Congress Offers a Glimmer of Hope for Taxpayers with Section 965 Transition Tax Overpayment

Wednesday, December 19, 2018

Recently proposed legislation would provide taxpayers who made an election under Internal Revenue Code (Code) Section 965(h) to pay the transition tax over eight years through installment payments the ability to claim a refund or credit of any overpayment with respect to such amounts.

If enacted, taxpayers would be able to claim a refund or credit on an overpayment with respect to their first installment payment under Code Section 965(h).

On November 26, 2018, House Ways and Means Committee Chair Kevin Brady, R-Texas, introduced the Retirement, Savings and Other Tax Relief Act of 2018 and the Taxpayer First Act of 2018 (H.R. 88), which was subsequently revised on December 17, 2018 (the Bill). The Bill is a broad tax package that includes certain tax extenders, retirement savings proposals, Internal Revenue Service (IRS) improvement legislation and several technical corrections to the Tax Cuts and Jobs Act (P.L. 115-97).

Included in the Bill is a provision that, if enacted, would allow taxpayers to claim a credit or refund of any overpayment with respect to an installment payment of the taxpayer’s transition tax under Code Section 965. In particular, section 14103 of the Bill amends Code Section 965(h) by introducing new Code Sections 965(h)(7) and 965(h)(8), which provide that the IRS may credit or refund any “excess remittance” in the same manner as an overpayment of tax, but without interest. An “excess remittance” generally means a payment (including an estimated payment) that exceeds the sum of (1) a taxpayer’s US federal income tax liability without regard to Code Section 965 and without regard to any income or deduction attributable to any dividend received from a deferred foreign income corporation, plus (2) the sum of all installments with which the due date has passed.

In addition, the Bill explicitly provides that any overpayments of the transition tax payable in installments under Code Section 965(h) shall not be credited against the remaining unpaid installments (by providing that the first sentence of Code Section 6403 shall not apply).

If enacted, these amendments would be retroactive to the effective date of Code Section 965 (i.e., December 22, 2017), meaning that taxpayers that made an overpayment with respect to their first installment payment may be able to claim a refund on such overpayment, or apply the overpayment to their 2018 estimated tax payments.

The inclusion of this provision in the Bill is in response to PMTA 2018-016, which reaffirmed and provided a substantive analysis of the IRS’s position originally set forth in earlier 2017 Q&A guidance. This unpublished guidance espouses the view that taxpayers making a Code Section 965(h) election cannot use any overpayments of 2017 tax liabilities as a credit for 2018 estimated tax payments and such amounts cannot be refunded unless and until the overpayment amount exceeds the full eight years of installment payments. In recent 2018 Q&A guidance, the IRS reaffirmed their position in PMTA 2018-016 by extending this view to taxpayers that made a section 965(h) election for the 2018 tax year and that make an overpayment of their 2018 tax liability.

Having said that, the 2018 Q&A guidance offers some relief insofar as taxpayers that made a section 965(h) election for the 2017 tax year may claim a refund or credit with respect to any overpayment of their 2018 tax liability.

Although the House Rules Committee voted to send the Bill to the floor of the House of Representatives on November 28, 2018, the House has delayed a vote on the Bill due to former President George H.W. Bush's
passing on November 30, 2018. In addition, Senate Democrats have cast doubt on whether an agreement can be reached on the Bill, making both the timing and likelihood of the Bill being enacted into law unclear.

Practice Point: The introduction of the Bill signals belief, at least among some members of Congress, that the IRS’s position in the Q&A guidance and its legal interpretation in PMTA 2018-016 conflicts with Congress’s intent in allowing deferral of the payment of the transition tax. It remains to be seen whether the Bill will pass, or whether this particular provision will be enacted in subsequent legislation. We will continue to follow this development and provide updates in the future.

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