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flash Alert

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United States – New Rules Remove Foreign Tax Credit Restriction for Cuba
by KPMG LLP's Washington National Tax practice, Washington, D.C. (KPMG LLP in the United States is a KPMG International member firm)

The U.S. Internal Revenue Service (IRS) will allow U.S. taxpayers to claim a foreign tax credit for foreign income taxes paid to Cuba as of December 21, 2015. According to an advanced version of Revenue Ruling 2016-8, released by the IRS on March 1, 2016, Cuba is no longer a country to which Internal Revenue Code (I.R.C.) section 901(j)(2) applies.¹

Why This Matters

Cuba is no longer considered a country subject to certain restrictions imposed by I.R.C. section 901(j) that denies U.S. taxpayers from claiming a foreign tax credit for foreign taxes paid to Cuba. U.S. taxpayers can claim a foreign tax credit for foreign income taxes paid to Cuba, with retroactive effect as of December 21, 2015.

Background

In general, I.R.C. section 901 permits U.S. taxpayers to claim a credit for income, war profits, and excess profits taxes paid or accrued during the tax year to any foreign country or to any possession of the United States.² However, U.S. taxpayers are restricted from claiming the benefits provided under section 901 for certain countries. Section 901(j)(1)(A) disallows a foreign tax credit for taxes paid or accrued to certain countries if the taxes relate to income attributable to a period during which the country is a restricted country as described in section 901(j)(2).

Section 901(j) generally applies to countries with which the U.S. does not have diplomatic relations, or which the Secretary of State has designated as a country that provides support for international terrorism. Revenue Ruling 2005-3 lists the countries which are described in section 901(j)(2) and specifies the periods to which the restrictions apply for each country.³ Restricted countries under existing rules include Iran and North Korea. Cuba was listed as a specified country to which the restrictions under 901(j) applied effective as of January 1, 1987.

Revenue Ruling 2016-8

With the release of Revenue Ruling 2016-8, the Secretary of State has certified to the Treasury Secretary that Cuba is no longer a country to which section 901(j)(2) applies. Further, Revenue Ruling 2016-8 modifies the effective date for Cuba with respect to the restrictions imposed by section 901(j). The Revenue Ruling provides that the restrictions under section 901(j) no longer apply to Cuba as of December 21, 2015.

KPMG Note

Revenue Ruling 2005-3 also imposes restrictions on qualified individuals from claiming the foreign earned income and housing cost exclusions under section 911(a).

Revenue Ruling 2016-8 does not modify the restrictions imposed on specified countries as it relates to claiming the foreign earned income and housing cost exclusions. Thus, foreign earned income continues to not include income from sources within Cuba and housing costs do not include housing expenses incurred in Cuba. Further, for purposes of claiming the foreign earned income and foreign housing cost exclusions, individuals will not be treated as a bona fide resident of or present in a foreign country during days spent in Cuba.

Footnotes:

- 1 See Rev. Rul. 2016-8 at <https://www.irs.gov/pub/irs-drop/rr-16-08.pdf>. Rev. Rul. 2016-8 will be published in the *Internal Revenue Bulletin* no. 2016-11, dated March 14, 2016.
- 2 I.R.C. § 901(b)(1).
- 3 Rev. Rul. 2005-3, 2005-1 C.B. 334.

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The above information is not intended to be "written advice concerning one or more Federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230 as the content of this document is issued for general informational purposes only.

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