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Recent Developments in International Taxation

United States

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I. OVERVIEW

Given the political landscape in the United States, in which neither political party currently controls both chambers of Congress (the House of Representatives and the Senate) and the Presidency, there has been limited legislative activity in the area of international taxation. Notably, prior to the 2022 mid-term elections, the United States Congress passed the Inflation Reduction Act of 2022 ("IRA"), key provisions of which are outlined below. Despite the lull in legislative activity other than the IRA, there have been numerous federal court decisions of note, and the U.S. Department of the Treasury ("Treasury") and the Internal Revenue Service ("IRS") have issued regulations and guidance relevant to international taxation. Below is a high-level overview of selected U.S. developments relevant to international taxation for the period beginning January 1, 2022 and ending June 30, 2023.

II. THE INFLATION REDUCTION ACT OF 2022

The IRA was signed into law by President Biden on August 16, 2022. The IRA added $80 billion of funding to the IRS over the next ten years, mostly directed toward enforcement, and included various tax provisions, most notably: (a) a 15 percent corporate alternative minimum tax ("CAMT") on certain large corporations; (b) a 1 percent excise tax on stock buybacks; and (c) clean energy tax credits.

a. CAMT

The CAMT imposes a 15 percent tax on the adjusted financial statement income ("AFSI") of "applicable corporations," to the extent such tax would exceed CAMT foreign tax credits. The CAMT applies if it exceeds an applicable corporation's regular tax liability plus any base erosion and anti-abuse tax ("BEAT") liability. This provision is effective for tax years beginning after December 31, 2022.

AFSI means net income or loss reported on a corporation's applicable financial statement with adjustments for certain items. If a taxpayer's financial results are reported on the applicable financial statement for a group of entities, the CAMT provisions treat that consolidated financial statement as the corporation's applicable financial statement.

An "applicable corporation" is a corporation (other than an S corporation, regulation investment company or real estate investment trust) with average annual AFSI of more than $1 billion (without loss carryovers) for the three-year period before the relevant tax year. For purposes of the more-than-$1 billion threshold, AFSI of all persons treated as a "single employer" with the relevant corporation is aggregated, including all members of a controlled group of corporations with a 50 percent ownership overlap, by vote or value, and partnerships with common control (subject to specific rules).

A U.S. corporate member of a foreign-parented multinational group is an applicable corporation if it has average annual AFSI of $100 million or more (without loss carryovers) for the applicable three-year period and its foreign-parented multinational group exceeds the $1 billion three-year average income threshold, without making specific adjustments required under the AFSI rules.

Notably, once a corporation is an applicable corporation, it generally will continue to be an applicable corporation.

On December 27, 2022, Treasury and the IRS issued a notice providing interim guidance regarding the application of the CAMT. In light of the lack of more extensive guidance on the CAMT, the IRS on June 7, 2023, released a notice waiving penalties on the failure to pay 2023 estimated tax payments of CAMT.

b. Excise Tax on Stock Buybacks

With limited exceptions, the IRA imposes an excise tax equal to one percent of (1) the fair market value of any stock repurchased by a "covered corporation" or a "specified affiliate" from a person other than the covered corporation or a specified affiliate during the taxable year, less (2) the fair market value of any stock issued by the covered corporation (or certain affiliates) during the taxable year, including compensatory stock issuances. The tax also applies to certain acquisitions of stock of publicly traded foreign corporations by their domestic subsidiaries. This provision applies to repurchases made after December 31, 2022.

A "covered corporation" generally means a publicly traded domestic corporation. A "specified affiliate" is any corporation or partnership more than 50 percent owned, by vote or value, directly or indirectly, by the covered corporation.

On December 27, 2022, Treasury and the IRS issued a notice providing interim guidance regarding the application of the excise tax on repurchases of corporate stock.

c. Clean Energy Tax Credits

The IRA provided a historic investment in clean energy and contained a variety of new tax incentives, loans, and grants (and modifications to certain existing tax incentives) to improve energy efficiency and climate resiliency. Below is a list of certain key tax credit provisions:

- Production Tax Credit for Electricity from Renewables, a tax credit for production of electricity from renewable sources.
- Investment Tax Credit for Energy Property, a tax credit for investment in renewable energy projects.
- Clean Electricity Production Tax Credit, a technology-neutral tax credit for production of clean electricity.
- Clean Electricity Investment Tax Credit, a technology-neutral tax credit for investment in facilities that generate clean electricity.
- Advanced Manufacturing Production Credit, a production tax credit for domestic manufacturing of components for solar and wind energy, inverters, battery components, and critical minerals.

Of note, taxpayers can monetize certain of these clean energy credits, as the provisions allow taxpayers to sell credits or receive a refundable payment in lieu of the credit. On June 14, 2023, Treasury and the IRS issued proposed regulations for selling certain tax credits, and taxpayers are permitted to rely on such proposed regulations until final regulations are published. Treasury and the IRS also released a temporary regulation, effective June 21, 2023, outlining an IRS registration system that parties must satisfy before any valid sale of credits. At the same time, Treasury and the IRS issued proposed and temporary regulations addressing the refundability of certain credits.

III. SELECTED CASE LAW

a. Eaton Corp. and Subsidiaries v. Commissioner

In *Eaton Corp. and Subsidiaries v. Commissioner,* 47 F.4th 434 (6th Cir. 2022), *aff'g in part, rev'g in part*, T.C. Memo. 2017-147, the Sixth Circuit Court of Appeals addressed the IRS's cancellation of two advance pricing agreements ("APAs"). A few years after executing the APAs and submitting annual reports to the IRS, Eaton identified certain errors in its annual reports and informed the IRS. Although Eaton corrected its mistakes, the IRS (1) canceled the APAs, (2) issued a notice of deficiency, and (3) asserted penalties.

Eaton petitioned the Tax Court and challenged the IRS's notice of deficiency and cancellation of the APAs. Though siding with the IRS on the applicable standard of review – whether the IRS abused its discretion in canceling the APAs - Tax Court held that the IRS was wrong to cancel the APAs.

The IRS appealed the Tax Court's holdings on APA cancellation and the assertion of penalties, and Eaton cross-appealed to reassert its claim to apply Revenue Procedure 99-32 (IRS procedures for adjustments that may be made to conform taxpayers' accounts to reflect allocations made under section 482 of the Internal Revenue Code of 1986, as amended ("IRC")). The Sixth Circuit found in favor of Eaton on all three issues. Notably, the Sixth Circuit held that contract law principles apply in the case of an APA, thereby placing the burden of proof on the IRS.

b. Medtronic Inc. v. Commissioner

In *Medtronic Inc. v. Commissioner,* T.C. Memo. 2022-84 ("*Medtronic II")*, the Tax Court, on remand from the Eighth Circuit Court of Appeals, opined on whether the comparable uncontrolled transaction ("CUT") or another method is the best method for testing the licensing agreements between Medtronic US and Medtronic Puerto Rico ("MPROC"). In 2018, the appellate court vacated the Tax Court's 2016 opinion ("*Medtronic I"*) and remanded the case, asserting that the Tax Court failed to analyze sufficiently whether the purported CUT and the licensing agreements between Medtronic US and MPROC were comparable. In *Medtronic II,* the Tax Court held that, upon further analysis, the CUT it previously determined was the best method in *Medtronic I* was no longer the best method. As a result of *Medtronic II,* the Tax Court computed higher royalty rates, a determination in favor of the IRS.

The Tax Court held that the Pacesetter agreement proffered as a CUT by Medtronic was not comparable to Medtronic US's license to MPROC because too many adjustments to the Pacesetter agreement would be necessary. Nonetheless, it held that the Pacesetter agreement could still serve as a "starting point for determining a proper royalty rate." The Tax Court adopted a three-step approach to apply Medtronic's proposed "unspecified method": (1) it first applied a modified version of the CUT method and the 8 percent trademark license to allocate income to Medtronic US's R&D functions; (2) next the court allocated income to MPROC based on modifications to the IRS's comparable profits method to account for differences in asset intensity; (3) finally the court allocated the remaining income between Medtronic US and MPROC on an 80:20 basis.

c. 3M Co. and Subsidiaries v. Commissioner

In *3M Co. and Subsidiaries v. Commissioner*, 160 T.C. No. 3 (2023), the Tax Court held that a regulation regarding "blocked income" under IRC section 482, was valid based on IRC section 482's "commensurate

with income" language. The dispute arose from an IRS-initiated adjustment proposing income allocations from a Brazilian subsidiary to its U.S. shareholder for licensing intangible property. 3M argued that, while the adjustment was arm's length, it was not appropriate because Brazilian law prevented the subsidiary from paying the additional royalty and challenged the validity of section 1.482-1(h)(2) of the Treasury Regulations, which addresses foreign legal restrictions.

The Tax Court's plurality opinion set forth a detailed review of IRC section 482's legislative history, case law, and the Administrative Procedure Act. In evaluating whether Brazilian legal restrictions met the requirements in the regulation, the plurality opinion concluded that five of the seven requirements to take a foreign legal restriction into account were not met.

The opinion also rejected arguments by 3M based on relevant case law and distinguished other cases predating the statutory amendment that incorporated the commensurate with income principle.

d. FedEx Corp. v. United States

In *FedEx Corp. v. United States,* T.C.M P50, 153 (W.D. TN. 2023), the U.S. District Court for the Western District of Tennessee granted FedEx's motion for partial summary judgement on the treatment of foreign tax credits ("FTCs") related to the distribution of IRC section 965(b) previously taxed earnings.

IRC section 965 was enacted as part of the Tax Cuts and Jobs Act of 2017 ("TCJA") and imposed a one-time tax at reduced rates on the earnings and profits of controlled foreign corporations ("CFCs") for which U.S. taxation had been deferred under pre-TCJA rules. When calculating the amount taxable, taxpayers could offset the earnings of their profitable subsidiaries by the losses of loss-generating subsidiaries (referred to in the case as "offset earnings"), reducing the amount of earnings and profits subject to the transition tax.

At issue in *FedEx* was the validity of a regulation under IRC section 965 that precludes FTCs for foreign taxes considered paid on offset earnings. The court ruled that the regulation is contradicted by the unambiguous language of certain IRC sections in effect prior to the TCJA. Therefore, FedEx was deemed to have paid the foreign taxes on offset earnings when those earnings were distributed to the United States.

The ruling in *FedEx* could create refund opportunities for other taxpayers who previously repatriated offset earnings.

e. Bittner v. United States

In *Bittner v. United States,* 143 S. Ct. 713, 215 L. Ed. 2d 1 (2023), the Supreme Court, in a 5-4 opinion, resolved an appellate circuit split on computing nonwillful penalties for failure to file timely the Report of Foreign Bank and Financial Account ("FBAR").

Under the Bank Secrecy Act, U.S. persons must file an FBAR for each year in which the U.S. person possesses a financial interest in or signature authority over a foreign financial account if the aggregate value of all such foreign financial accounts exceeds $10,000 any time during the calendar year. Penalties for failing to timely file FBARs range from $10,000 for a nonwillful violation to the greater of 50 percent of the maximum account value or $100,000 for willful violations.

Taxpayers and the IRS have disagreed over the application of the $10,000 penalty for nonwillful violations of FBAR filing requirements, with the IRS favoring a per-account penalty and taxpayers arguing for a per-form penalty. The Supreme Court resolved this longstanding dispute, holding that the penalty for nonwillful violations should be computed on a per-form basis.

IV. SELECTED REGULATIONS

a. FTC Regulations

i. 2022 Final FTC Regulations

On December 28, 2021, Treasury and the IRS issued a tranche of final FTC regulations ("2022 Final FTC Regulations"), which were officially published in the Federal Register on January 4, 2022. The 2022 Final FTC Regulations are effective March 7, 2022, and generally apply to taxable years, or foreign income taxes paid or accrued in taxable years, beginning on or after December 28, 2021.

The 2022 Final FTC Regulations fundamentally change the rules for determining the creditability of a foreign tax under IRC sections 901 and 903. Most significantly, the 2022 Final FTC Regulations introduce an "attribution requirement", which aims to limit the scope of gross receipts and costs that are attributable to a taxpayer's activities. The attribution requirement generally does not consider foreign taxes creditable unless the relevant foreign tax law requires a sufficient connection between the foreign country and the taxpayer's activities or investments. This requirement is intended to be much more restrictive than the former regulations issued in 1983, which provided that a foreign levy would be creditable if it constituted a tax and had the predominant character of an income tax in the U.S. sense.

A foreign tax would satisfy the attribution requirement in one of three ways: (1) the tax is attributable, under reasonable principles, to the taxpayer's activities in the foreign country (the "activities-based requirement"); (2) the tax is based on income sourced to the country imposing the tax, provided the sourcing rules in the foreign country are reasonably similar to U.S. sourcing rules (the "source-based requirement"); or (3) the tax is based on income from the sale or disposition of certain real or movable property located in the country imposing the tax (the "property-based requirement").

In addition to the attribution requirement, the 2022 Final FTC Regulations address, among other things, the disallowance of an FTC or deduction for foreign income taxes on dividends eligible for a dividends-received deduction; the allocation and apportionment of interest expense, foreign income tax expense, and certain deductions of life insurance companies; the definition of a foreign income tax and a tax in lieu of an income tax; the definition of foreign branch category income; and the time when foreign taxes accrue and can be claimed as a credit. The 2022 Final FTC Regulations also include clarifying rules relating to the deduction for foreign-derived intangible income.

Taxpayers and tax practitioners have raised numerous concerns about various aspects of the 2022 Final FTC Regulations.

ii. 2022 Proposed FTC Regulations

On November 22, 2022, Treasury and the IRS issued proposed FTC regulations ("2022 Proposed FTC Regulations"), addressing the reattribution asset rule (providing that when income from a payor to a recipient is reattributed, there must also be a reattribution of the tax book value of the payor's assets

generating the reattributed income to the recipient's taxable assets) for purposes of allocating and apportioning foreign taxes, the cost recovery requirement, and the attribution rule for withholding tax on royalty payments. The 2022 Proposed FTC Regulations provide some relief for concerns sparked by the 2022 Final FTC regulations, though additional concerns have yet to be addressed. Taxpayers may rely on all or part of the 2022 Proposed FTC Regulations, subject to certain conditions, until the effective date of final regulations.

The 2022 Final FTC Regulations provided that foreign gross income from a disregarded payment that is a reattribution payment (i.e., a disregarded payment that is deductible under foreign law) is assigned to the same statutory and residual grouping as the U.S. gross income that is reattributed to the recipient taxable unit. The 2022 Proposed FTC Regulations exclude any portion of the tax book value of property transferred in a disregarded sale from being attributed back to the selling taxable unit.

Under the 2022 Final FTC Regulations, an FTC is a creditable net income tax only if the determination of the foreign tax base conforms in essential respects to the determination of taxable income under U.S. tax principles, which, in part, requires that the foreign tax satisfies the cost recovery requirement. To satisfy the cost recovery requirement, the gross receipts of a creditable foreign tax must be offset by the recovery of significant costs and expenses attributable to those receipts under reasonable principles, and taxpayers must establish that the reason a deduction is disallowed under a foreign tax is consistent with the principles underlying disallowances in the IRC. The 2022 Proposed FTC Regulations provide that the relevant foreign tax law need only permit recovery of substantially all of each item of significant cost or expense and offer a safe harbor for the application of the cost recovery requirement.

The 2022 Proposed FTC Regulations provide a single-country exception to the source-based attribution requirement for foreign tax imposed on royalties: a foreign tax qualifies for the single-country exception if the income subject to the foreign tax is characterized as gross royalty income and the payment giving rise to that income is made under a single-country license. The 2022 Proposed FTC Regulations also revise the separate levy rule for withholding tax imposed on royalty payments made to foreign persons: if the tax is imposed on a foreign person under a single-country license, it is treated as a levy separate from a withholding tax imposed on other royalty payments made to the foreign person.

b. Final Subpart F Regulations

On January 25, 2022, Treasury and the IRS released final regulations regarding the treatment of the ownership of CFCs, as defined in IRC section 957, by domestic partnerships and their partners ("2022 Subpart F Regulations"). The 2022 Subpart F Regulations finalize proposed regulations issued in 2019, which were issued at the same time as other CFC-related final regulations ("2019 GILTI Regulations"). The 2022 Subpart F Regulations are intended to achieve consistent treatment of U.S. partners of domestic partnerships for purposes of determining subpart F and global intangible low-taxed income ("GILTI") inclusions.

Prior to the 2022 Subpart F Regulations, a domestic partnership that was a "United States shareholder" as defined in IRC section 951(b) of a CFC computed its subpart F inclusion at the partnership or S corporation level, and its U.S. partners included in income their distributive share of the entity-level subpart F inclusion. Consistent with the approach taken in the 2019 GILTI Regulations, the 2022 Subpart F Regulations provide that a U.S. partner of a domestic partnership that owns stock in a CFC will have a subpart F income inclusion only if the partner is a U.S. Shareholder of the CFC within the meaning of IRC

section 951(b). Similar principles apply to shareholders of an S corporation that is a "United States shareholder" of a CFC.

c. Proposed Passive Foreign Investment Company ("PFIC") Regulations

Concurrently with the issuance of the 2022 Subpart F Regulations, on January 25, 2022, Treasury and the IRS released proposed regulations under the PFIC regime ("2022 PFIC Regulations"). If finalized, the 2022 PFIC Regulations would amend the PFIC rules to be consistent with the approach in the 2019 GILTI Regulations and the 2022 Subpart F Regulations to treat domestic partnerships as aggregates of their partners (and S corporations as aggregates of their shareholders) for purposes of determining income inclusions and making various elections under the PFIC rules.

Specifically, the proposed regulations address domestic partnerships and S corporations that own stock in a PFIC for which a "qualified electing fund" ("QEF") or "mark-to-market" ("MTM") election could be made. Under current regulations, only the domestic partnership or S corporation (and not their U.S. partners or shareholders) can make QEF or MTM elections. If finalized, the 2022 PFIC Regulations would reverse the current rule so that only the U.S. partners or S corporation shareholders could make those elections. The 2022 PFIC Regulations would generally apply prospectively for tax years beginning on or after the date final regulations are published.

d. Proposed Foreign Currency Options Regulations

IRC section 1256 generally requires that certain contracts, including "foreign currency contracts," be marked-to-market annually. On July 5, 2022, Treasury and the IRS released proposed regulations that provide that only a forward contract on foreign currency constitutes a "foreign currency contract" as defined in IRC section 1256(g)(2). The proposed regulations do not change the status of foreign currency options that otherwise qualify as IRC section 1256 contracts.

These rules are proposed to apply to contracts entered into on or after the date that is 30 days after the regulations are finalized. A taxpayer may rely on the proposed regulations, as long as the taxpayer and its related parties consistently follow the proposed regulations for all contracts entered into during the tax year ending on or after July 5, 2022, through the applicability date of the final regulations.

e. Proposed Regulations Regarding Consolidated Group Previously Tax Earnings and Profits ("PTEP")

On December 9, 2022, Treasury and the IRS released proposed regulations, which would provide that when stock of a lower-tier CFC is transferred within a consolidated group, the consolidated group members are treated as a single U.S. shareholder so that the member that owns the lower-tier CFC stock at the end of the year cannot reduce its subpart F or GILTI inclusion by reason of PTEP distributions by the lower-tier CFC before the transfer. According to the preamble to the proposed regulations, the goal is to eliminate an approach taken by some consolidated groups to minimize income inclusions under subpart F and GILTI. The proposed regulations would apply to taxable years for which the original consolidated income tax return is due (without extensions) after the date on which the regulations are finalized.

f. Foreign Investment in Real Property Tax Act of 1980 (“FIRPTA”) Regulations

IRC section 897, commonly referred to as “FIRPTA”, subjects foreign persons to U.S. federal income tax on gain realized upon a disposition of a “United States real property interest” (“USRPI”), as if such gain were income effectively connected with a U.S. trade or business. A USRPI includes real property located in the United States and equity interests in a domestic “United States real property holding corporation” (“USRPHC”), a corporation in which USRPIs make up 50 percent or more by value of the aggregate value of its USRPIs, foreign real property interests, and business assets.

On December 29, 2022, Treasury and the IRS published final regulations regarding the application of FIRPTA to qualified foreign pension funds (“QFPFs”), as well as proposed regulations regarding the application of FIRPTA in relation to foreign governments and domestically controlled qualified investment entities (“QIEs”).

i. Final Regulations for QFPFs

Treasury and the IRS published final regulations on the qualification for the FIRPTA exemption under IRC section 897(l) for QFPFs and their wholly owned subsidiaries. These regulations also address gain from distributions described in IRC section 897(h) and related withholding requirements under IRC sections 1445 and 1446. These regulations generally apply to dispositions of USRPIs and distributions described in IRC section 897(h) occurring on or after December 29, 2022, although certain provisions apply to distributions of USRPIs described in IRC section 897(h) occurring on or after June 6, 2019.

ii. Proposed Regulations Regarding Foreign Governments and Domestically Controlled QIEs

IRC section 892 generally exempts foreign governments from U.S. tax on certain income, except income that is derived from commercial activity, derived by or from a controlled commercial entity (“CCE”), or derived from the disposition of a CCE. Under current rules, a USRPHC is deemed engaged in commercial activity and, therefore, treated as a CCE if controlled by a foreign government—even if the entity’s USRPIs are minority investments. Helpfully, the proposed regulations would provide an exception to this “deemed CCE” treatment for QFPFs that meet the definition of a USRPHC. In another friendly change, the proposed regulations would provide an exception to the “deemed CCE” rule for any entity that is a USRPHC solely due to direct or indirect ownership interests in one or more corporations not controlled by the relevant foreign government.

Of particular note to taxpayers investing in real estate investment trusts (“REITs”), the proposed regulations would introduce a “look-through” approach for purposes of the determination of when a REIT is domestically controlled. Under FIRPTA, equity interests in domestically controlled REITs are not considered to be USRPIs. A REIT is “domestically controlled” if less than 50 percent of its stock is held “directly or indirectly” by foreign persons at all times during a testing period. Particularly controversial is a proposed rule that would require a REIT to look through a domestic C corporation if foreign persons own, directly or indirectly, 25% or more by value of the C corporation.

g. Proposed IRC Section 367(d) Regulations

On May 3, 2023, Treasury and the IRS released proposed regulations that would terminate the continued application of IRC section 367(d) when a transferee foreign corporation repatriates intangible property to

a "qualified domestic person" and certain reporting requirements are met. For purposes of this provision, "qualified domestic person" generally means the U.S. transferor of the property or a U.S. person that is a successor to, or related to, the U.S. transferor. These proposed regulations are intended to be effective for repatriations that occur after the date that the regulations are finalized.

V. SELECTED IRS GUIDANCE

a. Foreign-Derived Intangible Income ("FDII") Guidance on Deferred Compensation

On May 6, 2022, the IRS Office of Chief Counsel released a generic legal advice memorandum regarding the allocation and apportionment of deferred compensation expense ("DCE") for purposes of calculating the IRC section 250 deduction for FDII ("2022 FDII Guidance"). The 2022 FDII Guidance concluded that DCE that relates to services provided in years prior to the enactment of IRC section 250, but that is deductible post-enactment, may be allocated to deduction eligible income ("DEI") and foreign-derived deduction eligible income ("FDDEI") if the class of gross income to which the deduction relates includes DEI or FDDEI.

b. BEAT Notice

On June 27, 2022, the IRS released a notice announcing the IRS's intent to amend regulations under IRC sections 59A and 6038A to defer the applicability date of certain reporting rules for "qualified derivative payments" ("QDPs") until tax years beginning on or after January 1, 2025. A QDP is defined as any payment made by a taxpayer to a foreign related party pursuant to a derivative if: (i) the taxpayer recognizes gain or loss on the derivative on a mark-to-market basis, (ii) the gain or loss is ordinary, (iii) any gain, loss, income or deduction on a payment made pursuant to the derivative is also treated as ordinary, and (iv) the taxpayer satisfies specific reporting requirements.

c. IRC Section 367(d) Advance Payments Disallowed

Except as provided in relevant Treasury Regulations, if a U.S. person transfers any intangible property to a foreign corporation in an exchange described in IRC section 351 or 361, IRC section 367(d) applies to the transfer. Under IRC section 367(d), a U.S. transferor is treated as having sold the intangible property in exchange for payments that are contingent upon the productivity, use, or disposition of the intangible property, and the U.S. transferor is treated as receiving amounts that reasonably reflect the amounts that would have been received annually over the useful life of the intangible property. A U.S. transferor generally takes an annual IRC section 367(d) inclusion into account regardless of whether the payments are actually made by the transferee foreign corporation. On September 23, 2022, the IRS released a memorandum stating that taxpayers cannot choose to make advance payments of annual inclusions under IRC section 367(d) except in limited circumstances.

d. Active Trade or Business ("ATB") under IRC Section 367

Subject to certain exceptions, IRC section 367(a)(1) provides that if a U.S. person transfers property to a foreign corporation in an exchange described in IRC section 332, 351, 354, 356, or 361, the foreign corporation will not be considered a corporation for purposes of determining the extent to which the U.S. person recognizes gain on such transfer—treatment that generally eliminates nonrecognition treatment under the enumerated IRC sections. One exception to this general rule requires that, among other things, the transferee foreign corporation (or any qualified subsidiary or qualified partnership) must have been

engaged in an ATB outside the United States for the entire 36-month period immediately preceding the transfer. On November 4, 2022, the IRS released a memorandum stating that, barring exceptional circumstances, an entity cannot satisfy the ATB requirement in IRC section 367 if it does not generate income for the entire 36-month statutory period.

e. Sourcing of American Depository Receipts ("ADR") Program Payments

In generic legal advice issued on February 10, 2023, the IRS concluded that payments made by U.S. depository institutions, whether as expense reimbursement or revenue sharing, to foreign corporations for the rights to sponsored ADR program issuances are treated as U.S.-source income and subject to withholding without treaty relief. This guidance was largely identical to similar guidance issued 10 years prior.

f. IRS Treaty and Transfer Pricing Operations ("TTPO") Guidance on APAs

The IRS released a memorandum dated April 25, 2023 indicating that it will now apply more defined review procedures to companies requesting APAs. The IRS's stated goal is to improve the APA process through earlier identification of potential obstacles and alternative tools for certainty, without limiting the number of APA submissions that the IRS's Advance Pricing and Mutual Agreement Program accepts. The guidance sets forth detailed steps for the IRS's TTPO employees regarding the IRS's review of APA prefiling memoranda and APA requests from taxpayers. The IRS indicated that it issued this memorandum to ensure that taxpayer and IRS resources are used as effectively as possible.

Following its review of the APA prefiling memoranda and numerous factors, the IRS will recommend that the taxpayer submit an APA request, provide additional information, or consider a different workstream (e.g., International Compliance Assurance Program ("ICAP")). If a taxpayer then files an APA request, the IRS will review it to decide whether the APA workstream is most appropriate to achieve certainty for the proposed covered transactions, taking into account various factors. Within eight weeks of submitting the APA request, the IRS will either accept the APA request or reject the APA request and recommend an alternative workstream. If the IRS believes that a joint audit might be a better option, it will inform the taxpayer and discuss timing and administrative issues relating to the joint audit process. The IRS has indicated that it will not force a company to pursue one of the alternative workstreams (e.g., joint audit, ICAP).

VI. TREATY DEVELOPMENTS

a. United States-Hungary Treaty

Effective January 8, 2023, the United States terminated its income tax treaty with Hungary in light of Hungary's decision to block the European Union's implementation of the 15 percent global minimum tax. For taxes withheld at source, the treaty will cease to have effect on January 1, 2024. For all other taxes, the treaty will cease to have effect for tax periods beginning on or after January 1, 2024.

b. United States-Chile Treaty

On June 23, 2023, the U.S. Senate approved the proposed income tax treaty with Chile, and it will enter into force once each country has notified the other of the completion of its ratification procedures. President Biden must sign the ratification instruments to complete the approval and ratification process

in the United States. The treaty is consistent with the 2006 U.S. model tax treaty and is the first treaty between the two countries.

VII. OECD PILLARS I AND II

Although U.S. Treasury Secretary Janet Yellen announced that the United States has signed on to the OECD Inclusive Framework's "Statement on a Two-Pillar Solution to Address the Tax Challenges Arising from the Digitalisation of the Economy" ("IF Statement") dated Oct. 8, 2021, the U.S. Congress has not passed legislation to enact the provisions of the IF Statement. After the 2022 mid-term elections created a partisan divide in the Congress, it seems highly unlikely that such legislation would be proposed prior to 2025.

On May 25, 2023, Republican members of the U.S. House Ways & Means Committee introduced the "Defending American Jobs and Investment Act" to guard against perceived adverse effects of the IF Statement. The bill would require the U.S. Treasury to identify extraterritorial taxes and discriminatory taxes imposed by foreign countries on U.S. businesses (e.g., such as the UTPR, formerly known as the "undertaxed payments rule") and would increase the tax rates on U.S. income of wealthy investors and corporations in those foreign countries by 5 percentage points each year for four years, with the elevated tax rates continuing thereafter as long as the "offending" foreign taxes are in effect.