long-awaited proposed PTEP rules have had several delays over the years.

IRS guidance modifying the rules under Section 367 applicable to cross-border triangular reorganizations "should be out anytime," the official said. The IRS has been actively working on regulations consistent with the guidance in Notice 2016-73 and Notice 2014-32. [Editor's note: These proposed regulations were released on 5 October 2023.]

And a major project on foreign currency gain or loss under Section 987 is still expected to be released in 2023.

### **Treasury official states US preference on transfer pricing rules**

A Treasury economist in September 2023 explained that the US government continues to prefer the adoption of "Alternative A" instead of "Alternative B" in the scoping rules for Amount B of BEPS Pillar One. Amount B provides for fixed returns for in-scope in-country baseline marketing and distribution activities. The key differentiator between the two alternatives - A and B - is whether an additional qualitative scoping criterion is required. Alternative A includes no additional qualitative scoping exclusions.

Other projects that the IRS reportedly is moving forward include finalizing Section 897(h)(4) regulations on disposition of investments in US real property interests by qualified investment entities. And work is continuing on software and cloud computing regulations, the official said. IRS guidance on Section 892 is not expected until sometime in 2024.

### **2024 CAP program accepting new applications**

The IRS's Large Business and International division (LB&I) announced ([IR-2023-164](#)) that it will accept, between 6 September and 31 October 2023, new applications for its Compliance Assurance Process (CAP) program for tax year 2024.

CAP, a cooperative pre-filing program available to certain large taxpayers, is intended to allow the IRS and taxpayers to reach agreement on the treatment of various tax issues before a return is filed. To be eligible, new applicants must: (1) have \$10m or more in assets; (2) be a US publicly traded corporation legally required to submit SEC Forms 10-K, 10-Q and 8-K; and (3) not be under investigation by, or involved in litigation with, any government agency that would limit the IRS's access to current tax records. (See the IRS's [CAP webpage](#) for more information.)

[Modifications](#) for the 2024 tax year include providing a new draft form for international issues.

## **IRS announces major new compliance initiative targeting large partnerships**

The IRS on 8 September 2023 [announced](#) a major new compliance initiative that will focus increased scrutiny on large partnerships, corporations, high-income taxpayers and "promoters abusing tax rules on the books." The IRS will expand its existing Large Partnership Compliance program to additional large partnerships with the help of artificial intelligence. By the end of the month, the IRS indicated it will open exams on 75 of the largest partnerships in the US across industries with assets of more than \$10 billion, on average.

According to the IRS, there will also be expanded focus on partnership issues through compliance letters. The IRS is citing "ongoing discrepancies on balance sheets involving partnerships with over \$10 million in assets, which is an indicator of potential non-compliance" – specifically, discrepancies between year-end balances and beginning balances the following year. Consequently, the IRS plans to focus on "high-risk partnerships" and, beginning in early October, will begin mailing letters to approximately 500 partnerships to address the issue.

The IRS also indicated it will expand its focus on digital assets.

## **IRS rules converting disregarded entity to domestic corporation does not modify debt**

In [PLR 202337007](#) (released in September 2023), the IRS ruled that a transaction in which a disregarded entity is converted into a domestic corporation did not cause a modification of debt previously issued by the entity under Reg. Section 1.1001-3. Accordingly, the transaction does not give rise to a taxable debt-for-debt exchange.

The latest ruling provides the IRS's current position on an issue that has been the subject of various private letter rulings, but which has not been addressed in a revenue ruling or other precedential guidance.

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