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Room 5203
Internal Revenue Service
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Ben Franklin Station
Washington, DC 20044

National Foreign Trade Council Comments on Notice 2023-64

The National Foreign Trade Council (the "NFTC") is writing to provide comments on Notice 2023-64 ("the Notice") regarding the new corporate alternative minimum tax ("CAMT") released by the Department of the Treasury ("Treasury") and the Internal Revenue Service ("IRS") on September 12, 2023.

The NFTC, organized in 1914, is an association of U.S. business enterprises engaged in all aspects of international trade and investment. Our membership covers the full spectrum of industrial, commercial, financial, and service activities. Our members support establishing and maintaining international tax norms that provide certainty to enterprises conducting cross-border operations.

NFTC members appreciate the clarifications provided by the Notice. We highlight that our members have an array of concerns and comments on the Notice; however, we only address issues with an international tax nexus in our comments. Provided below in more detail, NFTC recommends the exclusion of dividends from CFCs to prevent duplication of income with respect to CFCs under Section 56A(c)(2)(C) and (c)(3); additional clarity on CFC income adjustments and certain foreign tax credit ("FTC") rules; and an exclusion of dividends from certain international joint ventures ("JVs").

<u>Background</u>

Public Law 117-169 (August 16, 2022), commonly referred to as the Inflation Reduction Act of 2022 (IRA) amended section 55 to impose the CAMT. The CAMT is based on the "adjusted financial statement income" ("AFSI") of an applicable corporation for taxable years beginning after December 31, 2022. Generally, a corporation is an applicable corporation subject to the CAMT for a taxable year if it meets the average annual AFSI test.

Section 55(a) provides that, for the taxable year of an applicable corporation, the amount of CAMT imposed by section 55 equals the excess (if any) of (i) the tentative minimum tax for the taxable year, over (ii) the sum of the regular tax imposed by chapter 1 of the Code (chapter 1), within the meaning of section 55(c), for the taxable year plus the tax imposed under section 59A.

Potential Duplication of CFC Earnings under Section 56A(c)(2)(C) and (c)(3)

AFSI begins with a taxpayer's net income or loss on its applicable financial statement and then requires several adjustments, two of which may relate to CFC income. First, pursuant to section 56A(c)(2)(C), the taxpayer's AFSI is determined by "only taking into account dividends received from" subsidiaries that are not included on a U.S. consolidated return with the taxpayer, "reduced to the extent provided by the Secretary in regulations and other guidance" (the "dividend inclusion rule"). Second, pursuant to section 56A(c)(3), for US shareholders of CFCs, the taxpayer's AFSI is adjusted to also take into account its pro rata share of the CFC's income or loss (the "CFC adjustment rule").

Section 56A(c)(15) explicitly directs the Secretary to "issue regulations or other guidance to provide for such adjustments to [AFSI] as the Secretary determines necessary to carry out the purposes of this section, including adjustments…to prevent the omission or duplication of any item." This direction is important, because absent clarification, there is the potential for including the same income in AFSI twice (or more than twice). For example, dividends received by a US shareholder from a CFC could be included in AFSI under the dividend inclusion rule, even though they were paid from earnings that were already included in AFSI under the CFC adjustment rule. In addition, where an entity has tiers of CFC holding companies, it appears that the same earnings could be included in AFSI more than twice (e.g., additional inclusions for each time a dividend is made up the chain of CFCs and into the US), certainly an extreme and unintended result. Finally, under US GAAP, an entity that owns a second entity reports as part of its financial statement income that second entity's current year earnings as "equity pickup;" including both the current year earnings and the equity pickup in AFSI would result in an inappropriate duplication in income. Similar issues arise with respect to gains on the sale of CFC stock where some or all of gain represents earnings that have already been taken into account in AFSI.

Section 16.02(3) of the Notice recognizes the potential for duplication of income in these cases, and requests comments on approaches that should be considered to address these cases. Based on the grant of authority in the dividend inclusion rule of section 56A(c)(2)(C) to reduce the amount of dividends taken into account in AFSI and the grant of authority in section 56A(c)(15) to prevent duplication of any item, and the policies underlying the CAMT, it seems clear that the question is not whether duplication should be remedied but how.

We recommend that duplication of CFC income be addressed by excluding from AFSI all dividends and other distributions from CFCs, whether paid to other CFCs or paid to a US shareholder. This approach is the easiest administratively as it does not require the tracking of CFC earnings and profits. Income should be included once in AFSI when initially earned by a CFC of an applicable taxpayer, and not again where simply distributed within a corporate group by a CFC to another member of a taxpayer's corporate group. Thus, the approach provides a straightforward way to eliminate CFC income duplication, regardless of what category of earnings the distributions are paid from, such as PTEP, US ECI or earnings eligible for section 245A. This approach also incentivizes repatriation of earnings back to the US and reduces the compliance burden of tracking CFCs' earnings and profits for CAMT purposes.

Similarly, we recommend that gains from the sale of stock should be excluded to the extent the gains reflect amounts that have already been taken into account for CAMT purposes. Rules similar those provided for in section 961 could ensure that these amounts are not effectively taxed twice under the CAMT.

We also recommend that equity pickups related to CFC earnings be excluded from AFSI. As noted above, under US GAAP, an entity that owns a second entity report the current year earnings of the second entity as part of its financial income as equity pickup. Such equity pickups are then eliminated all throughout the chain as part of consolidation accounting entries. Section 5.02.3(c)(iii)(B) of the Notice disallows elimination entries with respect to an investment in another taxpayer unless it is a disregarded entity. The disallowance appears premised on the equity pickup is not included in AFSI under section 56A(c)(2)(C). However, the language of the Notice disallowing the elimination entries and example in 5.02.3(c)(vii) seem to suggest that equity pickups are not excluded from the calculation of AFSI. The distinguishing element of the example is that it is using a partnership and not a corporation, but it is not explicit enough to fully dismiss the concern.

We have considered whether rules similar to the PTEP rules provided under section 959 would be suitable to address the duplication of CFC income under the CAMT. On balance, we believe that such rules are likely to place administrative and compliance burdens on taxpayers and the IRS that are disproportionate to the incremental policies, if any, that would be advanced as compared to a CFC distribution exclusion rule. The policies underlying the CAMT are best effectuated by applying the minimum tax on the AFSI of the applicable taxpayer's corporate group (including CFCs) reported in taxable years beginning after December 31, 2022, and not the AFSI represented by distributions within the corporate group.

Timing of CFC Income Adjustment

NFTC requests clarity on the timing of a CFC income adjustment. The statute cross-references rules under Subpart F (section 951(a)(2)) to determine the taxpayer's pro rata share of income for the CFC (section 56A(c)(3)(A)). Under this section, a full year of Subpart F income is included on the last day of the CFC's taxable year. We recommend that guidance confirm that, for CAMT purposes, the book income adjustment is similarly on the last day of the CFC's local accounting period (since this is a book concept).

Separately, the CFC income adjustment rules provide that when the foreign income adjustment is a loss, then "the" succeeding taxable year shall be reduced (see Sec. 56A(c)(3)(B)). NFTC requests clarification confirming that "the" succeeding taxable year adjustment includes any cumulative unused prior year negative CFC adjustments. In certain industries, such as the insurance industry, this is particularly important due to the regular and expected loss activity.

CAMT Foreign Tax Credits

With regard to contested foreign taxes, we recommend that a foreign tax credit is permitted consistent with the foreign tax credit rules applicable to the regular income tax. Contested foreign tax generally does not accrue until the underlying dispute is resolved. In practice, the result is that an accrual method taxpayer cannot claim an FTC for a contested foreign tax until the dispute is resolved. However, in certain circumstances taxpayers may be permitted to elect relief in the form of a "provisional credit" for the portion of contested taxes paid. Under section 59(l)(1), a foreign income tax must be accrued (for an accrual method taxpayer) for federal income tax purposes in order to be a CAMT FTC. In the absence of such a rule, a contested foreign tax may result in a temporary CAMT liability because the foreign tax is credited against regular tax, but not against CAMT. This temporary CAMT liability will necessarily reverse when the contest is resolved, resulting in unnecessary administrative and compliance burdens. Therefore, Treasury and the IRS should clarify that CAMT FTC include provisional credits for contested taxes.

Relief for Dividends from Non-Controlled Foreign JVs

After TCJA, earnings repatriation from non-controlled 10% or greater owned foreign corporations is generally not subject to regular income tax because dividends are generally eligible for section 245A dividends received deduction ("DRD"). This system is aligned with the participation exemption systems prevalent in virtually all U.S. trading partners. Under pre-TCJA law, such dividends were not eligible for a DRD, but a deemed paid FTC was provided to relieve double taxation.

Section 59(l) does not provide any relief (e.g., deemed paid credits) for dividends from non-controlled foreign JVs. To the extent the distributions are included in AFSI under section 56A(c)(2)(C), the same earnings may be subject to both foreign tax and CAMT with no relief from double taxation. Had these JVs been treated as CFCs, the U.S. shareholders would be eligible for CAMT FTC for foreign taxed paid by the CFCs and presumably would not be taxed again when the earnings are repatriated back to the U.S. The failure to address double taxation would disincentivize new JV investments abroad, encourage holding JV earnings overseas, and result in double taxation inconsistent with international norms and general notions of fairness. There is no evidence that Congress viewed dividends from JVs, which generally are eligible for a section 245A DRD, as creating a book / tax difference that should be addressed under the CAMT.

Accordingly, we recommend that dividends from non-controlled 10% or greater owned foreign corporations should be excluded from the CAMT, consistent with the provision of a section 245A DRD under the regular tax.