Feedback for REG-106089-18 (§163(j)[1]) as of 2/25/2019

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Prop. Regs. §1.163(j)-1(b)	**Definitions**	Definition of interest	Amend the proposed regulations to define "interest" for purposes of §163(j) as any amount generally treated as interest under the Code or regulations for all purposes, and address tax planning through the anti-abuse rule in Prop. Regs. §1.163(j)-2(h), which allows the Commissioner to re-characterize or disregard arrangements entered into with a principal purpose of avoiding the rules of §163(j) or the §163(j) regulations, or a substantially similar rule. Correspondingly, Treasury and the IRS should withdraw the so-called "anti-avoidance" rule in Prop. Regs. §1.163(j)-1(b)(20)(iv). This rule is overbroad and prejudicial — it only treats amounts as interest expense, but not interest income, and is not limited to transactions or payments that have a purpose or intent of avoiding §163(j). Alternatively, if the proposal to narrow the definition of interest and rely on the -2(h) anti-abuse rules is not accepted, Treasury and the IRS should limit the "anti-avoidance" rule in Prop. Regs. §1.163(j)-1(b)(20)(iv) to transactions that have a principal purpose of avoiding the rules of §163(j) or the §163(j) regulations, similar to Prop. Regs. §1.163(j)-2(h). Finally, if narrowing the -1(b)(20)(iv) anti-abuse is not accepted, Treasury and the IRS should amend the "anti-avoidance" rule in Prop. Regs. §1.163(j)-1(b)(20)(iv) to be symmetrical — that is, any income or gain predominately	The definition of "interest" in the proposed regulations goes far beyond the congressional intent of §163(j), as evidenced by the statutory text and legislative history. There is no indication that Congress intended to address any transactions that were not indebtedness, or payments that are not interest, for U.S. federal income tax purposes. Further, creating an expansive definition of "interest" solely for purposes of §163(j) creates immense administrative burdens for taxpayers without meaningfully contributing to the administration of sound tax policy. For instance, such definition would require extensive analysis on the part of the government as well as taxpayers, and would potentially require system changes to account for the added administrative complexity. As is the case for other federal income tax rules, an anti-abuse rule targeting transactions with a purpose of avoiding the rules would be sufficient to address inappropriate tax planning.

[1] Unless otherwise noted, all section references are to the Internal Revenue Code of 1986, as amended, and the regulations promulgated thereunder.

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			received in consideration of the time value of money should be treated as interest income for purposes of §163(j).	
		Adjusted taxable income (ATI) computation	Strike the limit on depreciation, depletion, and amortization (DDA) included in the ATI addback under Prop. Regs. §1.163(j)-1(b)(1)(iii) and clarify that the exclusion is limited only to DDA captured in ending inventory and the addback for DDA applies to all DDA that reduces taxable income, regardless of whether the expense was above the line in cost of goods sold (COGS) or below the line in total deductions.	Prop. Regs. §1.163(j)-1(b)(1)(ii)(D) provides that for pre-2022 years, depreciation, amortization, and depletion expense deductions are added back for purposes of computed ATI. However, Prop. Regs. §1.163(j)-1(b)(1)(iii) excludes amounts capitalized to inventory for this purposes. The use of "deduction" and the distinction of costs capitalized into inventory suggests that DDA which is allocated to production activities and included in COGS would not be eligible for ATI addback. Legislative history does not indicate an intent to treat a DDA item differently whether an above-the-line component of COGS or a deduction from gross income. Prop. Regs. §1.163(j)-1(b)(1)(iii) should be stricken as it adversely impacts certain business sectors, contrary to Congressional intent. The House and Senate bills differed on whether depreciation, amortization and depletion should be disregarded in computing ATI. The 2022 effective date to reduce ATI for such items was a compromise in conference committee. The impact of this regulation is to

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				accelerate the negative impact selectively to manufacturers in 2018. The rules needed to track and report DDA included in ending inventory and COGS are already in place. • DDA capitalized to inventory is required to be itemized in an attached schedule (see parenthetical to line 4 of the Form 1125-A). • The taxpayer is required to apportion additional §263A costs (including DDA) to ending inventory and COGS pursuant to the regulations (see, e.g., Regs. §1.263A-2(b)). The IRS has procedures for auditing §263A costs, because they affect taxable income outside of §163(j). Thus, the IRS wouldn't be unduly burdened by enforcing rules already in place.
		Section 162 Standard	Clarify that partnerships holding real property under a triple net lease can be considered as engaged in a real property trade/business based on underlying facts since a partnership's trade or business activity is attributed to its partners.	Corporations were automatically granted trade/business status. However, the real estate industry typically uses partnerships or LLCs so clarification is needed to properly apply the real property exception for §163(j).

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Prop. Regs. §1.163(j)-2(g)	**Examples**	Coordination with property eligible for bonus depreciation under §168(k)	Clarify by adding examples consistent with the examples on page 127 of the TCJA "blue book" issued December 20, 2018 regarding property eligible for bonus depreciation under §168(k), that (1) where a taxpayer's business interest expense is not limited under §163(j) without regard to floor plan financing interest, that such floor plan financing interest will be considered not needed to be taken into account under §163(j)(1)(C); and (2) that if a taxpayer chooses to determine their business interest expense limitation without taking into account floor plan financing interest under §163(j)(1)(C), such interest will be considered as not taken into account under §163(j)(1)(C). Under either of these situations, the taxpayer's qualifying property would be eligible for bonus depreciation.	
Prop. Regs. §1.163(j)-4(d)	**Special rules for consolidated groups**	Super-Affiliation Rules	Apply the affiliation rule of the 1991 §163(j) proposed regulations for affiliated groups that do not file a single consolidated return.	When passthroughs were added to §163(j), the wording was changed from "corporation" to "taxpayer." The 1991 proposed regulations applied §163(j) to an affiliated group of corporations and defined an affiliated group to include all U.S. corporations controlled by the same parent, including non-consolidated affiliates. Although the legislative history indicates an intent to treat members of a consolidated group as a single taxpayer, it does not reference the affiliation rule in the 1991 proposed regulations. However, consistent with Notice 2018-28, the proposed regulations treat affiliates that file a consolidated return as a single taxpayer, but do not aggregate non-

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				consolidated affiliates for purposes of determining the §163(j) limitation. This is inconsistent with the 1991 proposed regulations and disadvantages affiliated groups prevented from filing a single consolidated return for business, legal, or regulatory reasons, many of whom had been applying prior §163(j) on an affiliated group basis. The proposed recommendation would not alter the proposed rules for consolidated groups, but would simply allow companies to apply the affiliation rule of the 1991 proposed regulations.
Prop. Regs. §1.163(j)-6	**Application of the business interest deduction limitation to partnerships and subchapter S corps**	Further clarification needed for the intended "self-charged lending transactions" rules	Clarify that when applying the self-charged lending transactions rules, an owner of a partnership or S-Corp should be treated as a lender or a borrower, as long as the owner is related to the owner that is the actual lender or borrower within the meaning of §267(b). The net impact would be that the interest expense is offset by interest income and ignored for purposes of applying §163(j), to the extent that the interest income and interest expense are ultimately recognized between and among related parties.	Treasury intends to adopt rules for the proper treatment of business interest expense and income with respect to lending transactions between a passthrough entity and an owner of the entity. Where a partner or S-corporation shareholder lends to, or borrows from, a passthrough entity, a rule excluding business interest expense and income from the §163(j) calculation would be appropriate. The amount excluded should be based on the amount of income or expense recognized by partners or shareholders that are lenders or borrowers, as well as partners or shareholders that are related to a lender or borrower partner within the

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				meaning of §267(b). To the extent that partners or shareholders are related under §267(b) to the partner or shareholder that is the lender or borrower, it would be appropriate to exclude the business interest income and expense realized by the related parties for purposes of the §163(j) calculation.
		Partnerships owned by a consolidated group	Amend the proposed regulations to provide that partnerships that are wholly owned by members of a consolidated group are disregarded, as are transactions and payments between that partnership and the members of the consolidated group. Although §163(j) treats partnerships as entities in general, it is appropriate to treat a partnership as an aggregate when the partnership is wholly owned by members of a consolidated group.	Applying the §163(j) limitation would treat similarly-situated taxpayers differently—i.e., two consolidated group members that conduct activities directly are considered in the aggregate as part of a consolidated group for purposes of §163(j), but two consolidated group members that conduct those activities through a partnership are subject to §163(j) at the partnership level. This would be consistent with the CFC rules, which treat a "controlled partnership" wholly-owned by CFC group members as a CFC group member. There is no reason to limit this principle to partnerships owned by CFCs. Consolidated groups are subject to a broader and more robust aggregation regime than CFCs. Therefore, aggregate treatment should extend to partnerships that are wholly-owned by a consolidated group of domestic corporations.

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Prop. Regs. §1.163(j)-7	**Application of the business interest deduction limitation to foreign corps and U.S. shareholders**	Application of §163(j) to foreign corporations	Treasury and the IRS should amend the proposed regulations to provide that they do not apply to CFCs without effectively connected income. Alternatively, if the preceding proposal is not accepted, Treasury and the IRS should limit the application of §163(j) to CFCs to instances where a taxpayer has a principal purpose of avoiding federal income taxes.	The rules introduce enormous administrative complexity, but would not meaningfully contribute to federal income tax revenue. While the §163(j) limitation would increase GILTI in the year of limitation, many taxpayers will not incur any additional tax on GILTI in that year as a result of such increase because of excess foreign tax credits in the GILTI basket, which otherwise would be permanently lost. In contrast, any interest expense disallowed by §163(j) could be carried forward indefinitely, reducing tax on GILTI in future years.
Prop. Regs. §1.163(j)-7(b)	**Application of §163(j) to an applicable CFC and certain partnerships**	Election revocability	Revise Prop. Regs. §1.163(j)-7(b)(3) to provide that the "CFC Group Election" alternative approach for computing the deduction for business interest expense is revocable after three tax years.	Taxpayers are allowed to change elections made under several sections of the Code (i.e. R&E expense apportionment, entity classification regulations). The facts for which a taxpayer elected to use the alternative approach under Prop. Regs. §1.163(j)-7(b)(3) could change over the years. Treasury should allow taxpayers to revoke this election after three years.
Prop. Regs. §1.163(j)-7(c)	**Rules concerning the computation of adjusted taxable income of an applicable CFC and certain CFC group members**	Further simplification of group CFC election	Further simplification to the Group CFC election would lead to substantially similar outcomes while reducing compliance burden. Under the proposed regulations, if a CFC Group has no net business interest expense on an aggregate basis, a U.S.	In general, an aggregation approach should provide a similar result to the application of "CFC excess taxable income" as provided in Regs. §1.163(j)-7(c)(3) without the administrative complexity and burden of following the rollup and ordering rules.

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			taxpayer need not engage in any further analysis to apply the §163(j) rules to its CFCs. A similar rule should be provided to taxpayers where, on an aggregate basis, the CFC Group's net interest expense is less than 30% of the CFC Group's adjusted taxable income. Proposed language is provided below: *1.163(j)-7(c)(3)(iii). Safe harbor for Certain CFC Groups. A CFC group (as defined in §1.163(j)-7(f)(6)) shall not apply the limitation in section 1.163(j)-2(b) to any CFC in the event that business interest expense of the CFC group would not have exceeded the amount allowed (as defined by §1.163(j)-2(b)) had an election been made under §1.163(j)-7(b)(3) regardless of whether the election was actually made.*	If the CFC group is in a limitation position after the safe harbor all of the prescriptive rules regarding allocation and election would still apply.
Prop. Regs. §1.163(j)-7(f)(6)	**Definitions**	Definition of CFC group	Amend the proposed regulations to allow grouping for CFCs that either (x) are owned more than 50%, by value, by a single U.S. shareholder or in the same proportion by related US shareholders, or (y) would constitute an affiliated group as defined in §1504(a) but without regard to §1504(b)(3).	As the preamble notes, the CFC group rules in the proposed regulations are based on the principle that money is fungible within a group of highly related CFCs, where borrowings essentially support the entire group. However, many situations that fall squarely within this principle are ineligible for CFC grouping under the unnecessarily narrow rules in the proposed regulations. The 80% threshold in the proposed regulations is arbitrarily high and inconsistent with existing CFC rules. A 50% threshold would be

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				more consistent with the existing rules, including the rules for determining CFC status. In addition, requiring that the highest-tier CFC in a CFC group satisfy a high minimum US ownership threshold excludes many situations in which highly related CFCs engage in intercompany loans to support all of the CFCs. For example, consider a situation where a US shareholder owns 30% of a CFC holdco that wholly owns several other CFCs, including a finco that on-lends to the other CFCs. The CFCs are all highly related to each other through their common ownership by the CFC holdco and are all supported by the finco's borrowings, such that not grouping the CFCs would result in an inappropriate mismatch of income and deductions.
Prop. Regs. §1.163(j)-10(c)	**Allocating interest expense and interest income that is properly allocable to a trade or business**	De minimis election	Any §163(j) de minimis rule that could be applied to a regulated utility should not be elective.	Making the de minimis rule elective would introduce regulatory uncertainty and undermines the administrative ease the de minimis rule seeks to provide.
Prop. Regs. §1.382-2(a), -6(b)	**General rules for ownership change, Closing-of-the-books election**	M&A transactions	Permit closing of the books. For acquisitions, the interest expense limitation disregards any election under §382 to close the books. Instead, it requires a pro rata allocation based on number of days in each period. This could create challenges with acquisitions as this may unnecessarily require	One significant issue that will impact M&A transactions is related to the calculation and utilization of the business interest expense limitations for entities acquired during the year. Under Prop. Regs. §1.382-2(a)(7), disallowed business interest expense (BIE)

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			buyers to share post-close financial information with sellers in order to properly calculate the pre-acquisition return.	should be allocated pro-rata to the pre- and post-acquisition periods based on the number of days regardless of whether an election was made to close the books. This is echoed in Prop. Regs. §1.382-6(b)(4) which states that the BIE is allocated based on the number of days without regard to any close-the-books election. Further, the limitation for the entity is allocated on number of days as well. For example, if X was sold to Y on 3/31/19 and had a limitation of $200 for the tax year, then a limitation of $50 (3/12 x $200) would be applicable to the pre-acquisition period and $150 to the post-acquisition. Further, if there was $600 of BIE for the year there would be a $400 disallowance ($600 BIE minus $200 limitation). This would be split so that $100 (3/12 x $400) would be applicable to the pre-acquisition period and $300 to the post-acquisition. This could create challenges with acquisitions since the full year business interest expense and adjusted taxable income is required to determine the limitations. It suggests a taxpayer would need to provide post-close information of the acquired entity, including taxable income, depreciation and amortization, business interest income, and BIE to the sellers for their preparation of the

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				pre-acquisition returns. Agreement on the calculation and presentation would be required for consistency across the return periods. To avoid this complication, a closing of the books election should also be allowed.