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Supreme Court Holds Mandatory Repatriation Tax Constitutional

Moore et UX., SCt, 2024-1 USTC *¶50,163*

In a 7 to 2 decision, the U.S. Supreme Court held that the Mandatory Repatriation Tax or MRT under Code Sec. 965 was constitutional under Article I, §§8 and 9 and the Sixteenth Amendment of the Constitution. The MRT attributed undistributed income of American controlled foreign corporations (CFCs) to their American shareholders and then taxed the American shareholders on that income. The MRT operated in the same basic way as Congress's longstanding taxation of partnerships, S corporations and subpart F income, long upheld by the Court.

Background

The taxpayers invested $40,000 in a CFC that supplied modern tools to small farmers in India. The taxpayers never received a distribution from the investment or paid tax with respect to the CFC, until Code Sec. 965, the one-time mandatory repatriation tax or MRT, was enacted by the Tax Cuts and Jobs Act (P.L. 115-97)). The taxpayers were then required to pay tax on their share of the CFC's post-1986 accumulated earnings, as greater than 10 percent shareholders in the CFC. These earnings were deemed to be subpart F income. Prior to the enactment of the MRT, tax on these earnings would have been deferred until distribution.

The taxpayers challenged the constitutionality of the MRT. The taxpayers argued that the MRT was a direct tax that violated the Apportionment Clause of the Constitution because it had not been apportioned among the states based on population and that the tax was not an income tax exempt from apportionment under the Sixteenth Amendment. The taxpayers argued that a shareholder must directly receive or realize income from a corporation before it could be taxed, in reliance on *Eisner v. Macomber*, SCt, 1 USTC ¶32. The taxpayers also argued that the tax violated the Due Process Clause of the Fifth Amendment as a retroactive application of a new tax.

The district court rejected the taxpayers' claims and held that the MRT was a taxation of income under the Sixteenth Amendment and the Court of Appeals for the Ninth Circuit agreed. The Courts of Appeals held that although the term "income" was not defined in the Sixteenth Amendment, over the years similar taxes have been held constitutional. And, the tax, even if retroactive, did not violate due process because it served a legitimate purpose in accelerating the repatriation.

The taxpayer framed the issue in its Petition for Certiorari as "Whether the Sixteenth Amendment authorizes Congress to tax unrealized sums without apportionment." The government framed the issue in its response as "Whether the MRT is a tax[] on incomes, from whatever source derived," U.S. Const. Amend XVI, within the meaning of the Sixteenth Amendment." Certiorari was granted on June 26, 2023.

MRT is Constitutional

The Court rejected the taxpayers' argument that the MRT was a tax on property, rather than income, and was unconstitutional because it was not apportioned. Instead the Court found that the MRT does tax income realized by the corporation, which is then attributed and taxed to the shareholders.

The precise and narrow issue before the Court was whether Congress can attribute an entity's realized and undistributed income to the entity's shareholders or partners, and then tax the shareholders and partners on their portions of the income. The Court found that the Court's longstanding precedents, reflected in, and reinforced by Congress's longstanding practice established that the answer was yes.

The Court looked to a line of its cases involving partnerships and corporations (i.e., *Burk-Waggoner Oil Assn.*, SCt, 1 USTC ¶143; *Heiner v. Mellon*, SCt, 38-2 USTC ¶9311; and *Helvering v. National Grocery Company*, 338-2 USTC ¶9312) that held that Congress can choose to tax either a business entity or its partners or shareholders. By 1938, the cases established a clear rule that Congress could attribute the undistributed income of an entity to the entity's shareholders or partners, and tax the shareholders or partners on their pro rata share of the entity's undistributed income. Additionally, the same principle has been repeatedly invoked in upholding subpart F, which taxes shareholders of CFCs on undistributed corporate income.

The Court found the taxpayer's reliance on *Eisner v. Macomber*, SCt, 1 USTC ¶32 and the attribution issue to be misplaced. In that case, a corporation created and distributed additional stock to all of its shareholders in proportion to its percentage of ownership so the value of the shareholders' stock in the corporation did not change. The Court in *Eisner* stated that income requires realization and neither the corporation or shareholders realized income with respect to the additional stock. The Court in *Eisner*, however, did not address the attribution issue and so the decision had no bearing on the current case.

Additionally, the Court found that Congress has long taxed shareholders and partners of business entities on undistributed income, noting, for example, partnership taxation, personal service corporation taxation, S corporation taxation, and subpart F taxation.

The Court found that the taxpayers failed to meaningfully differentiate the MRT from taxes long imposed by Congress and long upheld by the Courts, such as taxes on partnerships, S corporations, and subpart F income. The Court stated that "The upshot is that the Moores' argument, taken to its logical conclusion, could render vast swaths of the Internal Revenue Code unconstitutional." And, elimination of the tax provision would deprive the U.S. government and American people of trillions in lost revenue. According to the Court, "The logical implications of the Moores' theory would therefore require Congress to either drastically cut critical national programs or significantly increase taxes on remaining sources available to it-including, of course, on ordinary Americans. The Constitution does not require that fiscal calamity."

Comment. According to an October 3, 2023, letter written by the Joint Committee on Taxation to Ranking Member of the House Ways and Means Committee, Richard E. Neal, a number of look-through realization provisions could have been challenged if the Supreme Court found looking through an entity to be impermissible including, Subpart F and GILTI, Subchapter K, Subchapter S, and REMICs. If the Supreme Court found deemed realization provisions impermissible, a number of provisions could have been challenged, including the OID rules and below-market and short-term loans,

Clean Hydrogen Credit Inflation Factors and Applicable Amounts for 2023 and 2024 Released

The IRS released the inflation adjustment factors and the resulting applicable amounts for the clean hydrogen production credit for 2023 and 2024.

For 2023, the inflation adjustment factor is one, so the inflation adjusted applicable amounts are the same as those in Code Sec. 45V(b). Thus, the applicable amounts for a kilogram (kg) of qualified clean hydrogen produced in calendar year 2023 are $0.120 for clean hydrogen produced through a process that results in a lifecycle greenhouse gas (GHG) emissions rate between 4 kilograms and 2.5 kg of CO2e per kg of clean hydrogen; $0.150 if the GHG rate is between 2.5 kg and 1.5 kg; $0.200 if the GHG rate is between 1.5 kg and 0.45 kg; and $0.60 if the GHG rate is less than 0.45 kg.

For 2024, the inflation adjustment factor is 1.0364. Thus, the inflation adjusted applicable amounts for a kilogram of qualified clean hydrogen produced in calendar year 2024 are $0.124 for clean hydrogen clean hydrogen produced through a process that results in a lifecycle greenhouse gas (GHG) emissions rate between 4 kilograms and 2.5 kilograms of CO2e per kilogram of clean hydrogen; $0.156 if the GHG rate is between 2.5 kg and 1.5 kg; $0.208 if the GHG rate is between 1.5 kg and 0.45 kg; and $0.622 if the GHG rate is less than 0.45 kg.

Notice 2024-45

REFERENCE KEY

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

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mark-to-market for securities dealers and regulated futures contracts, imputed rental income, Subchapter L mark-to-market, and the mark-to-market exit tax of Code Sec. 877A. After the issuance of today's decision Neal issued a statement which read: in part: "While I have disagreed with the Supreme Court on many issues in the recent past, today's opinion upholding the repatriation tax recognizes the gravity of this case and rightfully recognizes the flimsy arguments put forth by the taxpayers. In doing so, the Court ensured that our tax system would continue to function as it has for nearly a century while declining to give in to the chaos and confusion sowed by partisan advocacy groups, and wreaking havoc on our tax code… "

Narrow Opinion

The Court stated that its decision is narrow and applies when Congress treats an entity as a pass-through. Specifically it applies to the taxation of shareholders of an entity on the undistributed income realized by the entity that has been attributed to the shareholders when the entity itself has not been taxed on the income.

A dissent and opinion concurring in judgment primarily focused on the realization issue and whether realization is required for an income tax. The Court did not resolve the issue of whether realization is a Constitutional requirement in deciding the case.

Aff'g, CA-9, 2022-1 USTC ¶50,165

IRS Issues Nonconventional Source Fuel Reference Price for 2023

The IRS has published the reference price under Code Sec. 45K(d)(2)(C). The credit period for the nonconventional source production credit under Code Sec. 45K ended on December 31, 2013, for facilities producing coke or coke gas (other than from petroleum based products). However, the reference price continues to apply in determining the amount of the enhanced oil recovery credit under Code Sec. 43, the marginal well production credit for qualified crude oil production under Code Sec. 45I, and the percentage depletion in case of oil and natural gas produced from marginal properties under Code Sec. 613A. The reference price for calendar year 2023 is $76.10.

Notice 2024-51

Treasury, IRS Announce Tax Loophole and Abusive Partnership Transaction Enforcement Initiative

On June 17, 2024, the U.S. Department of the Treasury and the Internal Revenue Service announced a new regulatory initiative focused on closing tax loopholes and stopping abusive partnership transactions used by wealthy taxpayers to avoid paying taxes.

Specifically targeted by this new tax compliance effort are partnership basis shifting transactions. In these transactions, a single business that operates through many different legal entities (related parties) enters into a set of transactions that manipulate partnership tax rules to maximize tax deductions and minimize tax liability. These basis shifting transactions allow closely related parties to avoid taxes.

The use of these abusive transactions grew during a period of severe underfunding for the IRS, as the audit rates for these increasingly complex structures fell significantly. It is estimated that these abusive transactions, which cut across a wide variety of industries and individuals, could potentially cost taxpayers more than $50 billion over a 10-year period, according to an IRS News Release.

"Using Inflation Reduction Act funding, we are working to reverse more than a decade of declining audits among the highest income taxpayers, as well as complex partnerships and corporations," IRS Commissioner Danny Werfel said during a press call discussing the new effort on June 14, 2024.

"This announcement signals the IRS is accelerating our work in the partnership arena, which has been overlooked for more than a decade and allowed tax abuse to go on for far too long," said IRS Commissioner Danny Werfel. "We are building teams and adding expertise inside the agency so we can reverse long-term compliance declines that have allowed high-income taxpayers and corporations to hide behind complexity to avoid paying taxes. Billions are at stake here".

This multi-stage regulatory effort announced by the Treasury and IRS includes guidance (discussed in the story below) designed to stop the use of basis shifting transactions that use related-party partnerships to avoid taxes.

In the June 14, 2024, press call, Commissioner Danny Werfel also noted that there will be an increase in audits of large partnerships with average assets over $10 billion dollars and larger organizational changes taking place to support compliance efforts, including the creation of a new associate office that will focus exclusively on partnerships, S corporations, trusts, and estates.

Basis-Shifting Transaction Reporting Rules Proposed

Proposed Regulations, NPRM REG-124593-23; Notice 2024-54; Rev. Rul. 2024-14; IR-2024-166; FS-2024-21

The IRS and Treasury have issued proposed regulations that would require taxpayers and their material advisers to disclose their participation in partnership basis-shifting transactions that the IRS deems abusive and to pay penalties for failure to disclose.

Background

The proposed regulations are part of a new initiative by the IRS and Treasury to close what they consider a major loophole exploited by large, complex partnerships. The IRS describes the initiative as a multi-stage effort to prevent partnerships from using certain business structures to inflate their deductions through "partnership basis-shifting transactions." In these transactions, a single business operating through different legal entities ("related parties") enters into a set of transactions that manipulate the partnership tax rules to maximize deductions without any corresponding economic consequences to the participating businesses.

The proposed rules would add Reg. §1.6011-18 to identify certain partnership related-party basis adjustment transactions as transactions of interest for purposes of Code Sec. 6011. Current Reg. §1.6011-4(b), which requires taxpayers participating in reportable transactions to file disclosure statements, identifies "transactions of interest" as reportable transactions. IRS Form 8886, Reportable Transaction Disclosure Statement must be attached to the taxpayer's return for each tax year in which the taxpayer participates in a reportable transaction. Taxpayers failing to make the disclosures required by Reg. §1.6011-4 are subject to penalties under Code Sec. 6707A and possibly under Code Sec. 6662A.

Code Sec. 6111(a) requires "material advisers"—person who provide material aid, assistance, or advice with respect to organizing, managing, promoting, selling, implementing, insuring, or carrying out reportable transactions and deriving at least a certain amount of gross income (Reg. §301.6111-3(b)(3)—to file information returns (Form 8918) regarding any reportable transaction in which they are involved. Material advisers failing to file a disclosure, or filing an incomplete or false disclosure, are subject to penalties under Code Sec. 6707(a). They are also subject to penalties under Code Sec. 6708 for failing to furnish identifying lists under Code Sec. 6112(a) for reportable transactions.

The IRS and Treasury stated that they are aware of related persons using partnerships to engage in transactions that inappropriately exploit the basis-adjustment provisions of Code Secs. 732, 734, 743, and 754 to generate artificial basis adjustments.

In these transactions—i.e., "partnership related-party basis adjustment transactions"—partnership property is distributed to a partner related to at least one other partner, and the distribution results in an increase in basis of the distributed or remaining property under Code Sec. 732 or Code Sec. 734(b) to the distributee partner, the related partner, or both. Alternatively, a partnership interest is transferred between related persons or to a transferee partner related to an existing partner and the transfer results in an increase to the inside basis of partnership property under Code Sec. 743(b). In either situation, the basis increase is allocated to property eligible for cost recovery allowance or eligible for a shorter cost recovery period or to property that the partnership or the distributee partner disposes of in a taxable sale or exchange—resulting in decreased taxable income or gain, or increased loss, to the related group as a whole with little or no effect on overall economic ownership of the property.

The IRS explained that, to present the opportunity for a partnership related-party basis adjustment transaction, a related partner's partnership interest must have certain features: (1) a partner's outside basis in its partnership interest that is low compared to the partnership's basis in property it distributes to that partner; (2) a partner's outside basis in its partnership interest that is high compared to that partner's share of the partnership's basis in the partnership property (i.e., the partner's share of inside basis); or (3) a partner's outside basis in its partnership interest that is high compared to the partnership's basis in property it distributes to such partner in liquidation of the partner's interest. According to the IRS, partnerships with related parties can create these characteristics through orchestrated contributions and distributions, as well as through allocations under Code Sec. 704(b) and (c).

The IRS has identified four variations of partnership related-party basis adjustment transactions (discussed below) that it deems inappropriate and that the proposed regulations would target.

The Proposed Regulations

Proposed Reg. §1.6011-18(a) would identify "basis adjustment transactions" as Reg. §1.6011-4(b)(6) transactions of interest. The proposed rules would include a $5 million minimum threshold, would contain a relatedness requirement, and would define "related partners."

Basis Adjustment Transactions

A basis adjustment transaction under Proposed Reg. §1.6011-18(c)(1)(i) would occur when a partnership makes a current or liquidating distribution of property to a partner who is related to one or more partners, and the partnership increases the basis of one or more of its remaining properties under section 734(b) and (c).

A basis adjustment transaction under Proposed Reg. §1.6011-18(c)(1)(ii) would occur if: (1) a partnership distributes property to a partner related to one or more partners in liquidation of a partnership interest (or in complete liquidation of the partnership); and (2) the basis of one or more distributed properties is increased under Code Sec. 732(b) and (c).

A basis adjustment transaction under Proposed Reg. §1.6011-18(c)(1)(iii) would occur when a partnership distributes property to a partner who is related to one or more partners, the basis of one or more distributed properties is increased under Code Sec. 732(d), and the related partner acquired all or a part of its interest in the partnership in a transaction that would have been a transaction described in Proposed Reg. §1.6011-18(c)(2).

A basis adjustment transaction under Proposed Reg. §1.6011-18(c)(2) would occur when a partner transfers an interest in the partnership to a related transferee or to a person who is related to one or more existing partners in a nonrecognition transaction, and the basis of one or more partnership properties is increased under Code Sec. 743(b)(1) and (c). Proposed Reg. §1.6011-18(b)(2) would define "nonrecognition transaction" by reference to Code Sec. 7701(a)(45).

For purposes of the $5 million threshold, Proposed Reg. §1.6011-18(c)(3) would aggregate basis increases from multiple transactions by the same partner or partnership during the tax year.

The proposed regulations would require basis adjustments to recoverable property in basis adjustment transactions to be reported in the tax year of the transaction, in each tax year in which there is a cost recovery allowance, and in the tax year in which the recoverable property is disposed of in a taxable transaction. Basis adjustments to other property would need to be reported in the tax year of the basis adjustment transaction and the tax year in which the other property is disposed of in a taxable transaction.

Proposed Reg. §1.6011-18(a) and (d) would include as transactions of interest "substantially similar" transactions to those in Proposed Reg. 1.6011-18(c) but involving tax-indifferent parties rather than related partners. A tax-indifferent party would be defined as a tax-exempt or, in certain cases, foreign person.

Whether a taxpayer has participated in a transaction of interest (and is, thus, subject to the proposed rules) would be determined under Proposed Reg. §1.6011-18(e). Participants would include "participating partners" and "participating partnerships" (as defined), "related subsequent transferees" (as defined), and tax-indifferent parties.

Disclosure Requirements

Proposed Reg. §1.6011-18(f) would require participants to provide the information required under Reg. §1.6011-4(d) and the Instructions to Form 8886 (or its successor form). The proposed regulations would treat the following information as sufficient detail for information reporting purposes: (1) a description of an increase in basis resulting from a transaction described in Proposed Reg. §1.6011-18(c) that includes the information required in Proposed Reg. §1.6011-18(f)(1)(i) through (iii); (2) reporting of the names and identifying number of all participants, as required by Proposed Reg. §1.6011-18(f)(1)(i); (3) identifying all basis adjustments resulting from a Proposed Reg. §1.6011-18(c) transaction, as required by Proposed Reg. §1.6011-18(f)(1)(ii), the participating partnership's adjusted basis in the distributed property immediately before the distribution, any basis adjustments under Code Sec. 732(a)(2), (b), (d) or Code Sec. 734(b), any basis adjustments under Code Sec. 743(b) with respect to a participating partner that is transferred an interest in a participating partnership, and (with respect to a participating partner that transfers an interest in a participating partnership) the participating partner's adjusted basis in the participating partnership interest and share of the participating partnership's adjusted basis in its property immediately before the transfer; (4) providing information required by Proposed Reg. §1.6011-18(f)(1)(iii) regarding income tax consequences realized during the tax year as a result of a transaction described in Proposed Reg. §1.6011-18(c) (including cost recovery allowances attributable to a basis increase or taxable gain or loss attributable to the disposition of property that was subject to a basis increase); (5) providing information regarding cost recovery allowances and taxable gain or loss on dispositions, as required by Proposed Reg. §.6011-18(c); and (6) sending a copy of Form 8886 to OTSA regarding property subject to an increase in basis as a result of transaction in Proposed Reg. §1.6011-18(c) when property subject to a basis increase is disposed of in a subsequent tax year in a taxable transaction, as required by Proposed Reg. §1.6011-18(f)(2).

Penalties

Participants failing to disclose these transactions as required would be subject to penalties under Code Sec. 6707A, and material advisors failing to disclose these transactions would be subject to penalties under section 6707. Material advisors failing to maintain lists of investors as required by Code Sec. 6112 would be subject to penalties under Code Sec. 6708(a). In addition, the IRS could impose other penalties on persons involved in these transactions or substantially similar transactions, including Code Sec. 6662 or Code Sec. 6662A accuracy-related penalties, the Code Sec. 6700 penalty for promoting abusive tax shelters, and the Code Sec. 6701 penalty for aiding and abetting understatement of a tax liability.

Material advisors would also have disclosure requirements with regard to transactions in prior years. They would, however, be required to make the disclosures only if they made a tax statement on or after six years before the date of the Treasury decision adopting these regulations as final regulations is published in the Federal Register.

Related Notice of Intent and Revenue Ruling

In addition to these proposed regulations, the IRS's initiative launched on June 17, 2024, includes a notice of intent and a revenue ruling.

Notice 2024-54 states that the IRS intends to issue two additional sets of proposed regulations, one on the mechanics of partnership basis-shifting transactions and the other applying a single-entity approach to partnership interests held by consolidated-group members.

Revenue Ruling 2024-14 informs taxpayers that the IRS will challenge certain basis-shifting transactions for lack of economic substance.

Request for Comments

The IRS and Treasury request comments on all aspects of the proposed regulations.

A public hearing has been scheduled for September 17, 2024, beginning at 10 a.m. ET, in the Auditorium at the Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. 20224.

Applicability Date

Proposed Reg. §1.6011-18(a) would apply to identify certain partnership related-party basis adjustment transactions described in proposed Reg. §1.6011-18(c) and substantially similar transactions as transactions of interest effective as of the date of publication in the Federal Register of a Treasury decision adopting these proposed regulations as final.

IRS Tightens Scrutiny on Employee Retention Credit Claims

IR-2024-169

The IRS has announced plans to deny tens of thousands of high-risk Employee Retention Credit (ERC) claims while beginning to process lower-risk claims. The agency's review has identified a significant number of improper claims. "The completion of this review provided the IRS with new insight into risky ERC activity," IRS Commissioner Danny Werfel said. The Service aims to deny billions in improper claims and expedite payments for legitimate claims following an in-depth analysis that began last September.

The IRS's review has revealed that 10 to 20-percent of ERC claims fall into the highest-risk category, showing clear signs of being erroneous. These claims, submitted during aggressive marketing campaigns, will be denied in the coming weeks. Additionally, 60 to 70-percent of claims show an unacceptable level of risk and will undergo further analysis. For the 10 to 20-percent of claims deemed low-risk, processing will resume at a slower pace to ensure increased scrutiny and compliance. Initial payments from this group are expected later this summer.

In response to the findings, the IRS will continue its moratorium on new ERC claims submitted after September 14, 2023. This pause allows for further consultation with Congress and other stakeholders on the program's future. The IRS has also encouraged businesses with unprocessed claims to use the special ERC Withdrawal Program to avoid compliance issues. Compliance efforts around erroneous ERC claims have surpassed $2 billion, with ongoing audits and criminal investigations targeting fraudulent claims and promoters.

Final Regs and Related Guidance Govern Prevailing Wage and Apprenticeship Requirements for Increased Green Energy Credits and Deductions

T.D. 9998; IR-2024-168

The IRS released final regulations and related guidance regarding bonus credits and deductions for taxpayers that satisfy prevailing wage and apprenticeship (PWA) requirements. The regs apply to the following "green energy" tax provisions that were modified or enacted by the Inflation Reduction Act of 2022 (IRA, P.L. 117-169):

- the Code Sec. 30C alternative fuel refueling property credit,
- the Code Sec. 45 electricity production tax credit (PTC),
- the Code Sec. 45L new energy efficient home credit,
- the Code Sec. 45Q carbon sequestration credit,
- the Code Sec. 45U zero emission nuclear power production credit,
- the Code Sec. 45V clean hydrogen production credit,
- the Code Sec. 45Y clean electricity production credit,
- the Code Sec. 45Z clean fuel production credit,
- the Code Sec. 48C advanced energy project credit, and
- the Code Sec. 179D energy efficient commercial building production credit.

Bonus credits for satisfying the PWA requirements are also available under the Code Sec. 48 energy investment credit and the Code Sec. 48E clean electricity investment credit. The IRS intends to issue separate guidance to finalize the proposed regs for these two credits.

In addition to these finalized regs, the IRS also issued or updated the following related guidance:

- Publication 5983, IRA Prevailing Wage and Apprenticeship Requirements Fact Sheet.
- Publication 5855, IRA Prevailing Wage and Registered Apprenticeship Overview, and
- Prevailing wage and apprenticeship frequently asked questions (FAQs).

Applicability Dates and Effect on Other Documents

The final regs were to be published in the Federal Register on June 25, 2024. They generally apply to qualified facilities placed in service in tax years ending after the date they are published, if construction begins after that publication date. A taxpayer may also choose to apply them to other facilities, provided that the taxpayer follows them in their entirety and in a consistent manner.

Taxpayers may also rely on the Proposed Regulations that were issued in NPRM REG-100908-23 on August 30, 2023, with respect to construction of a qualified facility beginning on or after January 29, 2023, and on or before the date the final regs are published, provided that beginning after October 28, 2023, taxpayers follow the Proposed Regulations in their entirety and in a consistent manner.

Sections 3 and 4 of Notice 2022-61, I.R.B. 2022-52, 560, are obsoleted for facilities, property, projects, or equipment the construction, or installation, of which begins after the date that is 60 days after the final regs are published.

Transition Rules

The final regs provide a transition rule under which any work performed before January 29, 2023, is not subject to the PWA requirements. This transition rule applies even if the particular statute does not include this beginning of construction (BOC) exception.

The final regs largely incorporate Davis-Bacon Act (DBA) standards for triggering the PWA requirements. Thus, taxpayers must comply with the PWA tests once a laborer or mechanic performs any work that is considered construction, alteration, or repair of the qualified facility. However, under a transition rule, the final regs waive penalties for taxpayers who relied on the BOC rules for determining when the obligation to pay prevailing wages began, provided the taxpayer makes the appropriate correction payments to the impacted workers within 180 days of the publication of the final regulations. These BOC rules generally rely on the Physical Work Test, the Five Percent Safe Harbor, and the Continuity Requirement to establish when construction begins.

Indian Tribal Governments

The final regs provide two special rules that apply to Indian Tribal governments, including their subdivisions, agencies and instrumentalities. First, an Indian Tribal government is excepted from the Prevailing Wage Requirements with respect to laborers and mechanics that are its own employees, including those the Tribal government employs in joint ownership arrangements. This exception is consistent with the force account exception to the DBA.

Under the second special rule, if Indian land encompasses or overlaps more than one geographic area with respect to which the DOL has made an applicable wage determination, then the Indian Tribal government may choose the applicable wage determination for any one of those geographical areas and apply that applicable wage determination for work performed on any qualified facility that is located on the Indian land. This rule also applies to a qualified facility that is subject to joint ownership arrangements that involve an Indian Tribal government.

Project Labor Agreements

Under the final regulations, qualifying project labor agreements (PLAs) must include provisions requiring the payment of wages at rates that are not less than the prevailing rates, include contract provisions complying with the Apprenticeship Requirements, and establish mechanisms for workers, labor organizations, and taxpayers to correct any underpayments.

The IRS declined to treat a PLA as establishing deemed compliance or a rebuttable presumption of compliance with the PWA requirements. However, the final regs provide that penalties do not apply if a taxpayer uses a qualifying PLA and makes the required correction payments before filing a return claiming the credit. On examination, the IRS will also take into account whether a taxpayer has a qualifying PLA in place, and consider books and records substantiating compliance with a qualifying PLA as an indication of compliance with the PWA requirements.

Scope of PWA Requirements

The IRS recognizes that only a portion of a construction project may be used to produce energy covered by the tax credits. Under the general rule in the final regs, the PWA requirements apply to the portion of the activity that is creditable or deductible under the applicable Code section.

The final regs also continue to use the DBA concept of site of the work with respect to secondary sites. However, they clarify that the site of the work concept is intended to prevent the extension of the PWA requirements to all work on a facility, wherever performed and however small. Thus, unrelated third-party manufacturers who produce materials, supplies, equipment, and prefabricated components for multiple customers or the general public are not subject to the PWA requirements.

Determining Prevailing Wage Rate

The final regs largely adopt the proposed regs' incorporation of standards from the Davis-Bacon Act for satisfying the prevailing wage requirement. However, they provide additional factors for demonstrating intentional disregard of those rules.

The final regs determine the applicable prevailing wage at the time the contract for the construction, alteration, or repair of the facility is executed by the taxpayer and a contractor. These prevailing wage rates also apply to the contractor's subcontractors. In the absence of a contract, or if a contractor or subcontractor cannot determine a contract's execution date, the applicable wage determinations are those in effect at the time construction starts. These rules apply to each contract, so more than one wage determination to apply with respect to the construction, alteration, or repair of a facility.

A new general wage determination must be used when a contract is changed to include additional, substantial construction, alteration, or repair work, but not when a contractor is given more time to complete its original commitment or perform additional work that is merely incidental. However, if a taxpayer enters into a contract for alteration or repair work over an indefinite period of time that is not tied to the completion of any specific work, the applicable wage rates must be updated on an annual basis.

The final regs adopt the proposed regs regarding general and supplemental prevailing wage rates, but adjust some of the deadlines for incorporating supplemental wage determinations and requesting rates for additional classifications.

Definitions

The final regs generally align the relevant definitions for the Prevailing Wage Requirements with those for the Apprenticeship Requirements, and more clearly distinguish alteration and repair work from maintenance work in line with Department of Labor standards.

Correction and Penalty Procedures

The final regs largely adopt the proposed regs regarding the correction of PWA failures, the penalties for noncompliance, and the increased correction and penalty payments for intentional disregard of the requirements. These regs generally encourage the taxpayer to make correction payments sooner by waiving the penalty payment requirement if the taxpayer makes the required correction payment in a timely manner and meets additional requirements.

The final regs clarify the requirements for the poster or notice that employers must provide to employees regarding the prevailing wage requirements. The regs identify additional factors that indicate intentional disregard of the prevailing wage requirements, including the knowing use of contractors that are debarred from publicly funded projects for violating prevailing wage requirements is added as a factor indicating intentional disregard.

The final regs require corrections to be made by the last day of the first month following the end of the calendar quarter in which the failure occurred. They also modify the proposed waiver provision, in part by increasing the maximum underpayment amount to up to five percent of all amounts required to be paid in the calendar year.

Apprenticeship Requirements

The final regs confirm that the Apprenticeship Requirements apply only to the construction of the qualified facility including alteration and repair work that is performed before the facility is placed in service, but not to alteration or repair work occurring after that time. taxpayers, contractors, and subcontractors have the flexibility to create their own registered apprenticeship programs or partner with existing registered apprenticeship programs.

The final regs clarify that the Labor Hours Requirement applies to the construction of a facility, not on a contractor-by-contractor or trade-by-trade basis. The taxpayer determines if the requirement is satisfied by aggregating all labor hours for laborers and mechanics on the construction of the facility. Training hours of qualified apprentices at the location of the facility that involve construction, alteration, or repair work count towards the Labor Hours Requirement, but on-the-job training hours at other locations do not. There is no minimum amount of time that a qualified apprentice must be registered or employed in order to count the qualified apprentice's work towards the requirement. Labor hours performed by qualified apprentices in excess of the apprentice-to-journeyworker ratio count towards the total labor hours, but they will not count as apprentice hours for calculating the applicable percentage.

The Participation Requirement applies if the taxpayer, contractor, or subcontractor employs four individuals in the construction of the qualified facility at any time during the construction, regardless of whether they are employed at the same location or at the same time.

With respect to the good faith effort exception to the apprentice requirements, the final regs clarify and modify the required request for apprentices, as well as what constitutes a response. The duration of a request is extended to 365 days (366 days in a leap year). A taxpayer cannot satisfy the Good Faith Effort Exception through a denial from a registered apprenticeship program it sponsors.

PWA Requirements for Particular Code Sections

The final regs also make some minor modifications to the proposed regs for various Code Sections.

Guidance Provided on Early Retirement Distributions for Emergencies and Domestic Abuse Victims

Notice 2024-55; IR-2024-170

The IRS has provided guidance on two exceptions to the 10 percent additional tax under Code Sec. 72(t)(1) for emergency personal expense distributions and domestic abuse victim distributions. These exceptions were added by the SECURE 2.0 Act of 2022, P.L. 117-328, and became effective January 1, 2024. The Treasury Department and the IRS anticipate issuing regulations under Code Sec. 72(t) and request comments to be submitted on or before October 7, 2024.

Distributions for Emergency Personal Expenses

Code Sec. 72(t)(2)(I) provides an exception to the 10 percent additional tax for a distribution from an applicable eligible retirement plan to an individual for emergency personal expenses. The term "emergency personal expense distribution" means any distribution made from an applicable eligible retirement plan to an individual for purposes of meeting unforeseeable or immediate financial needs relating to necessary personal or family emergency expenses. The IRS specifically noted that emergency expenses could be related to: medical care; accident or loss of property due to casualty; imminent foreclosure or eviction from a primary residence; the need to pay for burial or funeral expenses; auto repairs; or any other necessary emergency personal expenses.

A plan administrator or IRA custodian may rely on a written certification from the employee or IRA owner that they are eligible for an emergency personal expense distribution. Furthermore, the guidance provides that an emergency personal expense distribution is not treated as a rollover distribution and thus is not subject to mandatory 20% withholding. However, the distribution is subject to withholding. If the emergency personal expense distribution is repaid, it is treated as if the individual received the distribution and transferred it to an eligible retirement plan within 60 days of distribution.

If an otherwise eligible retirement plan does *not* offer emergency personal expense distributions, an individual may still take an otherwise permissible distribution and treat it as such on the taxpayer's federal income tax return. The individual claims on Form 5329 that the distribution is an emergency personal expense distribution, in accordance with the form's instructions. The individual has the option to repay the distribution to an IRA within 3 years.

Distributions to Domestic Abuse Victims

Code Sec. 72(t)(2)(K) provides an exception to the 10 percent additional tax for an eligible distribution to a domestic abuse victim (domestic abuse victim distribution). The guidance defines a "domestic abuse victim distribution" as any distribution from an applicable eligible retirement plan to a domestic abuse victim if made during the 1-year period beginning on any date on which the individual is a victim of domestic abuse by a spouse or domestic partner. "Domestic abuse" is defined as physical, psychological, sexual, emotional, or economic abuse, including efforts to control, isolate, humiliate, or intimidate the victim, or to undermine the victim's ability to reason independently, including by means of abuse of the victim's child or another family member living in the household.

As with distributions for emergency personal expenses, a retirement plan may rely on an employee's written certification that the employee qualifies for a domestic abuse victim distribution. Similarly, if an otherwise eligible retirement plan does *not* offer domestic abuse victim distributions, the IRS indicated that an individual may still take an otherwise permissible distribution and treat it as such on the taxpayer's federal income tax return. The individual claims on Form 5329 that the distribution is a domestic abuse victim distribution, in accordance with the form's instructions. The individual has the option to repay the distribution to an IRA within 3 years.

Request for Comments

The Treasury Department and the IRS invite comments on the guidance, and specifically on whether the Secretary should adopt regulations providing exceptions to the rule that a plan administrator may rely on an employee's certification relating to emergency personal expense distributions and procedures to address cases of employee misrepresentation. Comments should be submitted in writing on or before October 7, 2024, and should include a reference to Notice 2024-55.

United States-Russia Tax Treaty To Be Suspended

Announcement 2024-26

The United States has provided formal notice to the Russian Federation on June 17, 2024, to confirm the suspension of the operation of paragraph 4 of Article 1 and Articles 5-21 and 23 of the Convention between the United States of America and the Russian Federation for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital, signed at Washington on June 17, 1992 (Convention), as well as the operation of its accompanying Protocol, by mutual agreement.

The suspension will take effect both for taxes withheld at source and in respect of other taxes on August 16, 2024, and will continue until otherwise decided by the two governments.

Oregon Joins Direct File Program

Oregon has become the first new state to join the Direct File program after the Internal Revenue Service announced earlier this year that it will remain a permanent option for taxpayers to file qualifying returns beginning with the 2025 tax filing season.

"Oregonians will be able to use Direct File to file their federal returns directly with the IRS for free and then use Oregon's state tax filing tool to quickly and easily file their state returns for free," Department of the Treasury Secretary Janet Yellen said during a June 18, 2024, press teleconference.

Oregon will be joining the 12 pilot states, all of which are expected to continue to offer Direct File to their respective citizens for the 2025 filing season.

Senate Finance Committee Chairman Ron Wyden (D-Ore.) noted during the teleconference that it is important to have options and pointed to an error in the 2024 tax filing season made by the Intuit software program Turbo Tax caused "a whole lot of Oregonians" to overpay their state taxes.

"We had to put together intense public pressure to get … Intuit to commit to fixing their mistake," Sen. Wyden said.

The IRS announced that it would expand the program earlier this year after what it described as a successful pilot campaign under which residents from 12 states used Direct File to file more than 140,000 tax returns.

For the pilot, only very simple tax returns qualified for Direct File. The agency is planning on expanding the types of returns that can be filed using Direct File, but it has not offered any timeline on when it might announce that kind of expansion.

Current Plan Liability Rates Set for June 2024

Notice 2024-53

For pension plan years beginning in June 2024, the IRS has released:

- the 30-year Treasury bond weighted average interest rate,
- the unadjusted segment rates,
- the unadjusted segment rates, and
- the minimum present value segment rates.

Corporate Bond Rate

The three 24-month average corporate bond segment rates applicable for June 2024 (without adjustment for the 25-year average segment rate limits are as follows):

- 4.93 for the first segment rate,
- 5.27 for the second and
- 5.26 for the third.

June 2024 Adjustment Segment Rate

The June 2024 adjusted segment rates for plan years beginning in 2023 are:

- 4.93 for the first segment rate,
- 5.27 for the second and
- 5.74 for the third.

The rates for plan years beginning in 2024 are:

- 4.93 for the first segment rate,
- 5.27 for the second, and
- 5.59 for the third.

AFRs Issued for July 2024

Rev. Rul. 2024-13

The IRS has released the short-term, mid-term, and long-term applicable interest rates for July 2024.

Applicable Federal Rates (AFR) for July 2024

Short-Term	Annual	Semiannual	Quarterly	Monthly
AFR	5.06%	5.00%	4.97%	4.95%
110% AFR	5.58%	5.50%	5.46%	5.44%
120% AFR	6.09%	6.00%	5.96%	5.93%
130% AFR	6.61%	6.50%	6.45%	6.41%
Mid-Term				
AFR	4.49%	4.44%	4.42%	4.40%
110% AFR	4.94%	4.88%	4.85%	4.83%
120% AFR	5.40%	5.33%	5.29%	5.27%
130% AFR	5.85%	5.77%	5.73%	5.70%
150% AFR	6.77%	6.66%	6.61%	6.57%
175% AFR	7.92%	7.77%	7.70%	7.65%
Long-Term				
AFR	4.61%	4.56%	4.53%	4.52%
110% AFR	5.08%	5.02%	4.99%	4.97%
120% AFR	5.54%	5.47%	5.43%	5.41%
130% AFR	6.02%	5.93%	5.89%	5.86%

Adjusted AFRs for July 2024

	Annual	Semiannual	Quarterly	Monthly
Short-term adjusted AFR	3.84%	3.80%	3.78%	3.77%
Mid-term adjusted AFR	3.40%	3.37%	3.36%	3.35%
Long-term adjusted AFR	3.49%	3.46%	3.45%	3.44%

The Code Sec. 382 adjusted federal long-term rate is 3.49%; the long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months) is 3.62%; the Code Sec. 42(b)(1) appropriate percentages for the 70% and 30% present value low-income housing credit are 8.06% and 3.45%, respectively, however, under Code Sec. 42(b)(2), the appropriate percentage for non-federally subsidized new buildings placed in service after July 30, 2008, shall not be less than 9%; and the Code Sec. 7520 AFR for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest is 5.4%.

30-Year Treasury Weighted Average

For plan years beginning in June 2024, the 30-year Treasury weighted average securities rate is 3.46, with a permissible range of 3.11 to 3.63 under Code Sec. 431(c)(6)(E)(ii)(l).

The rate of interest on 30-year Treasury securities for May 2024 is 4.62 percent.

The minimum present value segment rates under Code Sec. 417(e)(3)(D) for May 2024 are:

- 5.18 for the first segment rate,
- 5.41 for the second, and
- 5.62 for the third

Washington Round-up

NTA highlights common pitfalls for taxpayers claiming an electric vehicle credit. National Taxpayer Advocate Erin Collins in a June 20, 2024, blog post highlighted some issues that could hamper a taxpayer's ability to capture the electric vehicle tax credit. One "stumbling block" is the modified adjusted gross income qualification ceiling. "Taxpayers whose MAGI was too high for the previous year might estimate their MAGI for the current tax year to fall within the eligible range when purchasing an EV only to finds that it exceeds the threshold by the end of the year," Collins wrote. "This miscalculation can lead to the IRS recapturing the credit, resulting in an unexpected tax bill." Collins also reminded EV buyers to make certain they don't leave the dealership without the Clean Vehicle Seller Report (IRS Form 15400) to make sure the EV qualifies for the credit. She also reminded taxpayers to make sure the vehicle identification number matches IRS records on what cars qualify for the EV credit.

ABA comments on proposed regs for the excise tax on stock repurchases. The American Bar Association in a June 11, 2024, letter to the Internal Revenue Service offered additional comments on proposed regulations covering the excise tax on stock repurchases. The comments cover a few areas, including acquisitive reorganizations, upstream reorganizations, tracing of target-sourced cash in taxable acquisitions, constructive specified affiliate acquisitions, list of economically similar transactions, non-stock instruments, transition relief for redeemable stock issued prior to the excise tax, and modification of the funding rule.

AICPA comments on Form 4797. The American Institute of CPAs in a June 13, 2024, letter made a pair of recommendations to the Internal Revenue Service on updates to Form 4797, Sales of Business Property, specifically in relation to digital assets. The recommendations including providing more detail in the instructions for line 10 about what constitutes a "qualifying abandonment," and indicating that a loss from abandonment or worthlessness of a digital asset are not usable if generated in 2018 through 2025. AICPA's 2024 tax policy and advocacy comment letters can be found at https://us.aicpa.org/advocacy/tax/2024taxadvocacycommentletters.html?.

TAX BRIEFS

Credit for Increasing Research Activities

The IRS has unveiled a revised draft of Form 6765, Credit for Increasing Research Activities, incorporating suggestions from various external stakeholders. Key changes include making Section G optional for certain taxpayers and reduced scope of business component detail. The revised Section G will be optional for all filers for the tax year 2024 and mandatory starting in the tax year 2025. Instructions for the updated form will be released later.

IR-2024-171

Jury Instructions

A district court erred by incompletely and incorrectly delineating allowable "impediments." A jury awarded the taxpayer (limited partnership) (P1) a refund of its payment of an IRS-imposed penalty for failure to file timely information returns. The challenged jury instruction could have affected the outcome of the case. Therefore, the court vacated the verdict and remanded for a new trial. The award to the taxpayer for attorney fees and costs was also vacated.

R S B C O, CA-5, 2024-1 USTC ¶50,160

2020 Recovery Rebate

A district court found that stimulus payments could not be made in connection with a tax year 2020 income tax return. Under the Consolidated Appropriations Act (CAA), no refund or credit was to be made after January 15, 2021, referencing Code Sec. 6428A(f)(3)(A)(i). And under the American Rescue Plan Act (ARPA), no refund or credit was to be made or allowed after December 31, 2021.

Walker, DC Ky., 2024-1 USTC ¶50,162

Superfund

The IRS has announced that the list of taxable substances regarding the Superfund tax on chemical substances is modified to include polyoxymethylene effective October 1, 2024. The tax rate is set at $3.65 per ton. The petitioner, an exporter of polyoxymethylene, submitted a petition to the IRS to add polyoxymethylene to the list of taxable substances.

Notice 2024-50