TaxNewsFlash

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Notice 2019-65: Regulations under section 987, additional deferral of effective date

The IRS today released an advance version of Notice 2019-65 announcing that the U.S. Treasury Department and IRS intend to amend the regulations under section 987 (concerning foreign currency gain or loss) to defer the applicability date of the final regulations under section 987 by one additional year.

Read **Notice 2019-65** [PDF 50 KB]

Background

In December 2016, Treasury and the IRS released three sets of regulations—final, temporary, and proposed regulations—concerning the taxable income or loss of a taxpayer with respect to a "qualified business unit" (QBU) subject to section 987 (the "2016 Regulations").

In July 2017, the IRS issued Notice 2017-38, which identified the 2016 Regulations as "significant tax regulations" requiring additional review pursuant to Executive Order 13789. As part of that review, today's notice states that Treasury and the IRS are considering changes to the final regulations that would allow taxpayers to elect to apply alternative rules for transitioning to the final regulations and alternative rules for determining section 987 gain or loss.

Subsequently, Notice 2018-57 provided that the 2016 Regulations and related temporary regulations will apply to tax years beginning on or after the date that is three years after the first day of the first tax year following December 7, 2016. Read ***TaxNewsFlash***

In May 2019, Treasury and the IRS finalized certain temporary regulations concerning combinations and separations of qualified business units (QBUs) and the recognition and deferral of foreign currency gain or loss in connection with certain QBU terminations and other transactions ("2019 Final Regulations"). Read ***TaxNewsFlash***

The 2019 Final Regulations dealing with QBU combinations and separations are applicable to tax years beginning on or after the day that is three years after the first day of the first tax year following

December 7, 2017. The deferral event and outbound loss rules contained in Reg. §1.987-12 are generally applicable to any deferral or outbound loss transaction occurring on or after January 6, 2017.

Notice 2019-65

Today's IRS notice further defers the applicability date of the 2016 Regulations (and certain related and temporary regulations) as well as certain of the 2019 Final Regulations by an additional year.

According to Notice 2019-65, the amended applicability date is the first day of the first tax year following December 7, 2020. Thus, after the amendments are made, for a calendar year taxpayer whose first tax year after December 7, 2020, begins on January 1, 2021, the 2016 Regulations would apply for the tax year beginning on January 1, 2021. The amended applicability date also applies to the 2019 Final Regulations dealing with QBU combinations and separations, but does not affect the applicability date of the 2019 Final Regulations dealing with outbound loss and deferral events, which continue to apply to such transactions occurring on or after January 6, 2017.

The related temporary regulations (which expire on December 6, 2019) will not become applicable. After the related temporary regulations expire, the amended applicability date will apply for purposes of the related proposed regulations.

Notice 2019-65 states that a taxpayer may choose to apply the 2016 Regulations, related temporary (if applicable) or proposed regulations, and the 2019 Final Regulations relating to QBU combinations and separations to a tax year beginning after December 7, 2016, and before the amended applicability date, provided that the taxpayer consistently applies those regulations to such tax years with respect to all section 987 QBUs directly or indirectly owned by the taxpayer on the transition date as well as all section 987 QBUs directly or indirectly owned on the transition date by members that file a consolidated return with the taxpayer or by any controlled foreign corporation (CFC) as defined in section 957, in which a member owns more than 50% of the voting power or stock value.

KPMG observation

What are taxpayers to do now? In the absence of an effective set of regulations, taxpayers have a great deal of flexibility in calculating the section 987 gain or loss attributable to their section 987 QBUs, provided the method used is reasonable and clearly reflects income.

Because section 987 gain or loss will affect the tested income of a CFC that holds a section 987 QBU, it is important that taxpayers apply a reasonable method now—taxpayers should not wait to adopt a method until either the final 2016 Regulations become effective or new regulations are released and finalized. KPMG professionals can help evaluate the available options and assess the impact of such options on existing or proposed structures.

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