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Final Regulations Coordinate Code Sec. 245A DRD Limit and GILTI Disqualified Basis Rule

T.D. 9934

Final regulations issued by the Treasury and IRS coordinate the extraordinary disposition rule that applies with respect to the Code Sec. 245A dividends received deduction and the disqualified basis rule under the Code Sec. 951A global intangible low-taxed income (GILTI) regime. Information reporting rules are also finalized.

Extraordinary Disposition Rule and GILTI Disqualified Basis Rule

The extraordinary disposition rule (EDR) in Reg. §1.245A-5 and the GILTI disqualified basis rule (DBR) in Reg. §1.951A-2(c)(5) both address the disqualified period that results from the differences between dates for which the transition tax under Code Sec. 965 and the GILTI rules apply. GILTI applies to calendar year controlled foreign corporations (CFCs) on January 1, 2018. A fiscal year CFC may have a period from January 1, 2018, until the beginning of its first tax year in 2018 (the disqualified period) in which it can generate income subject to neither the transition tax under Code Sec. 965 nor GILTI.

The extraordinary disposition rule limits the ability to claim the Code Sec. 245A deduction for certain earnings and profits generated during the disqualified period. Specifically, Reg. §1.245A-5 provides that the deduction is limited for dividends paid out of an extraordinary disposition account. Final regulations issued under GILTI address fair market basis generated as a result of assets transferred to related CFCs during the disqualified period (disqualified basis). Reg. §1.951A-2(c)(5) allocates deductions or losses attributable to disqualified basis to residual CFC income, such as income other than tested income, subpart F income, or effectively connected taxable income. As a result, the deductions or losses will not reduce the CFC's income subject to U.S. tax.

Coordination Rules

The coordination rules are necessary to prevent excess taxation of a Code Sec. 245A shareholder. Excess taxation can occur because the earnings and profits subject to the extraordinary disposition rule and the basis to which the disqualified basis rule applies are generally a function of a single amount of gain.

Under the coordination rules, to the extent that the Code Sec. 245A deduction is limited with respect to distributions out of an extraordinary disposition account, a corresponding amount of disqualified basis attributable to the property that generated that extraordinary disposition account through an extraordinary disposition is converted to basis that is not subject to the disqualified basis rule. The rule is referred to as the disqualified basis (DQB) reduction rule.

A prior extraordinary disposition amount is also covered under this rule. A prior extraordinary disposition amount generally represents the extraordinary disposition of earnings and profits that have become subject to U.S. tax as to a Code Sec. 245A shareholder other than by direct application of the extraordinary disposition rule (e.g., inclusions as a result of investment in U.S. property under Code Sec. 956).

Separate coordination rules are provided, depending upon whether the application of the rule is in a simple or complex case.

IRS Reminds Employers of Filing Deadline for Form W-2, Wage Statements

The IRS has reminded employers of filing file Form W-2, Wage and Tax Statement, and other wage statements by Monday, February 1, 2021, to avoid penalties and help the IRS prevent fraud. Due to the usual January 31 deadline falling on a Sunday, the due date will be pushed to the next business day. Various other due dates related to Form 1099-MISC, including dues to the IRS, can be found at https://www.irs.gov/forms-pubs/about-form-1099-nec. The IRS also recommended e-file as the quickest, most accurate and convenient way to file said forms. Further, automatic extensions of time to file Forms W-2 would not be available. Finally, guidance on information penalties can be found at https://www.irs.gov/government-entities/federal-state-local-governments/increase-in-information-return-penalties.

IR-2020-269

Reporting Requirements

Every U.S. shareholder of a CFC that holds an item of property that has disqualified basis during an annual accounting period and files Form 5471 for that period must report information about the items of property with disqualified basis held by the CFC during the CFC's accounting period, as required by Form 5471 and its instructions.

Additionally, information must be reported about the reduction to an extraordinary disposition account made pursuant to the regulations and reductions made to an item of specified property's disqualified basis pursuant to the regulations during the corporation's accounting period, as required by Form 5471 and its instructions.

Applicability Dates

The regulations apply to tax years of foreign corporations beginning on or after the date the regulations are published in the Federal Register, and to tax years of Code Sec. 245A shareholders in which or with which such tax years end. Taxpayers may choose to apply the regulations to years before the regulations apply.

Louisiana Victims of Hurricanes Delta and Laura Granted Tax Relief

Louisiana Disaster Relief Notice (LA-2020-06)

The president has declared a federal disaster area in Louisiana. The disaster is due to Hurricanes Laura (LA-2020-03) and Delta (LA-2020-05) that began on August 22, 2020 and October 6, 2020 respectively.

The disaster areas for Laura include: Acadia, Acadia, Avoyelles, Beauregard, Bienville, Bienville, Caddo, Calcasieu, Caldwell, Cameron, Catahoula, Claiborne, DeSoto, Evangeline, Grant, Iberia, Jackson, Jackson, Jefferson Davis, Lafayette, La Salle, Lincoln, Lincoln, Morehouse, Natchitoches, Ouachita, Pointe Coupee, Rapides, Sabine, St. Landry, St. Martin, St. Mary, Union, Vermilion, Vernon, Webster, West Feliciana, and Winn.

Thus, taxpayers who live or have a business in the disaster area may qualify for tax relief.

Louisiana Filing Deadlines Extended

The IRS extended certain deadlines falling on or after August 22, 2020 and October 6, 2020 (Hurricanes Laura and Delta) to December 31, 2020 and February 16, 2021 respectively. The extension includes filing for most returns, including:

- individual, corporate, estate and trust income tax returns;
- partnership and S corporation income tax returns;
- estate, gift and generation-skipping transfer tax returns;
- the Form 5500 series returns, and
- employment and certain excise tax returns.

However, the extension does not include information returns in the Form W-2, 1098, or 1099 series or Forms 1042-S or 8027.

REFERENCE KEY

USTC references are to ***U.S. Tax Cases***
Dec references are to ***Tax Court Reports***

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Casualty Losses

Affected taxpayers can claim disaster-related casualty losses on their federal income tax return. Taxpayers may get relief sooner by claiming their losses on their 2019 or 2020 return. Individuals may deduct personal property losses not covered by insurance or other reimbursements.

Taxpayers claiming a disaster loss for Hurricane Laura on their 2019 or 2020 return should write the disaster designation:

"**Louisiana – Hurricane Laura**"

Taxpayers claiming a disaster loss for Hurricane Delta on their 2019 or 2020 return should write the disaster designation:

"**Louisiana – Hurricane Delta**"

at the top of the return. This will allow the IRS to speed refund processing.

Also, the IRS will provide affected taxpayers with copies of prior year returns without charge. To get this expedited service, taxpayers should:

- add the disaster designation at the top of Form 4506, Request for a Copy of Tax Return, or Form 4506-T, Request for Transcript of Tax Return, and
- submit it to the IRS.

First Quarter 2021 Interest Rates Remain Unchanged

The over and underpayment interest rates for the first quarter of 2021 remain unchanged. The first quarter begins on January 1, 2021. The rates will be:

- 3 percent for overpayments
- 2 percent for corporate overpayments
- 3 percent for underpayments, and
- 5 percent for large corporate underpayments.

The interest rate for the part of a corporate overpayment exceeding $10,000 is 0.5 percent.

Computation of First Quarter 2021 Interest Rates

The IRS computes these interest rates quarterly. The first quarter rates are based on the federal short-term rate for October 2020 which is 0 percent.

For noncorporate taxpayers:

- the overpayment rate is the short-term rate plus 3 percent, and
- the underpayment rate is the short-term rate plus 3 percent.

For corporate taxpayers:

- the underpayment rate is the short-term rate plus 3 percent.
- the overpayment rate is the federal short-term rate plus 2 percent.
- the rate on the part of a corporate overpayment that exceeds $10,000 for a tax period is the short-term rate plus 0.5.
- the underpayment rate for large corporations is 5 percent.

Rev. Rul. 2020-28; IR-2020-270

IRS Warns Taxpayers and Tax Professionals Against Scams and Identity Theft Schemes

IR-2020-265

This year marks the 5th Annual National Tax Security Awareness Week-a collaboration by the IRS, state tax agencies and the tax industry. The IRS and the Security Summit partners have issued warnings to all taxpayers and tax professionals to beware of scams and identity theft schemes by criminals taking advantage of the combination of holiday shopping, the approaching tax season and coronavirus concerns. The 5th Annual National Tax Security Awareness Week coincided with Cyber Monday, the traditional start of the online holiday shopping season.

The following are a few basic steps which taxpayers and tax professionals should remember during the holidays and as the 2021 tax season approaches:

- use an updated security software for computers and mobile phones;
- the purchased anti-virus software must have a feature to stop malware and a firewall that can prevent intrusions;
- don't open links or attachments on suspicious emails because this year, fraud scams related to COVID-19 and the Economic Impact Payment are common;
- use strong and unique passwords for online accounts;
- use multi-factor authentication whenever possible which prevents thieves from easily hacking accounts;
- shop at sites where the web address begins with "https" and look for the "padlock" icon in the browser window;
- don't shop on unsecured public Wi-Fi in places like a mall;
- secure home Wi-Fis with a password;
- back up files on computers and mobile phones; and
- consider creating a virtual private network to securely connect to your workplace if working from home.

In addition, taxpayers can check out security recommendations for their specific mobile phone by reviewing the Federal Communications Commission's Smartphone Security Checker. The Federal Bureau of Investigation has issued warnings about fraud and scams related to COVID-19 schemes, anti-body testing, healthcare fraud, cryptocurrency fraud and others. COVID-related fraud complaints can be filed at the National Center for Disaster Fraud. Moreover, the Federal Trade Commission also has issued alerts about fraudulent emails claiming to be from the Centers for Disease Control or the World Health Organization. Taxpayers can keep atop the latest scam information and report COVID-related scams at www.FTC.gov/coronavirus.

TAX BRIEFS

Consolidated Returns

A professional corporation qualified as a member of a parent group and was permitted to join in the filing of a consolidated federal income tax return with the parent group. The parent was the common parent of an affiliated group of corporations filing a consolidated federal income tax return (the parent group). The parent corporation never declared nor paid any dividends, nor made other distributions, to any shareholder.

IRS Letter Ruling 202049002

Corporations

The transfer of certain target assets of a subsidiary was treated as if the first subsidiary contributed the target assets of its branch to the other subsidiary. A common parent of an affiliated group of corporations undertook a transaction in order to transfer certain of the assets and liabilities of certain foreign branches of three entities. The transaction also involved restructuring of the transfer of a portion of the target assets of a disregarded entity to be treated as if a subsidiary contributed a portion of the target assets of the disregarded entity to the subsidiary.

IRS Letter Ruling 202048003

Nuclear Decommissioning Costs

A limited liability company's (LLC's) proposed schedule of ruling amounts was approved because it satisfied the requirements of Code Sec. 468A. The LLC was an investor-owned electric utility principally engaged in the generation, transmission, distribution and sale of electricity in two states. The LLC also operated a plant and the proposed revised schedule of ruling amounts was derived from the estimated base cost for decommissioning the plant contained in an independent study. Further, the LLC had a qualifying interest in the plant and was, therefore, an eligible taxpayer under Reg. §1.468A-1(b)(1). Moreover, the LLC, as an owner of the plant, had calculated its share of the total decommissioning costs under Reg. §1.468A-3(d)(3). The proposed schedule of ruling amounts was derived by following the assumptions contained in the independent study. Thus, the LLC had demonstrated, pursuant to Reg. §1.468A-3(a)(4), that the proposed schedule of ruling amounts was based on reasonable assumptions and was consistent with the principles of Code Sec. 468A.

IRS Letter Ruling 202048005

Partnerships

An entity organized as a limited liability company (LLC) and classified as a partnership was granted a 120-day extension to file a basis election under Code Sec. 754. A partner of the taxpayer held a partnership interest when he died. The taxpayer inadvertently failed to file a valid Code Sec. 754 election to adjust the basis of partnership property along with the return. The taxpayer acted reasonably and in good faith and, therefore, granting relief would not prejudice the government's interests.

IRS Letter Ruling 202049001

Private Foundations

A private foundation's procedures for awarding educational grants were approved. The organization operated a scholarship program to award scholarships annually to high school seniors in a specific region. Further, the awards were not taxable to the recipients if used for qualified tuition and related expenses subject to the limitations of Code Sec. 117(b). Finally, the scholarship grants were not taxable expenditures under Code Sec. 4945(d)(3).

IRS Letter Ruling 202049006

Railroad Retirement Rates

The IRS has released the tier 2 Railroad Retirement Tax Act (RRTA) tax rates for 2021 for railroad employees, employers and employee representatives, respectively. For 2021, the tier 2 tax rate on employees is 4.9 percent of compensation and the tier 2 tax rate on employers and employee representatives is 13.1 percent of compensation.

Publication of the Tier 2 Tax Rates

S Corporations

A limited liability company was granted a 120-day extension to elect to be an S corporation. The taxpayer's members relied on a tax adviser to file Form 2553, Election by a Small Business Corporation. However, the tax advisor inadvertently failed to file the form. The taxpayer established reasonable cause for its failure.

IRS Letter Ruling 202049003

Tax-Exempt Organizations

A Code Sec. 501(c)(3) organization's request for tax-exempt status was denied under Code Sec. 501(a). The organization's purpose was to inspire and benefit families with donations. The organization failed the operational test as it conducted substantial social and recreational activities as well as hall rental activities. Moreover, its activities were neither charitable nor educational in nature.

IRS Letter Ruling 202049005

The IRS approved a tax-exempt organization's set-aside and granted a 60-month extension to pay out the set-aside amount. The organization was exempt from federal income tax under Code Sec. 501(c)(3) and was classified as a private foundation under Code Sec. 509(a). The organization wished to set aside funds for an astronomical research project.

IRS Letter Ruling 202049004