

CHAMBER OF COMMERCE
OF THE
UNITED STATES OF AMERICA

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August 21, 2018

The Honorable Steven T. Mnuchin
Secretary of the Treasury
U.S Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

The Honorable David J. Kautter
Assistant Secretary for Tax Policy
U.S Department of the Treasury
1500 Pennsylvania Avenue, NW
Washington, DC 20220

RE: Overpayments and §965(h)¹

Dear Messrs. Mnuchin and Kautter:

The U.S. Chamber of Commerce applauds Treasury Department and the Internal Revenue Service (IRS) guidance for reporting requirements under §965, as amended by the Tax Cuts and Jobs Act (TCJA). While the Chamber appreciates Treasury and IRS guidance implementing the TCJA, we are extremely concerned that recent §965 pronouncements,² which provide that an overpayment of taxes (including estimated taxes) will be applied in full against a taxpayer's transition tax liability, are contrary to Congressional intent.³ Accordingly, the Chamber respectfully requests that you revise relevant guidance to allow taxpayers a choice in how their tax payments are applied, consistent with the eight-year installment payment period enacted as part of §965(h) and the deferred payment period pending a triggering event for electing S corporation shareholders under §965(i)(1), and necessary for the equitable administration of the reformed tax code. It is imperative that the Administration deals with this issue expeditiously, given the upcoming tax return filing and estimated payment filing dates.

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

² See Office of Chief Counsel Internal Revenue Service memorandum CC:PA:04:TWCurtman, "Overpayments and I.R.C. § 965(h)," (Aug. 2, 2018), available at https://www.irs.gov/pub/irao/pmta_2018_16.pdf; "Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns," FAQ 13 and 14 (Apr. 13, 2018), available at <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns>.

³ On Aug. 16, 2018, Nina Olson, National Taxpayer Advocate, posted a blog titled "NTA Blog: IRS Administration of the Section 965 Transition Tax Contravenes Congressional Intent and Imposes Unintended Burden on Taxpayers," available at <https://taxpayeradvocate.irs.gov/news/nta-blog-irs-administration-of-the-section-965-transition-tax-contravenes-congressional-intent-and-imposes-unintended-burden-on-taxpayers?category=Tax>. The blog generally argues that "Congress enacted a provision with a transition rule intended to be extremely taxpayer-favorable, and the IRS is administering the provision in a way that seemingly runs contrary to congressional intent."

Background

IRS guidance⁴ indicates any taxpayer's overpayment of estimated tax payments to the IRS or any tax overpayment for any year will be applied *in full* against the taxpayer's *total* transition tax liability. In practice, instead of applying a 2017 overpayment as a refund or credit against 2018 tax liability, taxpayers are forced to have paid a large portion – or all – of their transition tax in the first year, effectively forfeiting the taxpayer's election to pay the tax over eight years (or until an S corporation triggering event) as planned. This guidance is contrary to statutory language, legislative intent, and even the IRS's own interpretation of these provisions.

Pursuant to §965(h)(1), the schedule for taxpayers who elect to pay their deferred foreign income tax over eight years is as follows: (1) for years one through five, the installment is 8% of the net tax liability, (2) for year six, the installment is 15% of the net tax liability, (3) for year seven, the installment is 20% of the net tax liability, and (4) for year eight, the installment is 25% of the net tax liability. Further, §965(h)(3) provides specific events that would accelerate payments under this section. Additionally, S corporation shareholders may elect to defer payment of their net §965 tax liability until the year in which a defined "triggering event" occurs pursuant to §965(i)(1), and can further defer payment of such liability over eight years following the triggering event under §965(i)(4). According to the legislative history,⁵ "[t]he tax resulting from the provision would be payable over time, *to allow taxpayers time to compute their liability and repatriate funds to pay it.*"

In its own guidance (FAQ 10) issued March 13, 2018,⁶ the IRS itself implies that the payments related to the §965 liability would be tracked separately from regular tax liabilities, detailing that it would require two separate payments, one payment reflecting the tax owed without regard to §965 and a separate payment reflecting the amount owed under §965. Then, on

⁴ See "Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns," FAQ 13 and 14 (Apr. 13, 2018), available at <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns> (emphasis added).

⁵ See Section-by-Section Summary prepared by Ways and Means Committee Majority Tax Staff for the Tax Cuts and Jobs Act (H.R. 1), As Ordered Reported by the Committee, available at https://waysandmeansforms.house.gov/uploadedfiles/tax_cuts_and_jobs_act_section_by_section_hr1.pdf (emphasis added). See also Olson, National Taxpayer Advocate, "NTA Blog: IRS Administration of the Section 965 Transition Tax Contravenes Congressional Intent and Imposes Unintended Burden on Taxpayers," available at <https://taxpayeradvocate.irs.gov/news/nta-blog-irs-administration-of-the-section-965-transition-tax-contravenes-congressional-intent-and-imposes-unintended-burden-on-taxpayers?category=Tax> (noting "Thus, congressional intent here seems pretty clear: The bad news for affected U.S. shareholders is that the United States plans to collect tax on the value of accumulated foreign earnings whether or not funds are actually repatriated. The good news is that taxpayers will have eight years to pay the liability – with smaller payment amounts in the early years and no interest charges at all."). Olson later notes, "Where Congressional intent is clear, it is the job of administrative agencies to give effect to that intent to the extent feasible. In some cases, that may require adopting a plausible interpretation, even if it not the "best" interpretation."

⁶ See "Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns," FAQ 10 (Mar. 13, 2018), available at <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns>.

April 13, 2018, the IRS issued additional guidance (FAQ 13 and 14),⁷ effectively abandoning the bifurcated approach of FAQ 10 mere days before tax payments were due.

As taxpayers often overpay with regard to their tax liability without regard to §965, FAQ 13 and 14 will consistently result in additional amounts allocated to §965 installment payments. This results in a significantly shortened installment period and an acceleration of millions of dollars of tax payments.⁸ That result is simply not consistent with the clear reading of §965(h) and (i) or with the policy Congress intended by including an election to make installment payments over the prescribed eight-year period or to defer the payment until the year of an S corporation triggering event.

Authority

The IRS released FAQs 13 and 14 without citing any supporting authority. Subsequently, on August 2, the IRS released a Chief Counsel Memorandum basing the FAQ position on an interpretation of §§6402 and 6403. Contrary to that memorandum, §6403 does not compel the result in the two FAQs. Section 6403 provides:

In the case of a tax payable in installments, if the taxpayer has paid as an installment of the tax more than the amount determined to be the correct amount of such installment, the overpayment shall be credited against the unpaid installments, if any. If the amount already paid, whether or not on the basis of installments, exceeds the amount determined to be the correct amount of the tax, the overpayment shall be credited or refunded as provided in section 6402.⁹

Taxpayers who overpaid their 2017 taxes did not overpay as an installment of the §965 tax; they overpaid their 2017 net income tax liability – which by definition excludes the §965 liability for the year. In fact, as the IRS required,¹⁰ taxpayers made separate payments of the first

⁷ See “Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns,” FAQ 13 and 14 (Apr. 13, 2018), available at <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns>.

⁸ See also Olson, National Taxpayer Advocate, “NTA Blog: IRS Administration of the Section 965 Transition Tax Contravenes Congressional Intent and Imposes Unintended Burden on Taxpayers,” available at <https://taxpayeradvocate.irs.gov/news/nta-blog-irs-administration-of-the-section-965-transition-tax-contravenes-congressional-intent-and-imposes-unintended-burden-on-taxpayers?category=Tax> (noting “As a practical matter, this interpretation sharply limits the value of Section 965(h), and in some cases, it may even render it meaningless. Large corporations frequently overpay their estimated taxes for a variety of reasons, including to minimize the risk they may become liable for underpayment interest. Some may even have “overpaid” by most or all of their Section 965 liability. According to the IRS’s interpretation, those corporations will not receive any of the benefits Congress provided by enacting Section 965(h).”).

⁹ Emphasis added.

¹⁰ See “Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns,” FAQ 10 (Mar. 13, 2018), available at <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns>.

installment of the §965 tax liability. Thus, there is no overpayment of the tax payable as an installment.

FAQs 13 and 14 are obviously inconsistent with the intent of Congress in allowing taxpayers to pay their §965 liability over an eight-year period or upon an S corporation triggering event. Since enactment of the TCJA, the Administration has regularly announced its intention of providing robust guidance to carry out the purposes of the rules. In that regard, §965(o) gives Treasury the authority to prescribe “such regulations or other guidance as may be necessary or appropriate to carry out the purposes” of §965 including “regulations or other guidance to prevent the avoidance of the purposes of” §965. The Chamber believes this regulatory authority allows the Treasury and IRS to issue guidance preserving for taxpayers the full eight-year period for paying §965 liabilities, even if they have overpaid their taxes.

In addition, the Chamber is very concerned that FAQs 13 and 14 are functionally tax regulations issued with immediate effect and without following the applicable rules of the Administrative Procedure Act (APA). The Chamber believes this guidance is a legislative rule subject to notice and comment and one that should have been incorporated into the proposed regulations.¹¹ The Chamber was recently involved in invalidating other taxpayer-adverse regulations that would have taken immediate effect without complying with the normal notice and comment requirements required under the APA.¹²

Issues

The practical interpretation in this IRS guidance is problematic for a myriad of reasons. The U.S. tax return process is complex and requires the analysis of large amounts of data. While current law allows for an extension of time to file corporate tax returns resulting in a due date of October 15, the taxpayer is required to satisfy the ultimate tax liability by the original due date, April 15. Therefore, the payment made at April 15 is an estimate of the final amount to be due. Many taxpayers are conservative when making estimated payments to ensure they fully pay their tax liability by the due date so that they do not incur any late payment penalties or interest.

Further, because tax reform became law so late in 2017, many taxpayers were forced to overestimate in preparing their 2017 extension payments to minimize potential underpayment penalties. Unfortunately, since the IRS issued its initial guidance¹³ regarding the application of overpayments to the transition tax when most taxpayers had already scheduled their electronic fund transfers (EFTs), there was insufficient time to redirect the payment to the Q1 2018

¹¹ 5 U.S.C. §553.

¹² See *Chamber of Commerce of the United States v. IRS*, 2017 U.S. Dist. LEXIS 166985.

¹³ The additional IRS guidance on overpayments under §965(h) was issued April 13, 2018. See “Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns,” FAQ 10 (Apr. 13, 2018), *available at* <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns>.

estimate instead of the 2017 extension.¹⁴ As a result, taxpayers lost the right to determine how the funds should be applied. Fiscally conservative taxpayers should not be punished for acting responsibly; rather, taxpayers should have flexibility and be allowed discretion in how overpayments are applied.

For all businesses – and particularly publicly traded companies who report their projected cash taxes – free cash flow is a critical component of financial guidance issued to investors and is used to plan capital investments projects, hiring for job expansions, and other functions. In building cash tax estimates, businesses include anticipated federal tax overpayments to determine the net impact to free cash flow for each respective year. This IRS guidance creates unanticipated volatility in the ability of certain taxpayers to achieve these projected financial commitments for 2018. This can result in businesses being forced to cancel capital investments projects and reduce or cancel planned job expansions, effectively inhibiting some of the intended pro-growth impacts of tax reform.

Additionally, this guidance places taxpayers who are in an overpayment position at a competitive disadvantage to taxpayers who are in an underpayment position. The IRS should not write the election out of the Code for a set of otherwise similarly situated taxpayers simply because one taxpayer has money on account with the government and the other does not, especially where Congress did not draw that distinction in the Code regarding the ability to make the election. Overpayments on account are not a “triggering event” in the Code.

Solution

The Chamber respectfully requests that you revise relevant guidance to allow taxpayers a choice in how their overpayments of tax are applied, consistent with the eight-year installment payment period enacted as part of §965(h) and necessary for the equitable administration of the reformed tax code.

This treatment would be consistent with other similar situations where a taxpayer has an election to pay a liability over a number of years. For example, where a taxpayer has a §481(a) adjustment which is unfavorable to that taxpayer,¹⁵ the full amount of the liability is known; however, the IRS does not take a taxpayer’s overpayment situation into account and the intent of allowing a taxpayer to pay the liability over a number of years is respected. Likewise, the Securities and Exchange Commission (SEC), shortly after the enactment of tax reform, issued guidance,¹⁶ which allows taxpayers a year to calculate and report the tax impact of tax reform in their financial statements. This is in sharp contrast to the current IRS approach, which unduly punishes taxpayers’ use of estimates in calculating tax payments.

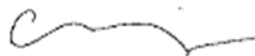
¹⁴ Further, at the time taxpayers made this first payment, the failure to make this required payment could have resulted in the inability to utilize the eight-year installment plan.

¹⁵ See Rev. Proc. 2015-13, §7.03(1), available at <https://www.irs.gov/pub/irs-drop/rp-15-13.pdf>.

¹⁶ See Staff Accounting Bulletin No. 118 (SAB 118), available at <https://www.sec.gov/interps/account/staff-accounting-bulletin-118.htm>.

In sum, the Chamber strongly urges Treasury and the IRS to expeditiously revise relevant guidance to allow taxpayers a choice in how their tax payments are applied, consistent with the eight-year installment payment period enacted as part of §965(h) and the triggering event payment date enacted under §965(i)(1), and necessary for the equitable administration of the reformed tax code. This will ensure as little disruption as possible to normal business operations and encourages the U.S. economy to achieve its true growth potential. The Chamber looks forward to working with you to address this and other issues as we work to implement our new, pro-growth tax code. Thank you for your time and attention.

Sincerely,



Caroline L. Harris

CC: Orrin Hatch, Chairman, Committee on Finance, United States Senate
Ron Wyden, Ranking Member, Committee on Finance, United States Senate
Members of the Senate Committee on Finance
Kevin Brady, Chairman, Committee on Ways and Means, U.S. House of Representatives
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