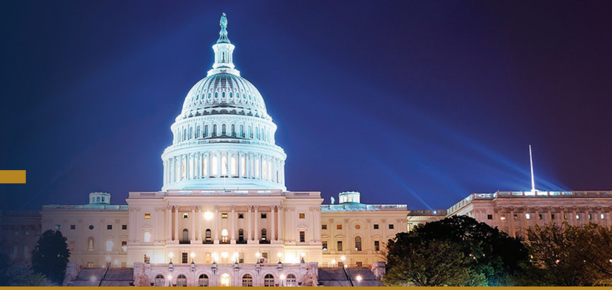
Washington TAX INSIGHT



July 2020

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Politics and Congressional Activity

Discussion of the next COVID-19 pandemic relief legislation continues to dominate discussion in Washington *despite the fact that many other important issues have yet to be addressed.* ***Funding for FY21 for the federal government*** *is being addressed in the House and Senate appropriations committees, but time is beginning to run short on the likelihood that Congress will meet the end of September deadline.*

Police reform legislation is being considered in the House and Senate, but it is unclear whether the two parties can resolve their differences. Major infrastructure legislation *has been introduced and passed the House on a mostly partisan vote of 223-188, and the White House is expected to weigh in on this subject with their own proposal.* ***House and Senate investigations*** *continue on a number of issues related to actions by the Administration.* ***The upcoming November elections*** *will put pressure on Congress to act on any key legislation before the August recess, as the attention of House members and Senators up for re-election will turn to their political races in the fall especially in light of the fact that this is a Presidential election year.*

With respect to appropriations legislation, which must be approved in both the House and Senate in order to provide funding for the federal government when FY21 begins on October 1st, the House Appropriations Committee has announced that the 12 subcommittees and the full committee will mark up bills the first two weeks in July and work to pass all the bills in the latter two weeks of July. The bills are likely to advance along party lines in the House, but there will be challenges in negotiations with the Senate, which needs bipartisan support to advance its spending bills. The Senate has not yet announced a timeline for its process. **Without agreement by the end of September, Congress will face the prospect of a federal government shutdown or the need to approve temporary funding extensions for any parts of the federal government not yet covered for FY21. Since this is an election year, any temporary funding bills could have expiration dates that fall after the November elections.**

House and Ways & Means Committee

On July 1st, the House approved the INVEST in America Act by a vote of 223-188, with the bill now going to the Senate, which is not expected to consider it in the near future. The bill is a $500 billion, five-year reauthorization of highway and mass transit spending, but it also includes spending for a number of other programs including affordable housing, broadband Internet access, wastewater infrastructure, and health care upgrades. The legislation includes nearly 70 tax provisions that, if enacted, would reduce federal revenues by nearly $350 billion over 10 years. Those provisions include: (1) Build America Bonds and Advance Refunding Bonds; (2) New Markets Tax Credit; (3) Rehabilitation Tax Credit; and (4) Low-Income Housing Tax Credit. There are no significant revenue offsets in the bill to cover the cost of the spending and tax incentives, which means that there would have to be a transfer from the general fund. The Administration is reportedly also drafting a major infrastructure bill that they are expected to send to Congress soon.

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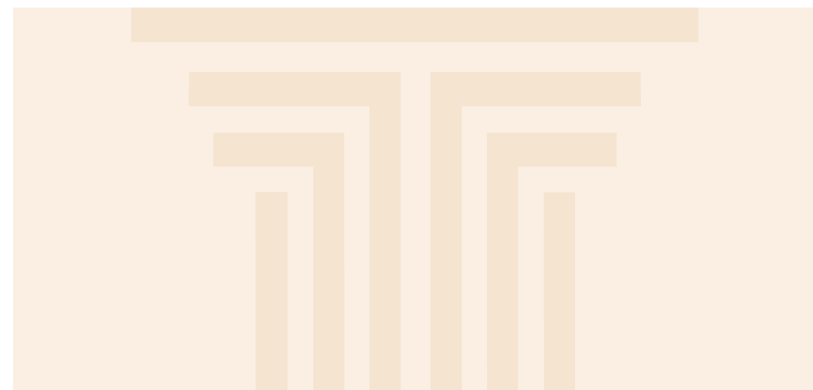

"In a reversal of their initial position, the Administration has agreed to make public the names and other information about businesses that receive more than $150,000 in loans from the Paycheck Protection Program."

Government Response to COVID-19, the Coronavirus Pandemic

In response to the COVID-19 pandemic, government officials in Washington DC have taken a number of actions related to the economic effects of the crisis including legislation, regulatory action, and government agency action.

As summarized in past True Alerts (Tax Issues Addressed by COVID-19 Emergency Legislation; Congressional Action on the COVID-19 Pandemic: The CARES Act), Congress has passed several major pieces of legislation to provide economic relief to the US economy and US taxpayers.

Discussions about a "Phase 4" pandemic relief bill continue, with recommendations from both parties in Congress and the White House being debated on a daily basis but without any real progress being made yet on defining the scope and cost of the next bill. As for a timeline on this legislation, **there will be some pressure in July for action,** as proposals such as the enhanced unemployment benefits expire at the end of July, and Congress will face its scheduled month long recess in August. **Agreement on the next bill, however, will be extremely challenging** as there are members of Congress who are concerned about another costly bill that will increase the federal deficit especially without the benefit of reviewing the impact of legislation already enacted.

In a reversal of their initial position, **the Administration has agreed to make public the names and other information about businesses that receive more than $150,000 in loans from the Paycheck Protection Program.** Information on borrowers of loans below $150,000 will be released in aggregated form. Some Democratic leaders in Congress have recommended that a second round of loans be approved as part of the next pandemic-related legislation.

Miscellaneous Issues

Altera Petition for Cert Denied by Supreme Court: The US Supreme Court refused to hear the Altera case that challenged transfer pricing regulations that require affiliated businesses to include stock-based compensation in their cost-sharing agreements for developing intangible property. A 2-1 Ninth Circuit panel upheld the Treasury rules in June of 2019, overturning a US Tax Court ruling for Altera. Altera argued that Treasury ignored public comments, pointing out that unrelated companies did not share stock-based compensation costs, thereby stating that the final rules fail under the standard for determining whether regulations were "arbitrary and capricious." Note that since the allegations in this case were first made, Treasury has generally included in regulatory guidance a careful analysis of comments from taxpayers and practitioners possibly in response to this argument.

Treasury and the IRS

Tax Cuts & Jobs Act (TCJA) Guidance

Business interest limits/163(j): Final and proposed regulations on the limitation on the deduction for business interest expense under §163(j) were submitted to the Office of Information and Regulatory Affairs (OIRA), which is part of the Office of Management and Budget (OMB), on June 15th for their second review. OIRA had completed its first review of this guidance early in 2020, but Treasury delayed the release of those regulations primarily due to the temporary changes that were enacted in the CARES Act to the TCJA changes to §163(j). The TCJA changes generally capped the deduction for business interest expense at the sum of (1) the taxpayer's business interest income; (2) 30 percent of the taxpayer's adjusted taxable income (ATI); and (3) the taxpayer's floor plan financing interest expense for the taxable year. The CARES Act relaxed that limitation by increasing the 30 percent of ATI threshold to 50 percent for taxable years beginning in 2019 and 2020 and allowing taxpayers to elect to use their 2019 ATI in 2020 (with special partnership rules applying).

GILTI/High Tax Exception/§954(b)(4): The final regulations on the global intangible low-taxed income (GILTI) high-tax exception and proposed rules under §954(b)(4) (addressing high-taxed subpart F income) and §964 (determining the earnings and profits of a foreign corporation) were submitted to OIRA for review. The GILTI rules, which were enacted as part of the TCJA's anti-base erosion regime, generally require a US shareholder of a controlled foreign corporation to include its GILTI in gross income. GILTI is determined based on complex calculations and deductions, and the TCJA provides that gross income excluded from foreign base company income or insurance income by reason of the high-tax exception under §954(b)(4) is not taken into account in calculating "tested income" for purposes of determining GILTI.

GILTI/FDII Regulations/§250: OIRA is reviewing **the final regulations under §250, related to deductions for Foreign-Derived Intangible Income (FDII) and GILTI,** which were enacted in the TCJA.

Treatment of Qualified Transportation Fringe Benefit Expenses/§274: The IRS issued **proposed regulations that provide guidance for the deduction of qualified transportation fringe and commuting expenses under §274.** The TCJA does not allow deductions for qualified transportation fringe (QTF) expenses and does not allow deductions for certain expenses of transportation and commuting between an employee's residence and place of employment.

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The law also provided that a tax-exempt organization's unrelated business taxable income is increased by the amount of the QTF expense that is nondeductible. However, on December 20, 2019, this was repealed as part of the Further Consolidated Appropriations Act of 2020. This repeal was retroactive to the original date of enactment by the TCJA. These proposed regulations specifically address the elimination of the deduction for expenses related to QTFs provided to an employee of the taxpayer. The proposed regulations also provide guidance and methodologies to determine the amount of QTF parking expense that is nondeductible.

QBI Deduction for RIC Shareholders/§199A: The IRS issued **final regulations permitting a regulated investment company (RIC) that receives qualified real estate investment trust (REIT) dividends to report dividends the RIC pays to its shareholders as §199A dividends.** §199A, which was enacted as part of the TCJA, allows individual taxpayers and certain trusts and estates to deduct up to 20 percent of certain income. The §199A deduction is available to eligible taxpayers with qualified business income (QBI) from qualified trades or businesses operated as sole proprietorships or through partnerships, S corporations, trusts, or estates, as well as for qualified REIT dividends and income from publicly traded partnerships. The regulations provide that a shareholder in a RIC may, subject to limitations, treat a §199A dividend received from a RIC as a qualified REIT dividend for purposes of determining the §199A deduction. The regulations also provide additional guidance on the treatment of previously disallowed losses that are included in QBI in subsequent years and provide guidance for taxpayers who hold interests in split-interest trusts or charitable remainder trusts.

Like Kind Exchanges/§1031: The IRS issued **proposed regulations that add a definition of real property to reflect changes in the TCJA that limit §1031 to exchanges of real property.** The guidance clarifies the definition of real property to distinguish it from personal property. Building off existing regulations, the rules define real property to include "land and improvements to land, unsevered crops and other natural products of land, and water and air space superjacent to land." Land improvements include "inherently permanent structures, and the structural components of inherently permanent structures." The guidance also covers personal property incidental to real property the taxpayer receives in an exchange.

Rehabilitation Tax Credit/§47: The IRS issued **proposed rules under §47 on the rehabilitation tax credit,** including instructions on coordinating the new 5-year period over which the credit may be claimed with other special rules for investment credit property. The guidance provides that the rehabilitation tax credit is properly determined in the year the qualified rehabilitated building (QRB) "is placed in service (consistent with prior law) but allocated ratably over the 5-year period as required by the TCJA, rather than resulting in the determination of five separate rehabilitation credits."

"The current tax filing deadline for individuals is July 15th, but recent comments from Treasury Secretary Mnuchin suggested that the idea of further deferring the filing and/or payment deadline is under consideration."

Carried Interest/§1061: OIRA is in the process of reviewing proposed regulations under §1061, related to the treatment of partnership interests held in connection with the performance of services. §1061 was enacted in the TCJA and provides that in order for partners holding carried interests to obtain long-term capital gain treatment, the person who disposed of the property must have held the property for more than three years.

Excise Tax on Tax-Exempt Executive Compensation/§4960: The IRS issued **proposed regulations on the excise tax on pay above $1 million and any excess parachute payments paid by certain tax-exempt organizations to covered employees** under §4960, which was enacted in the TCJA. The excise tax on remuneration is equal to the 21 percent corporate tax rate.

Withholding Rules for Certain Retirement and Annuity Payments/§3405: The IRS issued **proposed rules under §3405 for tax withholding on certain periodic retirement and annuity payments** to implement an amendment made by the TCJA. The rules would replace the reference to a married individual claiming three exemptions as the default withholding rate, providing instead that the withheld amount be determined by the IRS in the applicable forms, instructions, publications, and other guidance.

COVID-19 Crisis Guidance & Related Issues

Guidance on CARES Act Retirement Plan Provisions: The IRS issued **Notice 2020-50 providing further guidance related to the COVID-19 pandemic-related distribution (CRD) and loan provision**s in the CARES Act. As expected, this Notice uses some of the principles that were included in Notice 2005-92, which addressed similar provisions in the Katrina Emergency Tax Relief Act of 2005. There are some new elements to this guidance, however. It expands access to retirement savings under the CARES Act provisions by broadening the definition of "qualified individual" and provides a sample certification with respect to such status. It also provides guidance and a safe harbor for the administration of loan repayment suspensions. For nonqualified deferred compensation plans, it allows for the cancellation of deferral elections under §409A for recipients of CRDs.

Tax Filing Deadline for Individual Returns: The **current tax filing deadline for individuals is July 15th,** but recent comments from Treasury Secretary Mnuchin suggested that the idea of further deferring the filing and/or payment deadline is under consideration. There have

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been parties on both sides of the issue stating their positions publicly including those in favor of another deferral arguing that July would be a bad time to pull money out of the economy, while others suggest that another deferral is of limited use to taxpayers if states don't once again align with the deferral.

Net Operating Loss (NOL) Rules/§1502: OIRA is reviewing proposed regulations under §1502 addressing the calculation of net operating losses (NOLs) by consolidated groups. The TCJA generally eliminated the NOL carryback period but allows an indefinite NOL carryforward, subject to an 80 percent limitation, for NOLs arising in tax years ending after December 31, 2017. The CARES Act, however, modified these rules to allow taxpayers to carry back NOLs arising in 2018, 2019, and 2020 to the five prior years, and also allow NOLs incurred in these years to fully offset prior-year taxable income. OIRA's review of a separate set of regulations under §172 addressing the TCJA's changes to the NOL rules was completed in March of this year, but those regulations have not yet been published.

Guidance on Employer Leave Donations to Virus Charities: The IRS issued **Notice 2020-46, which instructs that employer cash payments to coronavirus relief charities in exchange for forgone employee leave (sick leave, vacation, or personal leave) will not be considered compensation.** Similarly, the employees will not be treated as receiving the value of the leave as income and cannot claim a deduction for the leave that they donated to their employer. Employers, however, may deduct these cash payments as a business expense or as a charitable contribution deduction if the employer otherwise meets the respective requirements of either section.

Relief for New Markets Tax Credit Investments/§45D: The **IRS issued Notice 2020-49,** which postpones to the end of 2020 the due dates for making investments and reinvestments, and spending on construction of real property for purposes of the **New Markets Tax Credit** under §45D. The IRS explains that the guidance provides community development entities (CDEs) and qualified active low-income community businesses (QALICBs) with relief for the following specified time-sensitive acts: (1) making investments; (2) reinvestments; and (3) expending amounts for construction of real property.

Other Issues and Guidance

Chief of the IRS Independent Office of Appeals Appointment: The IRS announced that **Andy Keyso** has been named **Chief of the IRS Independent Office of Appeals.** Mr. Keyso has been with the IRS for over 25 years, serving in a number of positions including IRS Chief of Staff, Associate Chief Counsel of the Income Tax and Accounting Division (Office of Chief Counsel), and Special Counsel to the Chief Counsel. IRS Appeals is a division within the IRS where taxpayers have the right to seek an independent review of their case after the examination is completed. It has been proven to be a successful process by which taxpayers and the IRS have avoided litigation of tax disputes in court.

2020-2021 Priority Guidance Plan: The IRS issued **Notice 2020-47, which solicits input for the 2020-2021 Priority Guidance Plan.** The annual plan lists the regulations, revenue rulings, revenue procedures, notices, and other published administrative guidance that the IRS intends to issue over the next 12 months. Recommendations are due by July 20th.

Quarterly Update to Priority Guidance Plan for 2019-2020: The IRS issued a **third-quarter update to its 2019-2020 Priority Guidance Plan,** which lists the regulations, revenue rulings, revenue procedures, notices, and other administrative guidance the agency expects to issue during its plan year. This update reflects 25 additional projects which have been published (or released) during the period from January 1, 2020 through March 31, 2020. The updated plan also includes the following additional project: "Regulations related to the foreign tax credit, including on the allocation and apportionment of interest expense, the definition of a foreign income tax, and the timing of when foreign taxes accrue and may be claimed as a credit."

Comments Sought on Proposed Reporting Methods for Partnerships/§704(b): The IRS issued **Notice 2020-43, which solicits input on requiring partnerships to use one of two proposed methods to satisfy tax capital reporting** for taxable years ending on or after December 31, 2020. If finalized, partnerships would no longer report partner capital accounts using any other method, including §704(b) and US generally accepted accounting principles (GAAP). The guidance proposes two alternative methods: Modified Outside Basis Method and Modified Previously Taxed Capital Method. Comments are due by August 4th.

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Proposed Rules on Carbon Capture Credits/§45Q: The IRS issued **proposed regulations implementing the credit for carbon sequestration** under §45Q, as modified by the Bipartisan Budget Act of 2018. The regulations provide guidance on two new credits for capturing carbon oxide with equipment placed in service on or after February 9, 2018, allowing up to $50 per metric ton of qualified carbon oxide for permanent sequestration, and up to $35 for Enhanced Oil Recovery purposes. Neither of these new credits is subject to a limitation on the number of metric tons of qualified carbon oxide captured. Additionally, the proposed regulations address issues for which taxpayers had questions, including: procedures to determine adequate security measures for the geological storage of qualified carbon oxide, exceptions to the general rule for determining who the credit is attributable to, procedures for a taxpayer to make an election

to allow third-party taxpayers to claim the credit, standards for measuring utilization of qualified carbon oxide, and rules for credit recapture. Earlier this year, the IRS issued other guidance regarding the definition of "beginning of construction" and providing a safe harbor for partnerships in Notice 2020-12 and Revenue Procedure 2020-12.

Rules on Deductibility of Payments for Medical Care Arrangements/§213: The IRS issued **proposed regulations on the tax treatment of amounts paid for certain medical care arrangements,** including direct primary care arrangements, health care sharing ministries, and government-sponsored health care programs. §213 of the Code allows individuals to take an itemized deduction for expenses for medical care, including insurance for medical care, to the extent the expenses exceed 7.5% of adjusted gross income. The proposed regulations respond to Executive Order 13877, which directs the Secretary of the Treasury, to the extent consistent with law, to "propose regulations to treat expenses related to certain types of arrangements, potentially including direct primary care arrangements and healthcare sharing ministries, as eligible medical expenses under Section 213(d)" of the Code.

2021 Inflation Adjustments for HSAs/§223: The IRS issued **Revenue Procedure 2020-32, which sets the inflation-adjusted contribution limits for Health Savings Accounts (HSAs) for 2021** under §223. The annual limitation on deductions for an individual with self-only coverage of $2800 for family coverage, and the annual out-of-pocket expenses (deductibles, co-payments, and other amounts, but not premiums) do not exceed $7,000 for self-only coverage or $14,000 for family coverage.

Reporting Relief for Certain Tax-Exempt Organizations/§6033: The IRS issued **final regulations under §6033 that update information reporting obligations for tax-exempt organizations** under §501(a). The rules reflect statutory changes and certain grants of reporting relief for tax-exempt organizations required to file Form 990 or Form 990-EZ information returns. Among other provisions, the final regulations incorporate the existing exception from having to file an annual return for certain organizations that normally have gross receipts of $50,000 or less. That exception was previously announced in Revenue Procedure 2011-15. The regulations also provide that the requirement to report contributor names and addresses on annual returns generally applies only to returns filed by §501(c)(3) organizations and §527 political organizations. All tax-exempt organizations must continue to maintain the names and addresses of their substantial contributors in their books and records.

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International Issues

OECD - Adoption of a Global Minimum Tax & Digital Taxation

Multilateral tax negotiations, which have been ongoing at the Organization for Economic Cooperation and Development (OECD) with the goal of producing a **global agreement on the taxation of multinational corporations, including those that provide digital services,** have been impacted by the COVID-19 pandemic. The 2020 timeline has been modified, but the deadline of producing an agreement continues to be the end of 2020.

New actions taken by the US Trade Representative with respect to unilateral digital services taxes (DSTs) that have been proposed or enacted by several countries have now raised additional questions about the ability of the OECD/G20 137-member Inclusive Framework to meet that deadline. At June 17th hearings before the House Ways & Means Committee and the Senate Finance Committee, USTR Robert Lighthizer confirmed reports that Treasury Secretary Mnuchin had informed several other negotiating partners that the **US was withdrawing from the OECD talks,** although there is some confusion about the US position on the talks proceeding. Although he suggested US support for a global negotiated agreement still exists, this action could now lead to a trade war as countries move ahead with unilateral DSTs, and the US responds with retaliatory tariffs.

Please see True Alert **(Will The US Withdrawal From the OECD Project on Digital Services Taxation Lead to a Trade War and a Missed Deadline?)** for a full discussion of this issue.

The **next full Inclusive Framework meeting, which was scheduled for July, has now been postponed to October** due to the COVID-19 pandemic. The Inclusive Framework's original schedule planned for virtual meetings to start the week of June 15th. **The delay has resulted in speculation that the OECD will not meet its deadline of reaching a global agreement by the end of the year, but the Inclusive Framework continues to have a stated goal of meeting that deadline.**

The goal of the next OECD meeting is for countries to sign off on a complete political agreement covering Pillar One, with that scheduled to happen just before the meeting of the G20 leaders in November. OECD Director of the Center for Tax Policy, Pascal **Saint-Amans, recently acknowledged that the project may now take longer than initially planned** and has stated that it may be a staged process with some decisions shifting into 2021.

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Challenges to the prospects for agreement by the end of 2020 within the Inclusive Framework on Pillar One and Pillar Two of the project are significant especially now with the US withdrawal from negotiations and the threat of a trade war over unilateral DSTs. The COVID-19 pandemic will continue to affect the practical logistics of negotiating and meeting to work through issues and technical details. The pandemic will also continue to demand the attention of government personnel trying to deal with the severe economic impacts of the crisis.

European Union

The **European Parliament has voted to set up a permanent subcommittee on tax matters,** which signals the intent to strengthen the legislature's role in tax policy. The economic and monetary affairs subcommittee, which will have 30 members from the Parliament, is assigned a mandate to deal with tax evasion and avoidance as well as questions of tax transparency.

EU Tax Commissioner Paulo Gentiloni has announced that his **upcoming tax action plan** will include proposals on administrative cooperation and environmental taxes, as well as work on an EU wide proposal on digital services taxation, should the OECD effort to reach a global agreement fail. The plan will also cover the issues of tax fraud and money laundering, which are two issues that will not require unanimity from all member states. In addition, the plan will focus on the review and improvement of the EU Code of Conduct rules and regulations that govern how the EU responds to countries that fail to align with EU tax standards.

The **European Council** has recommended that the EU finance ministers group move its deadline for **reviewing how tax havens are selected** from December 31, 2020, to mid-year 2021. In addition, talks on possibly expanding the EU's list of tax havens has been postponed until October at the earliest.

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